Indian Economy Gross Domestic Product and Monetary Policy of RBI

By V. Mohan Rao*

India is presently facing unprecedented slump in its economy. This has been aggravated by COVID-19 virus relating to lock down that has added to the decline in consumer demand investment Economists have analyzed and predicted that the Gross Domestic Product (GDP) of the worlds fifth largest economy (Indian Economy) will contract by 18.3% in June quarter compared to 3.1% growth in the previous quarter.

Restrictions on transport, educational institutions, trade and Restaurants have left manufacturing, Industry, retail sales and services sectors in doldrums culminating in millions of workers loosing their Jobs.

To combat the steep slump in economy the Prime Minister announced a $ 226 Billion stimulus package in May including credit guarantee for bank loans and free food grains for the poor people. However this has not stirred the consumer demand which is still in a limbo.

The Reserve Bank of India on its part has reduced the bench mark repo rate by a total of 115 basic points since February 2020 and kept the rates on hold in the midst of rising inflation. Federal and state government could not angument on spending consequent to more than 40% fall in revenue receipts during June quarter.

India started publishing quarterly gross Domestic Product (GDP) data from 1996.

The April-June quarter of 2020 depicted that the GDP contracted by a 23.9 per cent year on year. The economy is witnessing its worst ever fall since 1996. The economy had grown by 3.1 % in the January-March quarter 2020. According to the National statistical office the gross value added (GVA) came to 22.8% Q1 mining contracted by 23.3% versus 4.7 yoy. The Q1 manufacturing growth plummeted by 39.3%. The only silver lining is agriculture growth was at 3.4% versus 3.1 yoy. However the construction growth declined to 50.2% versus 5.2% yoy. Gross Fixed Capital formation was down 47% yoy and government final consumption expenditure rose to 16% yoy Trade, hotels, transport and communication saw a decline of 47 per cent mining output was at 23.3%, whereas electricity & gas declined by 7%.

The RBI may postpone the rate cut to December. The government had capped the fiscal deficit for 2020-21 at Rs. 7.96 lakh crore on 3.5% of the GDP in the budget. Fiscal deficit had soared to 7 years high at 4.6% of GDP in 2019-20 consequent to poor revenue realization which further aggravated towards March due to lock down.

As per the data of CGA the governments revenue receipts was at Rs. 227402 crore or 11.3% of the budget estimate. During the corresponding period last fiscal the realization stood at 19.5% of the budgeted estimate. The revenue collected was at Rs. 202788 crore or 12.4% of budgeted estimate during the first 4 months of fiscal in comparison to 20.5% of BE during the corresponding last fiscal. The total receipts of the government was 10.4% of budgeted estimate or Rs.232860 crore. The budget estimate was Rs. 22.45 lakh crore. The total expenditure of the government was at Rs. 1054209 crore or 34.7% of BE.

Since India's economy contracted by 23.9% in April June Quarter the real GDP for Fy21 is expected to decline by 10.9% as per SBI research report ECOWRAP. Its earlier estimate of real gross domestic product (GDP) was (-) 6.8% for the current fiscal.

The first quarter GDP contraction was at 3% growth when compared to 5.2% expansion in the same period.

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As per SBI estimate all the 4 quarters of Fy21 will show negative real GDP growth and the decline of full year growth is expected to be in double digits around 10.9%.

The SBI report further estimates Q2 real GDP to decline by about (-) 12% to (-) 15% while Q3 GDP is expected to be (-)5% and (-) 10% Q4 is projected to be in the range of (-) 2% to (-)5%.

The report attributes the decline in the Country's GDP growth to 23.9% in Q1 Fy 21 due to the nations lock down consequent to the COVID 19 pandemic.

The private final consumption expenditure (PFCF) growth also plummeted due to COVID 19 containment measures was mostly pertaining to essential items. As the investment demand was not picking up as a result of unused capacity, it is expected that shares of private consumption expenditure will be high in the overall GDP estimate. The Corona virus has impacted expenditure patterns substantially under the individual consumption expenditure with respect to health and education.

The RBI data regarding sector wise credit for the month of July exhibits that credit has increased in all major sectors except industry. The credit to MSE (micro and small enterprises) agriculture and allied sectors, personal loans have increased significantly.

The report also said new project announcements were seen during first quarter included road ways, basic chemicals, electricity, community services like hospital, water sewage pipelines.

However there is an imperative need to revive sectors that are deeply in trouble like construction, hotels, aviation and trade. It is incumbent to restore transportation services and emphasis on infrastructure by way of issuance of special bonds like RBI perpetual bonds besides supporting states by fiscal measures.

Rules allowing banks more room to buy and hold government debt would help towards absorbing the extra expenditure needed for the growth of the economy.

The RBI is conducting a FED style "Operation TWIST" program where in the banks will buy long term debt while selling shorter maturity securities.

The World Bank commented on this in its Global Economic Prospects report published in June for developing economic "the exceptional severity of the pandemic and economic collapse raises concerns about the risk of super hysteresis not only a permanent loss of output levels but a permanent slow down in potential output growth". It further said the foundation upon which the emerging markets boom of the past few decades under threat. ❑