LEXFORTI LEGAL JOURNAL | [ISSN: 2582 2942]
VOLUME I -ISSUE IV

Slowdown and the Indian Economy

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ABSTRACT

India's developmental strategies since independence have focused on achieving rapid economic growth while diversifying productive structure. The Indian economy was primarily an agricultural economy with a semi-feudal structure. The basic objective was to change this structure of the economy through rapid industrialization. However, in the early 1990s, our economy plunges into the arena of globalization and became a developing economy. Nevertheless, due to the recent economic slowdown, many manufacturers are suffering a sharp downturn in sales resulting in foreign investors pulling their money out of the Indian stock market leading to high volatility. Since the economic slowdown, all growth indicators are pointing to the fact that growth expectations may not be met. Many economists have acclaimed that there will be a liquidity trap in the economy for an indefinite period unless there is a shift on the new developmental policy agenda.

Keywords: *Economic slowdown, liquidity trap, India*

INTRODUCTION

India was a very independent economy before the British rule, towards the end it was exhausted. Our economy had been a victim of anomalous exploitation. Natural resources, wealth, and manpower were subject to intense exploitation. Due to these atrocities, the Indian economy at the eve of independence shows poor/low economic growth. It is a known fact that over 70% of India's national income comes from its agricultural activities. Back then, before 1947 it was 95% of the country's income. The agricultural sector was prone to low productivity and high vulnerability. There was a de-industrialization in India during the British period, the decay of handicraft industries followed by the slow growth of modern industry and limited growth of PSEs lopsided industrial structure. Post-independence, Jawaharlal Nehru enacted an economic policy based on import substitution industrialization (ISI). The Nehru-Mahalanobis Approach, often referred to as the second five-year plan emphasized the development of bases and heavy industries as a means of accelerating economic growth. The industrial policy resolution of 1948 proposed a mixed economy. Earlier the Bombay plan, proposed by eight influential industry lists including JRD Tata and GD Birla, envisaged a substantial Public sector with state interventions and regulations in order to protect indigenous industries.

India suspended the five-year plan briefly, drawing up annual plans between 1966 and 1969 instead. The 1960s was a decade of multiple economical and political challenges for India but in the year 1991, the new economic policy re-introduced a measure of stability to the economy and allowed the Soviet people to recover from years of war, civil war, and governmental mismanagement. The small businessmen and managers who flourished In this period became as NEPmen. Indian economy flourished in the NEP P.V.Narsimha Rao's Government as there was a reduction in import duties, opened reserved sectors for private players, and devalued Indian currency to increase export.

The current Indian economy is characterized as a developing market economy. It is the world's fifth-largest economy by nominal GDP and the third-largest by purchasing power parity. According to IMF, on per capita income base is India ranked 142nd by GDP and 119th by GDP per capita in the financial year 2018. There was a quarterly growth number of 10% at one point around 2008 before the financial meltdown happened but now the

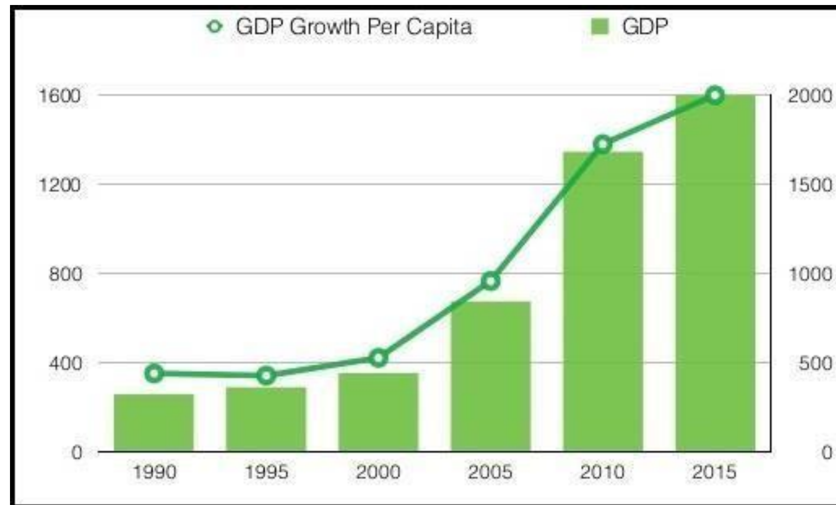
current growth rate in the FY 2019-20 GDP is likely to print 6% in 3Q vs. 2Q's 5% nearing the trough for this cycle. Failing demand blurs the 5 trillion economy dream as the core sectors are bleeding. Despite recent policy reforms, the government has been struggling to counter a multi-sector slowdown. It is a serious concern before it worsens.

