Boosting Economic Growth

What is the issue?

- There is significant selling of Indian equities by foreign portfolio investors (FPI) in recent days.
- Concerted measures are needed to boost the economy and growth rate in India.

What are the recent developments?

- In July, 2019, the FPI selling has touched almost $2.5 billion, and now, seems to be accelerating.
- Consequently, India has had a very tough year on a relative basis.
- While the markets globally are hitting new highs, India is struggling to stay in positive territory.
- In a ranking of the top 50 equity markets, in terms of performance year-to-date, India is ranked 43rd.
- In all, the country is doing poorly and the Indian markets are struggling, despite its favourable economic backdrop.

What are the positive factors at play?

- The government that investors wanted has come back with a much stronger-than-forecast mandate.
- Oil prices are stable, and seem to be in a safe range; the top end of the range does not seem to be a level that will disrupt the economy.
- The rupee is very stable; it has, in fact, appreciated post the Lok Sabha election.
- Globally, liquidity is very easy and rates are declining everywhere.
- Moreover, India is on the verge of starting another round of central bank easing, led by the US Federal Reserve and the European Central Bank.
- Undoubtedly, India will be the fastest-growing major economy over the coming decades and definitely grow faster than China.
- However, the current growth pace is less encouraging, given India's favourable position.

What are the possible reasons?

- **Lack of corporate earnings growth** - This has been the single-biggest

disappointment in Indian equities over the last 8 years.

- Back in 2008, the share of corporate profits/GDP in India and the US was basically the same at about 7%.
- Today, these ratios are near 10% in the US and just over 2% in India.
- There has been a total collapse in corporate profitability in India over these years.
- The reasons for this include corporate bank NPA clean up, higher taxes, technological disruption, economic shocks, inadequate private investment, an overvalued rupee, etc.
- This aside, worryingly, the fact remains that no one has been able to forecast the turn in corporate profitability.
- No one can explain when and why earnings will accelerate, beyond the obvious point that corporate profits cannot keep dropping as a share of GDP.
- It is hard for the markets to resume a sustained uptrend in the absence of strong earnings growth.
- **Weak economy** - Economic sentiment in India is very poor at the moment, among both domestic investors and industrialists.
- This negativity is now affecting the global investor base.
- The weak corporate sentiment witnessed in the country is more pronounced than in recent years.
- Investors and companies just talk of deleveraging and hoarding liquidity, and there is no interest in setting up new capacity.
- Demand scenario is less encouraging and the Non-banking financial companies (NBFCs) are only in a survival mode after the recent defaults.
- Many businesses have no access to credit.
- Business confidence gets even more shaken when states, like Andhra Pradesh, attempt to renegotiate signed contracts.
- **Tax** - It is undeniable that the country needs to spend as much as possible in improving the basic quality of life of the average Indian.
- However, the present approach seems to be to focus on the existing narrow tax base to get the required resources.
- There has undoubtedly been huge abuse of the system by Indian industrialists.

What is the way forward?

- **Economy** - The government to its credit has tried to lower rates in the economy, and thus boost consumption and investment.
- This will help, but in addition to easing monetary policy, investors would be benefitted more by the next generation reforms in land, labour and judiciary.
- This would go a long way in making India an easier place to do business.
- Going forward, there has to be a better articulation of the government's

economic philosophy, priorities and game-plan for the next 5 years.

- **Tax** - Given the need for resources in rural India, India cannot afford to give bailouts of lakhs of crores to PSUs, be it the banks, Air India or BSNL/MTNL.
- Finding ways to broaden the tax base and being far more active in monetising government assets to get the money needed are essential.

Source: Business Standard

