# Assessing India's Economic Landscape: Growth Prospects Amid Challenges

**Abhijit Mukhopadhyay,**
Consulting Economist, The Secretariat

## Tackling Poverty, Geopolitical Shifts and Innovation to Bridge Divides and Sustain Stability

**Intro:** Amidst the ebb and flow of global economic tides, India stands at a crossroads, poised for transformation. In an exclusive interview, at **Socio-economic Voices** this week, we have **Abhijit Mukhopadhyay Consulting Economist, The Secretariat** delving into the heart of India's economic narrative, dissecting the intricate web of challenges and opportunities. From grappling with poverty to navigating geopolitical complexities and embracing innovation, join Indiastat on a journey through the corridors of India's economic resilience and growth. An exclusive interaction with senior journalist **Mahima Sharma.** Read on for more details...

**MS: India set for strong growth, macro-stability in FY24 | Mint But what about our microeconomic level, poverty level issues? What policies are needed on priority basis and how must their implementation happen in a limited time to bridge the class divide?**

**AM:** Defining poverty within official policymaking has hit a roadblock for decades now. Most often cited (but not official) the Tendulkar Committee prescribed and measured poverty based on income criteria for 2004-05, but that was two decades back. The poverty line defined then was Rs. 446.68 per capita per month for rural areas and Rs. 578.80 for urban areas.

**Adopting the Tendulkar methodology, the poverty lines for 2011-12 were estimated at Rs. 816 and Rs. 1,000 per capita per month. A recent SBI Report estimated 2022-23 poverty ratios after updating the poverty lines – Rs. 1,622 for rural and Rs. 1,929 for urban. The report estimated that rural poverty declined from 25.7% in 2011-12 to 7.2% in 2022-23 while urban poverty decreased from 13.7% to 4.6% in the same period.**

However, there is not yet any official recognition of any definition of poverty lines. The stalemate continues.

Since India does not have any national-level income survey, all the estimates are based on the Household Consumption Expenditure Survey (HCES). Internationally, the World Bank definition of extreme poverty puts the line at $1.90 per day, which amounts to around Rs. 150 in purchasing power parity terms. As can be seen, our poverty lines are way below this.

There have also been talks about including non-income criteria to measure poverty. But nothing concrete came out of it till now.

An array of redistributive social welfare programmes are undertaken by the central and various state governments. These schemes are utilised to provide foodgrain, gas cylinders, piped water connections, among others. Given the current situation, the best policy response at this point of time may be to **widen the social safety net by including more people (who are in need)** in these schemes.

**MS: Coming back to the key challenges facing macroeconomic stability. What's your take towards the same owing to climatic and geopolitical changes across the globe? And how must the government address them effectively in the next decade?**

**AM:** Current geopolitical situations definitely pose challenges to policymakers. The Russia-Ukraine war created supply chain bottlenecks initially, but after a while it provided economic benefits also for the Indian economy, particularly in terms of oil and gas exports. However, the fluid situation on ground can spring surprises any time.

**For example, if embargo against Russian exports in the EU eases down in future the pattern of Russian oil and gas exports once again may go back towards the Euro zone.**

**Trouble in the Middle-East is already hurting the movement and logistics of international trade. India is also affected, as freight costs are going up. Any flare-up can push international energy and commodity prices.**

**India's industry, particularly manufacturing, needs raw material and capital goods imports. Any disruption can hurt future economic growth.**

However, these are external factors (or supply shocks) beyond the control of the Indian government. If disruption happens, then at the most the government can make efforts to avail crucial imports needed for the economy's growth from other possible sources. But if international prices go up, beyond a limit no government can do much.

Climate change, on the other hand, poses a systemic challenge to the Indian economy. The way things are moving, a time will come when different products and services may get blocked in different countries if they are not compliant with requisite climate and environmental norms.

For example, the European Union is already in the process of adopting Carbon Border Adjustment Mechanism (CBAM) – apparently to put a fair price on the carbon emitted during the production of carbon-intensive goods. It started with heavy emitting sectors like steel, cement, fertilisers and electricity generation. But the future plan is to expand the scope of CBAM in other sectors.

**In simple words, EU imports in these sectors in future would be determined by the amount of carbon emission during production.** In the name of putting a fair price, these products from other countries may get costlier. For example, Indian steel prices may go up and become non-competitive in the Eurozone markets, as a result.

The Government of India needs to closely monitor these climate-related developments in major export and import markets. Only then solutions can be found in future.

**MS: In the next 5 years what do you foresee as the potential implications of geopolitical tensions on India's economy? And how should policymakers respond/what should be the policy change and which all sectors?**

**AM:** As mentioned earlier, geopolitical tensions can jeopardise the supply chain of aspiring Indian manufacturing. A future roadmap towards self-sufficiency has become imperative undoubtedly. The Government of India is also aware of this. The emphasis on an "Atma Nirbhar Bharat" is a proof of that.