Thus, this paper seeks to examine the relevance or otherwise of growth strategy in the context of Indian financial and economic conditions and further examine if the consumption slowdown is making India a victim of the crisis. The sequence of the paper is as follows. Section 2 presents a review of growth strategies and the background to the recent economic slowdown. The actual and potential impact of prices is highlighted in section 3. The policy response to the crisis and the way forward is the focus of section 4 while section 5 summarizes and concludes.

REVIEW OF GROWTH STRATEGIES IN INDIA

The progress of economic reform in India is followed. World Bank suggests that the most important priorities are public sector reforms, infrastructure, agriculture, rural development, and removal of labor regulations followed by reforms in lagging states. The economic development in India is Socialist inspired politician for most of its independent history, including state-ownership of many sectors. Since the mid-1980s, India has slowly opened up its market through economic liberalization. India Changed its economic policy to bring in competition for the Indian producers and barriers to foreign trade and investment were removed. New economic policy 1991 main objective was to give new thrust on market orientation. At the beginning of the mid-1990s, the government has made some radical changes in its policies related to foreign trade, foreign direct investment FDI, exchange rate, industry, fiscal discipline, etc. The trust of new economic policy has been towards creating a more competitive environment in the economy as a means to improve the productivity and efficiency of the system. This was to be achieved by removing the barriers to entry and the restrictions on the growth of forms. India has resorted to importing Substitution which was later reversed during the 1991 currency crisis. The failure of ISI strategy was due to lack of Indian industries' basic sophisticated infrastructure.

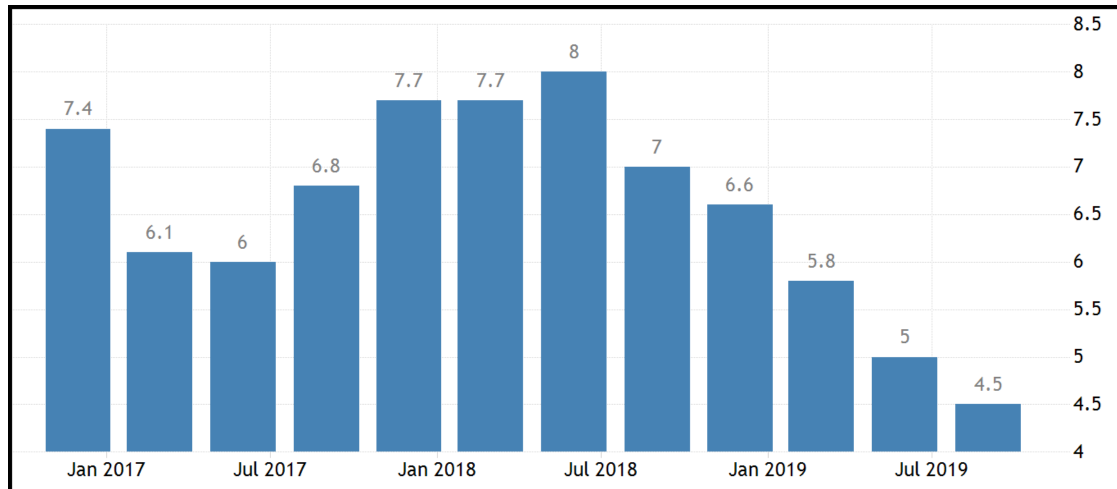
Fig.1: GDP growth rate per capita (1990-2015)



The present growth of the Indian economy has been pretty dominated by consumption inclusive of both private final consumption expenditure is PFCE and government final consumption expenditure GFCE. Private consumption is the main lifeblood, and the driving force of the Indian economy has been visibly slowed down in recent months. The slowdown in the Indian economy is evident now as indicators of the economy's domestic consumption, credit off take, import points towards a slump in the economy. India's GDP growth during the FY of 2015 was 7.5% compared to China, making it the fastest-growing economy.

Although major reforms have been taken place like demonetization and the implementation of goods and service tax in FY 2016-17 the economic growth has been slowed down in 2017-18 as it is expected to grow at 6.7% and four cast to rebound by 8.2% in 2018-19.

Fig 2: GDP rate per capita (2017-2019)



SOURCE: MINISTRY OF STATISTICS AND PROGRAMME IMPLEMENTATION (MOSPI)

In summary, we have to state that frozen credit markets, large loss in financial wealth, shaken investor and consumer, confidence have re-enforced each other to depress aggregate demand. This is the situation of the credit crunch or liquidity trap in the economy.

