

Economic Survey 2016-17



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A magnifying glass is positioned over a financial document, highlighting several large monetary values. The document contains various numbers, some in red and some in black, representing different financial figures. The magnifying glass is centered over the text, which is overlaid on a semi-transparent blue background.

Fiscal rules and lessons from states

1.365.144,00

1.255.870,00

92.130,00

150.264,00

370.454,00

55.807,00

20.147,00

325.612,00

5.012.569,00

1.045.789,00

Why is fiscal prudence important?

- The three critical risks of a higher fiscal deficit — higher inflation, higher interest rates and a weaker currency
- BoP crisis like situations
- Industrial growth suffers

FRBMA 2003

- Fiscal management principles, making it incumbent on the Centre to reduce the fiscal deficit and, to eliminate revenue deficit - as per the targets set out there after
- No deviation from the targets in permitted except on grounds of national security/calamity.
- Prohibits the Centre from borrowing from the Reserve Bank of India — that is, it bans deficit financing through money creation.
- Requires the government to place before Parliament three statements covering - Medium Term Fiscal Policy, Fiscal Policy Strategy and Macroeconomic Framework, each year along with the Budget.

FRLs

- Fiscal targets were established, which were the same for all states
- The overall deficit was not allowed to exceed 3 percent of GSDP at any point (relaxed to 4 percent of GSDP in 2009/10 due to 2008 crisis)
- Revenue deficit was to be eliminated by 2008/9
- The 12th Finance Commission allowed states to borrow directly from the market, in the hope that investors would also exercise some discipline, by pushing up interest rates on states whose fiscal position had not improved
- New reporting requirements: publish annual Medium-Term Fiscal Policy reports
- Average debt to GDP ratio fell by 10 percentage points

Is it all due to FRLs?

- Acceleration of nominal GDP growth (6%) helped boost states' revenues by about 1% of GSDP.
- Own tax revenues as a percent of GSDP increase by 1 percentage point
- Increased transfers from the centre of about 0.9 percent of GSDP because of the 13th FC
- Reduced interest payments of about 0.9 percent of GSDP - debt restructuring package offered by the centre
- CSSs spending by the center

Future Lessons

- Need to incentivise good fiscal performance:
- 13th FC's recommendation of allocating resources across states (the so-called "horizontal" criteria) based on states' own fiscal performance (which had 17% weightage) can be brought in again.
- 14th FC's attempted to shift towards incentive by relaxing some of the FRL limits for better performing states, but there was some element of tension in its recommendations
- Need for greater market-based discipline on state government finances
- Incentivizing good performance by the states will require the centre to be an exemplar of sound fiscal management itself

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How to create more jobs?

- Generating rapid economic growth
- Nurturing an enabling environment for investment
- Targeted action in certain labour intensive sectors

Why focus on jobs

- Every month more than a million people become eligible to join the workforce
- Unemployment rate has grown from 6.8 in 2001 to 9.6 in 2011
- By 2050, at least 280 million more people will enter the job market in India

What kind of jobs?

- Can generate jobs that are formal and productive,
- Provide bang-for-buck in terms of jobs created relative to investment,
- Have the potential for broader social transformation as they employ women,
- Can generate exports and growth

Apparel and leather and footwear meet this criteria

Why only these sectors?

- Every successful economic growth take-off in post-war history in East Asia has been associated with rapid expansion in clothing and footwear exports in the early stages
- In its take-off phase of growth, India has underperformed relative to the East Asia
- Female labour intensity for apparel and leather industry is very high when compared to major manufacturing sectors
- Opportunity for women means that these could be vehicles for social transformation
- China stabilizing or losing market share – because of rising wage levels in China
- The space vacated is being taken over by Bangladesh and Vietnam in case of apparels; Vietnam and Indonesia in case of leather and footwear.

Why only these sectors?

