Addressing Demand Drought in Indian Economy

What is the issue?

- Indian Economy is evidently witnessing a slowdown phase, with weak consumption demand being a factor.
- In this context, here is an overview of the causes for it and the ways to address it.

What is the present economic scenario?

- A worryingly persistent slowdown dragged the economic growth in India down to 5% in the first quarter of 2019-20.
- This is the weakest pace of the economy in more than 6 years.
- Private consumption expenditure has decelerated so sharply that at 3.1%, the expansion is at an 18-quarter low.
- Notably, private consumption expenditure contributes more than half the GDP and is the mainstay of demand.
- Automobile sales continued to plunge in August 2019.
- It posted the worst drop since the Society of Indian Automobile Manufacturers (SIAM) started collating wholesale vehicle sales data in 1997-98.
- The absence of demand pervades almost every key sector - from consumer durables to biscuits and housing.

What contributed to the demand drought?

- Multiple factors have contributed to the demand drought:

i. lack of jobs, or even where jobs are available, a limitation about the incomes from such work
ii. the long-lasting rural distress
iii. widening inequality
iv. even the RBI's successful targeting of inflation

- **Inflation** - It is said that the RBI's remit of containing consumer price index (CPI) based inflation within a 2-6% band may be proving less than ideal for India.
- This is especially the case if monetary policy makers are focused at pegging inflation at or less than 4% (even it means retarding growth as a fallout).

- Low inflation extracts costs in the form of lower nominal growth (growth measured in current prices).
- This could crimp tax receipts and in turn lead to cuts in government spending.
- Also, with wage/salary increases most often linked to inflation, slower price gains would result in smaller annual increments.
- This would further leave the earners more wary of spending on discretionary or non-essential purchases.
- **Rural demand** - The crisis of demand in the rural hinterland has worsened to the point where sellers of consumer goods have seen appreciable slowing in sales growth in recent quarters.
- Weak growth in rural income and moderation in rural infrastructure spending would lead to de-growth in tractor sales volume by 5-7% in 2019-20 fiscal.

What is the need now?

- **Consumer sentiment** is a key ingredient affecting consumption.
- It is vital for policy makers to address weakness in consumer sentiment through a mix of measures in the economic realm.
- Both monetary and fiscal measures are needed, as well as ensuring a congenial socio-political climate to enhance the 'feel-good' factor is essential.
- **On the monetary side**, ensuring lower borrowing costs as well as adequate availability of credit is crucial.
- This would create an enabling environment for consumers to consider taking out loans to fund their purchases.
- **On the fiscal side**, targeted tax breaks or non-tax sops that incentivise consumption is one option.
- The latest decision to cut baseline corporate tax rates is certainly a good move, aimed at incentivising and boosting capital investment.
- However, companies may be uncertain of investing when demand for their manufactured goods is still weak.
- It is therefore imperative that the revival of demand remains a key priority of any new policy measure.
- As far as **rural demand** is concerned, the government must go beyond the PM-KISAN income supplementing scheme.
- It should tackle the crisis of low real farm incomes by radically recalibrating its approach to the agrarian economy.
- As an immediate and necessary measure, the Mahatma Gandhi National Rural Employment Guarantee Scheme needs to be reinvigorated.
- Ensuring timely and adequate funding and the fixing of appropriate wage levels are essential.

What are the challenges?

- Any economic stimulus package that the government may come up with would necessarily assume a short-term loosening of the fiscal deficit goals.
- If the stimulus also entails a large expenditure component, there could also be second-order inflationary consequences.
- However, the necessity to revive demand at a juncture when the economy is heading for a stall is high now.

Source: The Hindu