ECONOMICAL AND FINANCIAL CRISIS AND THE INDIAN ECONOMY

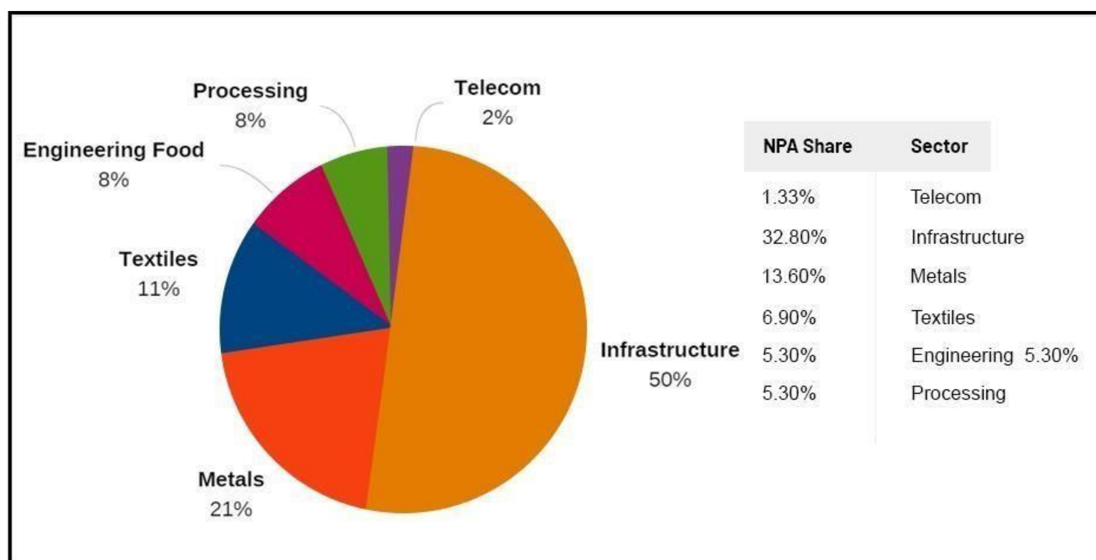
The recent collapse in the automobile sector, rising number of non-performing assets, failing manufacturing sector, and sluggish consumer demand has led the Indian economy to hit a rough patch and it has gained unanimous acceptance. The economy has slipped to 5.8% in the first quarter Q1 of FY 2019-20 which is the lowest in past 6 years. The private investment cycle is not picking up as it was expected. Despite recent policy concerns, the government has been struggling to counter a multi-sector slowdown.

IMPACT OF THE CRISIS: MATTERS ARISING

The greatest worry with respect to the impact of the financial crisis in the Indian economy is its negative impact on growth and the resulting consequences on living standards. The expenditure by Indian households has accelerated with an average growth rate of 7.8% compared to an average of 6.1% in 2011-14. But recent sharp fall in PFCE in June quarter to 3.1% compared to 7.2% in the March quarter has significantly contributed to the recent slowdown.

The manufacturing sector is 5% low. Brass and steel in the commodity market are severely affected. The rural wages in the agricultural sector are not growing. These wages are 1.36% low. Exports are down by 10%. There is credit growth in the economy. The shortage of direct tax is aggregated to 62,000 crore rupees. Factory output contracted by 4.3% and eight crore segments have again just registered negative growth. The population is growing by 20% per decade leading to problems that include food deficit, sanitation deterioration, pollution, and unemployment. India needs 10 million new jobs every year to keep up the economy growing and improving the living standards of the people. The banking system Exposure to unsecured loans has risen to an all-time high, RBI data shows. Credit card outstanding due to 93,600 crore rupees at the end of the year versus 74,300 crore rupees during the same period last year. Personal loans grew 6.2 lakh crore rupees versus 5 lakh crore rupees last year. The gross non-performing assets (NPAs) for the system will come down to 8-8.5% by March from a peak of 11.5% in March 2018 as fresh accretion through slippages got slower.