- Jobs per unit of investment – Apparels are 80-fold more labour-intensive than autos and 240-fold than steel
- High employment elasticity – due to this, rapid export growth could generate about half a million additional direct jobs every year

Table 2. Jobs to Investment Ratio for Select Industries

Sectors	Investment (Rs Crores)*	Jobs (Lakhs)	Jobs per lakh Investment	Female Jobs (Lakhs)	Female Jobs per lakh Investment
Apparels (NIC 14)	3156	75.4	23.9	25.9	8.2
Leather & Footwear (NIC 15)	1624.5	11.6	7.1	5.5	3.4
<i>Of which</i>					
Tanning and Dressing of Leather & Fur (NIC 1511)	470.8	2.2	4.6	1.1	2.4
Leather Goods (NIC 1512)	218.3	2.2	9.9	0.8	3.9
Footwear (NIC 1520)	935.4	7.2	7.7	3.6	3.8
Textiles (NIC 13)	17814.7	71.3	4	22.5	1.3
Food Processing (NIC 10)	21119	50.2	2.4	27.9	1.3
Autos (NIC 2910 & 2930)	29647.6	7.6	0.3	3	0.1
Steel (NIC 2410 & 2431)	70528.3	7.8	0.1	3.7	0.05

Source: ASI 2012-2013, NSSO 68th round

Note: *Investment is Gross Fixed Capital Formation

Challenges are abundant



Logistics

Labor Regulations

**Tax and Tariff
Policies**

**Export market
discrimination**

Solutions

- Textile and apparel firm to be provided a subsidy for increasing employment
- FTA's with EU and UK
- Rationalization of taxes through GST
- Choice to employees on deductions

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Review of Economic Developments

➤ Fiscal Developments

- FD projected at 3.5% down from 3.9%
- Indirect taxes grew despite possible short term effects of demonetization
- Revenue Expenditure on account of 7th PC
- Increase in food subsidy
- Grants for creation of capital assets to the states

➤ Inflation

- Pulse continued to be the major contributor of food inflation
- The food inflation is likely to remain subdued in the light of
 - ❖ Higher Rabi sowing acreage,
 - ❖ Projected increase in the production of pulses and key agri-products globally
 - ❖ Astute food management and price monitoring by the Government.

Review of Economic Developments

➤ Strengthening corporate bond markets

- Permitting commercial banks to issue rupee-denominated bonds overseas (masala bonds) for their capital requirements ,financing infrastructure and affordable housing
- Brokers registered with the SEBI and authorized as market makers in corporate bond market permitted to undertake repo / reverse repo contracts in corporate debt securities
- Banks allowed to increase the partial credit enhancement they provide for corporate bonds to 50 per cent from 20 per cent.
- Simplified procedures to ease access to the foreign exchange market for hedging in over the counter (OTC) and exchange-traded currency derivatives up to a limit of US\$30 million at any given time.

Review of Economic Developments

- Top three import destinations of India were China, UAE and USA in 2016-17
- USA followed by UAE and Hong Kong were the top export destinations
- Positive factors helping narrowing of CAD:
 - Sharp contraction in trade deficit outweighed the decline in net invisible earnings.
 - Decline in oil import bill due to low prices by around 18 per cent
 - Sharp decline in gold imports led to a reduction in India's overall imports.

Improving learning outcomes

- Teacher absenteeism and the shortage of professionally qualified teachers remain an issue to be addressed
- Shortage of professionally qualified teachers remain an issue to be addressed.
 - Biometric attendance of all teachers in primary schools should be taken, regularly monitored by local communities and parents and should also be put in public domain.
 - Apart from this, adequate teaching aids, recorded lectures, etc. should be used to fill in for absentee teachers.
 - The implementation should leave for local flexibility so the same do not end up as top driven 'Model Schools'.
 - The pilot of biometric attendance of teachers should be accompanied with an evaluation of learning outcomes.