**Endeavours like Make In India and Atmanirbhar Bharat are meant to increase the manufacturing share in GDP. That is, however, not happening. Share of manufacturing in GVA (gross value added) in India fell from 16% in 2015 to 13% in 2022, according to World Bank data.**

Major economies of the world are also looking inward and creating barriers to trade. In fact, the sharp decline in multilateralism, since the 2018 US-China trade war, is making exports difficult for all emerging economies, including India. Recent geopolitical tensions are adding to that.

In this kind of a situation, policy measures aiming to boost exports may not yield the desired effect in the final result. **The Indian government is trying its best and providing incentives to produce and export more. However, the data show that all these are not translating into the desired outcome of increasing exports. In 2023-24, India's merchandise exports shrank over 3%.**

While the focus of recent schemes like PLI (production linked incentives) has been on high-end and high-tech sectors like semiconductor chips and drones, the labour-intensive export sectors such as textiles and leathers have fallen out of the radar. In terms of employment generation, these sectors need to be incentivised. Otherwise, India may keep on losing potential export markets to countries like Vietnam, Indonesia and Bangladesh.

**MS: What immediate steps does India need to take to balance the need for fiscal stimulus with long-term fiscal sustainability, especially in light of recent global economic disruptions?**

**AM:** To put it simply, it does not look like that the government is any more interested in providing any fiscal stimulus. On the contrary, going by the last two years' budget speech, fiscal consolidation is the priority.

In other words, the government wants to adhere to the long-term fiscal deficit numbers. This means more emphasis will be on rationalising expenditures.

**MS: Which CORE THREE reforms in your vision and experience are necessary to improve India's business environment and attract more foreign investment?**

**AM:** Increasing ease of doing business would be the first. Any individual or company, willing to set up an establishment in India, has to go through a plethora of paperworks. This wastes a lot of time while starting a business.

Even after starting, there are long-drawn periodic submissions on account of taxes, licenses and other formalities. All these take time, and time is indeed money in any business.

**Attracting foreign investment** may result in removing capital control, at least partially. So, a reform of the capital account of the Indian balance of payments may also be on the cards.

**Labour reform** is also another agenda that has been periodically pushed further away.

However, implementing these three reforms is easier said than done. **The bureaucratic red tape refuses to completely disappear from the Indian economy. Capital control is also one contentious issue, and so is labour reform.**

There will be resistance against all of these from different and diverse quarters. It would be interesting to see how the new government tackles these issues.

**MS: The consumers' economy of India: What do the recent macro numbers tell us? And what reforms are needed, especially when it is being driven by over-the-top, and even misleading strategies?**

**AM:** As GST collections keep on hitting new highs, it might seem at the outset that consumption in the economy is going up. In the month of April 2024, GST collections hit a record Rs 2.10 lakh crore.

**However, the macro GDP data confirms a slowdown in the growth of private final consumption expenditure (PFCE). It has been declining in the last couple of years. The growth in PFCE in 2023-24 was the slowest in two decades, barring the pandemic year of 2020-21.**

This may seem a bit contradictory, but it is not. The economically better-off sections are splurging on high-end goods and services that attract higher GST rates, thus keeping indirect tax collections buoyant even as overall consumption demand in the economy remains subdued.

**This is something that has linkages with the growing inequality across the income distribution.**

The solution lies not in any reform, but in strengthening existing direct income transfers schemes, including MGNREGA. Unless the bottom half of the population gets money in their hands to spend, the overall consumption figures in the economy will always be under some cloud.

Though the top layer of the population, for the time being, is somehow compensating with their splurging on high-end goods and services, it would slow down at some point of time.

Revival of consumption requires disposable income in the hands of the population.

**MS: In your experience, which key sectors of Indian macro-economy must fast leverage tech-advancements and innovations to drive economic growth? Here please add, how can India enhance global competitiveness without losing manpower to AI-driven work models?**

**AM:** Apart from the information technology and software sector, there are a few more high-end high-tech sectors, where India aspires to be a bigger player. Electronics, aviation (particularly, drones), medical devices, and high-end telecom manufacturing are some of those.

In the start-up arena, there are futuristic companies in sectors like robotics. A policy orientation towards making India a semiconductor chip hub is quite visible. This is another area where India aspires to be a larger player.

**Getting into high-end products astronomically increases the profit margins of the companies involved.** Therefore, bigger companies always aspire to get into high-tech space. However, the future success of all these mentioned sectors will be dependent on government policy support in the initial days.

For example, the IT sector benefited hugely from initial policy support from the government, like prolonged and extended tax holidays.

Artificial intelligence (AI) is going to affect all high-tech sectors. The impact has already started in the software and IT sectors, as can be seen from the media reports of lay-offs across all major companies.

Unfortunately, losing manpower to different AI-driven work models is likely to be an eventuality that cannot be avoided. When any globally technology-driven sector starts adopting AI, the immediate impact will be on the profit margins. So, other companies will follow suit to survive in that particular sector.