Fig 3: Impact of NPAs of Indian economy, industry and banks



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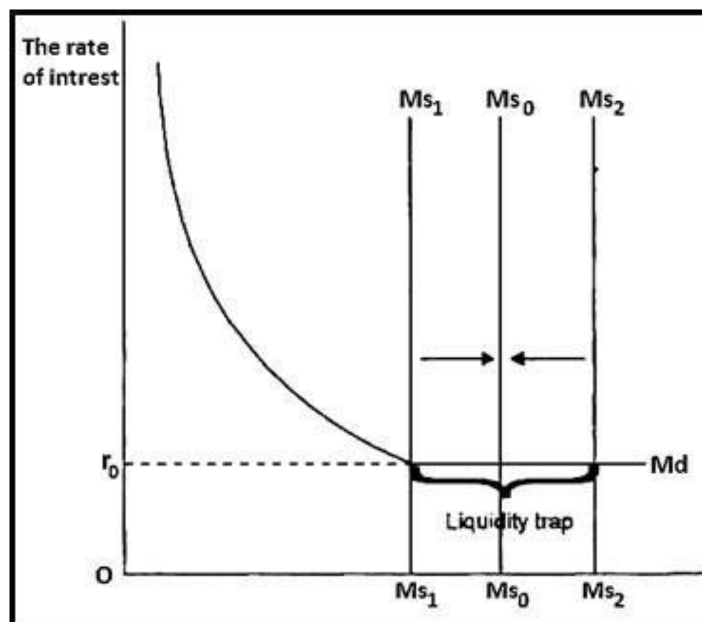
TRANSMITTING SLOWDOWN

The slowdown can be transmitted with the concept of a liquidity trap is the extreme effect of monitory policy in which the general public is prepared to hold on to whatever amount of money is supplied, at a given rate of interest. In that case, a monetary policy is carried out through open market operations has no effect on either the interest rate or the level of income. There is a liquidity trap at short term zero percent interest rate when interest rates zero, the public would not want to hold any bond, since money, which also pays zero percent interest, has the advantage of being usable in a transaction. The monitory policy is ineffective as a result investor shun bonds to avoid capital losses as interest rates initially rise. The high demand for money balances neutralizes the capacity of monitoring pumping to stimulate an economy.

FIG 4: LIQUIDITY TRAP



In order to reduce the risk of digging deeper and creating financial blue in the national economy the authorities have two options.

RAISING THE INFLATION TARGET

Inflation targeting is a policy where RBI follows an explicit target for medium term and announces this inflation target to the general public. The bank will lower or raise rates on the basis of above target and below targets inflation respectively.

LOWER THE ZERO NOMINAL INTEREST RATE FLOOR

This is the situation in which central bank can no longer reduce interest rate to encourage economic growth. Zero lower bond is a macro economic problem that limit the capacity of RBI to stimulate growth.

POLICY RESPONSE TO THE CRISIS AND WAY FORWARD

Growth has momentum and slowdown has inertia. This slowdown can only be reversed if both short-term and long-term reforms are undertaken sectoral collapse because of poor business decisions in banking, real estate, construction, and lately in non-banking finance companies. The government has had discussions with several sections of business and economists over the last few weeks. It has plucked out of all the prickly issues which created a negative perception and eroded trust.

Removing taxation on foreign portfolio investors and other prickly issues Is a hygiene factor. Answer trinity is the main reason which has actually unnerved investors. Government goes ahead and announces the sovereign boring in the budget and then there is so uncertainty around it and government discontinue the policy. There is also a cleanup that is happening in the government of Chronic capitalism. Banks and capital list along with industry leaders And political leadership ensured that money was given out to anybody and banking sector reached to the level of high debt leading to distrust between Government and industries, bankers and borrowers with the general public.

IMMEDIATE STEPS

- Give auto sector incentives to invest and shift to electric vehicles.

- Incentives to auto sector employees to upskill on electric vehicles.
- Change GST collection to quarterly for companies below 1 crore rupees.
- Reduce the GST slab rates.
- Adopt the direct tax code, cut income tax for the bottom slab.
- Improve credit flow to both consumer and industry.
- Reduce real interest rates by 135 basis points as cost of capital has to come down.
- Change the credit culture in public sector banks.
- Stimulus should drive investment up skilling for displaced employees.
- Factor market forms, including bringing the cost of land down.

SUMMARY AND CONCLUDING REMARKS

Economic slowdown occurs when the rate of economic growth slows in an economy. Countries usually measure economic growth in the gross domestic product which is the total value of goods and services produced in an economy during a specified period of time. The economic fluctuations are explained by the business cycle. The session of the slowdown can be for a short period of time if proper corrective actions are immediately taken. The government should reduce the cost of borrowing And make loans more attractive.

The reduction in mortgage interest payment will lead to increase disposable income for householders and saving should be made less attractive. Capable entrepreneurship can lead to the growth of capital formation in a country enough to escape poverty and generating jobs for millions of young people to enter the work force. Government think tank Niti Aayog made a case for taking extraordinary steps to deal with unprecedented stress in the financial sector. The government needs to take steps that element its apprehensions from the minds of private sector players and encourage them to step up investments. This will ensure growth and improve the financial stability and growth in the economy.“ dark economic clouds will dissipate into the emerging blue sky of opportunities”.

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