Agricultural Price Management - Pulses

- Government procurement machinery should be prepared to ensure the procurement of 29 Kharif pulses at this season's announced MSP.
- To ensure effective procurement, a High Level Committee comprising Ministers of Finance, Agriculture, and Consumer Affairs and Principal Secretary to PM should be constituted.
- Build up gradually but opportunistically 2 million tons of pulses stock with targets for individual pulses, especially tur (3.5 lakh tonnes) and urad (2 lakh tonnes).
- Eliminate export ban on pulses and stock limits which coupled with weak procurement forces farmers to sell most of their output at market prices that are well below MSP; at the very least limits on wholesalers should be eliminated.
- Encourage states to delist pulses from their APMC.
- Review Essential Commodities Act, 1955 and futures trading of agricultural commodities.
- Create a new institution as a Public Private Partnership (PPP) to compete with and complement existing institutions to procure stock and dispose pulses
- Encourage development of GM technologies

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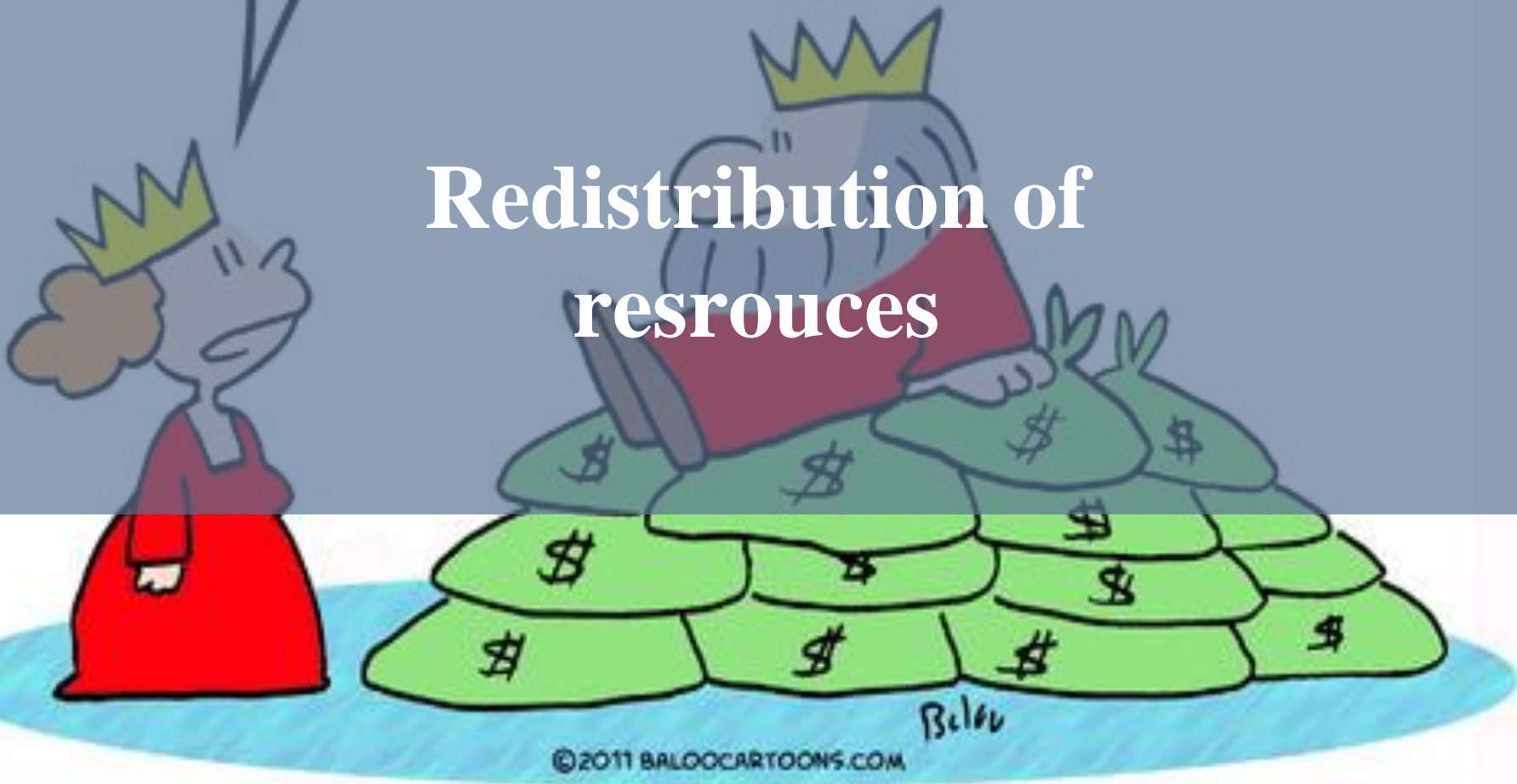
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ACTUALLY, THE IDEA IS THAT
YOU REDISTRIBUTE THE
WEALTH TO **OTHER** PEOPLE.

