India's GDP Controversy

Why in News?

Recently, an allegation has been made on the government that it is overstating its GDP growth rate after the release of quarterly data of GDP value.

What is GDP?

- Gross Domestic Product (GDP) is defined as *total market value of all final goods and services* in an economy.
- It is used to assess the size of economy.
- The performance of the country can be measured both from one year to another as well as among other countries.
- **Growth of GDP –** It can be either due to increase in actual production or due to increase in prices of goods and services or combination of both the above two factors.
- **Nominal GDP** – It is the value of *GDP at the current prevailing prices*.
- **Real GDP** – It is the value of *GDP at some constant set of prices.*
- It is calculated by removing the effects of price inflation from the nominal GDP using *GDP or price deflator*.

Real GDP growth rate = Nominal rate – Inflation (GDP Deflator)

- Since these prices remain fixed, if the real GDP changes, it is ascertained that the volume of production is undergoing changes.
- **The GDP deflator** – It is the ratio of nominal to real GDP.
- It gives us an idea of how the prices have moved from the base year (the year whose prices are being used to calculate the real GDP) to the current year.

GDP Deflator = Nominal GDP / Real GDP

How is GDP calculated?

- Generally, GDP is calculated by *3 different methods* –
  - Income method
  - Expenditure method
  - Production method
- In India, it is calculated through income and expenditure method.
- The ***National Statistical Office (NSO)*** under the *Ministry of Statistics and Programme Implementation (MoSPI)* releases the economic growth data.
- The base year for GDP calculation is ***2011-12.***

Why is India's GDP facing controversy?

- **Issue of overstating GDP** – The released GDP growth rate is 7.8% which implies that inflation was around 0.2% in the three months.
- But in the said quarter, retail inflation was around 4% in all 3 months, while wholesale inflation was negative.
- If one was to "deflate" nominal GDP using consumer price inflation, the real GDP would fall to less than 4%.
- But then if one goes by wholesale inflation, the real GDP will actually be much higher than 8%.
- **Issue of GDP discrepancy** – The GDP data obtained from the two methods vary due to issues such as lack of availability of data on time, etc.
- The difference between the GDP estimates from production method and income method is called "*discrepancy*".



- The NSO in its latest report treats income as the right one and assumes that expenditure *must be identical* to income earned which is an obvious violation of international best practice.
- **Issue with WPI** – In recent times WPI (Wholesale Price Index) and CPI (Consumer Price Index) are not moving together suggesting that one of the indices is not reflecting the real price.
- It is *unrepresentative of economy* as it does not include services whose share in consumption basket is large and increasing.
- Calculation of WPI by Department of Commerce and Industry is based on *Index of Industrial Production (IIP)* which itself is in criticism.
- It does *not provide information on rural and urban* as well as the state level estimates, which are all relevant for public policy.

What lies ahead?

- More attention has to be given to India's macroeconomic data.
- India's inflation indices need to be updated periodically.
- Wholesale price index (WPI) must be discarded and has to be altered with a new *Producer Price Index* which is a measure of the change in prices that domestic producers receive for their goods and services.

Quick facts

	Wholesale Price Index	Consumer Price Index
Definition	• A WPI measures and tracks the changes in the price of goods before they reach consumers. • WPI tracks inflation at the producer level.	• The CPI examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food, and medical care. • CPI captures changes in prices levels at the consumer level.

Components/ Types	• Manufactured products - 64.2% • Primary articles - 22.6% • Fuel and power - 13.1%	• CPI for Industrial Workers (IW) • CPI for Agricultural Labourer (AL) • CPI for Rural Labourer (RL) • CPI (Rural/Urban/ Combined)
Base Year	• 2011-12	2012
Published By	• Office of Economic Adviser, Ministry of Commerce and Industry	• CPI –IW, AL and RL are compiled by the Labour Bureau, Ministry of Labour and Employment. • The National Statistical Office (NSO) releases the CPI-Rural, Urban, and Combined.
Services	• WPI does not capture changes in the prices of services	• CPI capture changes in the prices of services
Uses	• It is a marker for price movements in the purchase of bulk inputs by traders.	• The dearness allowance of Central government employees is calculated on the basis of movement in this index. • Inflation rate will be based on the final combined CPI.

Index of Industrial Production (IIP)

- It is a composite indicator measuring changes in the volume of production of a basket of industrial products over a period of time.
- It measures the growth rate of industry groups classified under,
  - **Broad sectors** - Mining, Manufacturing and Electricity
  - **Use-based sectors -** Basic Goods, Capital Goods and Intermediate Goods
- **Base year** - *2011-12*
- It is compiled and published on a *monthly basis* by the ***CSO (now known as National Statistics Office (NSO))*** with a time lag of 6 weeks from the reference month.

References

1. IE| GDP Controversy
2. NCERT | Concepts of GDP

SHANKAR IAS PARLIAMENT
Information is Empowering