**Measures like re-training and upgrading skills of the existing workforce can be one way to mitigate this impact. However, when machines take over job loss cannot be avoided. For a hugely populous country like India, AI indeed poses a gigantic challenge, as far as employment creation is concerned.**

Putting the policy focus back on labour-intensive sectors like textiles and leather can be one way of cushioning adverse impacts from high-tech sectors. However, a deep policy introspection is needed in a country like India about how much AI can be adopted in what sectors.

**MS: Amid what has happened in the neighbouring nations and their sunk economies, how can India effectively manage its external debt and trade deficits to safeguard economic stability?**

**AM:** At this point of time, the Indian economy does not face any immediate risk related to external debt and trade deficit. That is due to the adequate amount of foreign exchange reserves that the country holds at present.

However, there are of course long-term challenges. Foreign direct investment (FDI) inflow is one of these. As global trade decelerates, the component of exports is bound to be subdued in all major economies. And India is no exception.

For the Indian economy, the saga of shrinking trade deficit, as a result of a larger drop in imports compared to exports, continues. Notably, rapidly falling imports are not a good sign for an aspiring economy.

FDI inflows could have offered some cushion, but these have been declining too. In 2018-19 and more recently in 2022-23, lower FDI inflows and subsequent lower capital account surplus could not offset the current account deficit, resulting in the depletion of foreign exchange reserves. Deficit in goods (merchandise) trade in India is usually compensated by the surpluses in services trade and capital account.

**Recent trends point towards the risk of running these two buffers (services trade and capital account surpluses) thin on the margin,** in case of an exports deceleration. Given the current geopolitical tensions in the Middle-East, exports dwindling further is a real possibility. There are other factors, such as lack of global demand for IT services that may adversely impact the services exports as well.

If that happens, then a goods trade deficit may translate into an overall balance of payments deficit, dwindling foreign exchange reserves, and a further weakening of the rupee. That would mean any Indian citizen spending money on any international transactions, like trade, education, tourism, or health, would have to pay more.

So, **ensuring a renewed acceleration in FDI inflow looks like an immediate task,** if the external balance of payments situation has to be made stable.

**MS: What measures should the government take to enhance the resilience of India's financial sector and prevent systemic risks?**

**AM:** As mentioned earlier, there is a probability of easing capital control in the near future. The immediate objective of such a move would be to attract more FDI into the economy. But in a way, it is a shortcut policy measure. Long-term changes like making it easier to do business in India would be far better ways to do that.

Removing capital control essentially means that money coming from outside can easily go out also, if such a time comes. Here it is important to note that sizable and steady inflow of FII (foreign institutional investment) into stock markets has also been a reality for the Indian economy for a long time.

**Once any panic creeps into stock or any other financial market, the FIIs are the flows that get out of the country first. That is why FII inflows are often called "hot money." Add to this the amount of equity investment that comes under the FDI route. In simple words, under the category of FDI foreign investment often arrives in India to buy equities of existing companies.**

Under a more liberalised capital control regime, even these FDIs will find it easier to leave the Indian economy immediately if there is any business shock to the market.

India successfully insulated itself from any major setback during the 2008 financial crisis and earlier international shocks. One of the main reasons was its existing capital control. So, it will be wiser to get into details before hastily removing capital controls.

As more global money flows into the financial markets of India and more domestic investors start participating in financial markets, particularly the stock market, there is an urgent need to regulate and supervise these spaces.

Enabling and further empowering all financial regulators, including the RBI and SEBI, would be imperative to ensure the resilience of Indian financial markets and to prevent systemic risks.

***About Abhijit Mukhopadhyay***

*Abhijit is the Consulting Economist, The Secretariat and has more than 21 years of experience in economic analysis and policy research, academic study, project report writing and business school teaching. His core areas of expertise include economic, monetary, banking, financial and trade policy, sustainability and development research. He consistently contributes articles in national and international academic journals and various media platforms on macroeconomic management, government impact and public policy related issues. He has also participated and presented research papers in international and national conferences, seminars and workshops.*

**About the Interviewer**

*Mahima Sharma is an Independent Journalist based in Delhi NCR. She has been in the field of TV, Print & Online Journalism since 2005 and previously an additional three years in allied media. In her span of work she has been associated with CNN-News18, ANI - Asian News International (A collaboration with Reuters), Voice of India, Hindustan Times and various other top media brands of their times. In recent times, she has diversified her work as a Digital Media Marketing Consultant & Content Strategist as well. Starting March 2021, she is also a pan-India Entrepreneurship Education Mentor at Women Will - An Entrepreneurship Program by Google in Collaboration with SHEROES. Mahima can be reached at media@indiastat.com*

***Disclaimer :*** The opinions expressed within this interview are the personal opinions of the interviewee. The facts and opinions appearing in the answers do not reflect the views of Indiastat or the interviewer. Indiastat does not hold any responsibility or liability for the same.