Redistribution of resources



Models of development

- **Peninsular India has offered three different models of development:**
- **Traditional East Asian mode of escape from development based on manufacturing (Gujarat and Tamil Nadu)**
 - **Remittance-reliant mode of development exemplified by Kerala**
 - **“Precocious India” model based on specializing in skilled services (Karnataka, Andhra Pradesh and TN)**

In other Indian states (‘Other Indias’), including hinterland, forested, natural resources rich, and ‘Special Category’ status states, two models of development can be observed:

- **Based on “aid” or special status - most applicable to the erstwhile ‘Special Category’ states that include North-eastern states and Jammu and Kashmir**
- **Based on natural resources - Jharkhand, Chhattisgarh, Odisha, Gujarat and Rajasthan. Natural resources include coal, onshore oil and natural gas, major and minor minerals but exclude forest cover**

Models of development

- Two views of development for poor and developing countries emerged –
 - Foreign aid
 - Mineral resources: those with vast amount of minerals should sell them to gain capital

Counter Narrative

- develop Aid perpetuates resource dependency: recipient countries may fail to their own tax bases or their institutions
- natural It may trigger ‘Dutch disease’: named after the impact that discovery of gas in the North Sea had on the economy of Netherlands.
- industries, The extra income spent domestically, pushed up prices of nontradeables like services. This eroded profitability of export and import competing de-industrializing the economy

Redistributive Resources Transfer

- The relationship between per capita RRT and per capita GSPD shows that as expected poorer states receive the highest transfers
- Despite such flows over the past few decades, higher the RRT, the slower is growth, the smaller is the share of manufacturing in GSDP, The lower its own tax revenues and even on part of quality of governance, the RRT found negative relationship.
- This suggests that there might be an “RRT curse”.

Economies with resource base

- Three possible explanations for resource curse:
 - Exploitation of natural resources generates rents, which leads to rent-seeking and increased corruption.
 - Exposes countries to commodity price volatility, which can destabilize GDP growth.
 - Natural resource ownership – like foreign aid — makes countries susceptible to “Dutch Disease”

Economies with resource base

➤ Natural Resources and Evidence from Indian States

- The mineral resource rich states are: Jharkhand, Chhattisgarh, Odisha, Rajasthan and Gujarat.
- The relationship between availability of resources and reduction in poverty in mineral rich states shows that they seem relatively successful. Their poverty ratio fell by around 31% over nearly two decades, compared with 28% in the other states.
- However the gains were not passed on equally to all sections of the population. In particular, ST population of the mineral-rich states, which forms the predominant population in these areas, saw only a 17% decline in poverty, smaller than the 22% fall in the other states.
- There seems to be no concrete evidence either in favour or against a “resource curse” in the context of Indian states. However, the resource rich states need to bolster efforts to counter any possible downsides of a “resource curse” that may emerge in the future

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Competitive Sub Federalism

Importance of urbanization

- As recently as 1991, there were only 220 million Indians living in cities, equivalent to about one-quarter of the population. By 2011, there were no less than 380 million
- Urban Indians now form about one-third of the population – and they produce more than three-fifths of the country's GDP
- The exodus of rural Indians into the cities over the coming decades will pose tremendous challenges for government

Problems with India's urbanization

- India's urbanization rate appears to have been similar to that in other countries
- But patterns of urbanization show anomaly as per Zipf's law
- Many of the smaller cities are unusually small and contrary to what one might think, so are the bigger ones
- Much of this urban growth is likely to take place in the bigger cities, possibly bringing the country in line with Zipf's Law

Reasons for failure of Zipf's law

- Infrastructure of the cities are overburdened.
- India is land scarce relative to most countries, discouraging migration particularly because distorted land markets render rents unaffordable.
- Mobility in India is limited by strong place based preferences embedded in deep social networks in India

Key Challenges

- **ULBs face major and inextricably linked problems: poor governance capacities, large infrastructure deficits and inadequate finances.**
- **There is a significant fragmentation of responsibilities and service delivery across gamut of institutions**
- **Transparency / accountability issues: because implementation of the e-Governance initiative has also not been uniform**

Key Challenges

- Addressing infrastructure deficit will require resources, some of which could come from the Centre and the states. The rest of the required funds would have to come from local resources but raising sufficient resources has not proved easy
- Devolution of functional and financial powers to the ULBs. Some states have not even allowed the municipalities to levy property taxes
- Even when powers have been devolved, exercising them has proved difficult. Municipal own income comes from taxes; user fees; and domestic borrowing

Issues with property taxes

- Is the most important constituent of own revenue but problems of low coverage, low rates, low collection efficiency, and lack of indexation of property values, making it a non-buoyant source of revenue
- ULBs by and large have not been able to levy adequate user charges to cover even the operation and maintenance costs
- Issuing municipal bonds has been challenging owing to the poor state of ULB finances and governance

Municipal bonds

- Municipal bonds have been in existence in India since 1997. Cities such as Ahmedabad, Bengaluru, Nashik and Madurai have issued them; mostly privately placed with institutions, and not tradable. As a result, the municipal bond issues only touched ₹1,353 crores and there have been no new issues since 2010.
- SEBI has put in place several conditions : The corporation needs to have investment grade credit rating and must contribute at least 20 per cent of the project cost. 2.It must not have defaulted on any loans in the last one year. 3. Required to maintain full asset cover to repay the principal amount. Revenues from the project for which bonds were raised are to be kept in a separate escrow account. And banks or financial institutions would monitor the account regularly
- USA and UK. In China, the government is reported to soon start a full-fledged nationwide market called the ‘Muni bonds market’
- A potential of Rs 1,000-1,500 Cr. per annum could be raised through Municipal bonds over the next five years

Municipal bonds

- On the demand side, the conservative approach of insurance and pension firms to invest in Municipal bonds and limited credit enhancements for municipal bonds limit the potential demand for these bonds
- On the supply side on the other hand, issues such as very few municipal entities with high credit, lack of incentives for municipal bodies to tap debt market, preponderance of institutional finance and lastly absence of any particular requisites to issue bonds serve as major impediments

Way Ahead

- The states should empower cities to levy all feasible taxes
- Efficient collection of existing tax base, there is need to adopt the latest satellite based techniques to map urban properties in order to tap full potential of property tax
- Higher bodies (state governments) should cede power and share resources with local bodies. Finance commission can play a vital role by allocating more resources to ULBs
- Also, data and transparency can play an important role here. Grants to ULBs by MoUD can be more tightly linked to comprehensive and updated data disclosure and transparency
- NITI Aayog should compile comparative indices of municipalities' performance annually. This index should be based on the actual accountability and administrative capacity to deliver the core public services

Thank You

THANK YOU



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