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HOUSE OF CARDS

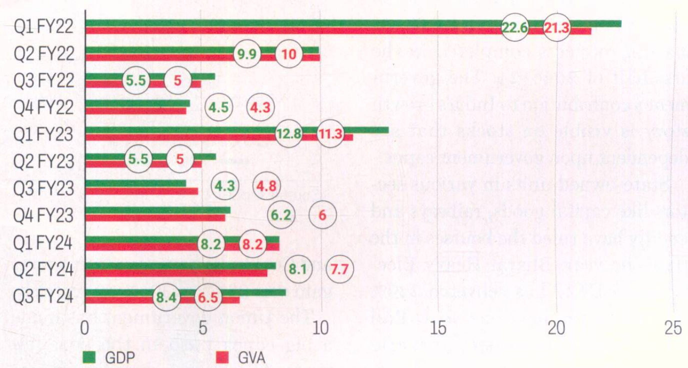
At 8.4%, India's GDP surpassed the expectations of analysts of almost all dispositions. But are GDP numbers hiding a bleaker story? It is not just the missing private money, there are more devils in the story

» Parth Singh

Photo: Shutterstock

WIDENING GAP

Usually, there is not much difference between GDP and GVA figures. However, in the December quarter of 2023-24, the disparity between India's GDP and GVA figures reached a 10-year high



Source: Ministry of Statistics and Programme Implementation

India's gross domestic product (GDP) growth rate for the December quarter of the fiscal year 2023-24 has astounded observers, reaching 8.4%, a figure that even the Reserve Bank of India was not expecting. Currently when eurozone economies are stagnant and China, the second-biggest economy, faces headwinds, India's growth is perhaps the only bright spot in a world racked by geopolitical tensions.

"Robust 8.4% GDP growth in the third quarter of 2023-24 shows the strength of Indian economy and its potential. Our efforts will continue to bring fast economic growth which shall help 140 crore Indians lead a better life and create a *Viksit Bharat*," Prime Minister Narendra Modi posted on X (formerly Twitter).

There has been considerable debate regarding the reliability of GDP data in recent quarters, with critics suggesting potential inflation through methodological jugglery. The latest data sets have received similar criticism, with some pointing to the disparity between gross value added (GVA) and GDP.

While GDP is a measure of the total value of goods and services produced within a region's borders, GVA is the value producers add to the goods and services they buy, and thus provides an insight into the raw economic output within the country. Mathematically, GVA is calculated by adding subsidies to the GDP and subtracting indirect taxes (GST).

In the December quarter of 2023-24, the disparity between India's GDP and GVA figures reached a 10-year high. During the recent quarter, while India recorded a GDP growth rate of 8.4%, its GVA grew by only 6.5%—reflecting a significant divergence of 190 basis points.

"The wide gap [between GVA and GDP numbers] follows from a surge in growth of net indirect taxes to a six-quarter high of 32% in this quarter, which is unlikely to be sustainable," says Aditi Nayar, chief economist at ratings agency, ICRA.

In the December quarter, the Centre's subsidy burden decreased to less than half from the same period a year ago, leading to a 190-basis point difference between GDP and GVA. However, placing excessive emphasis on this gap is fussing over inconsequentials.

Even with a 6.5% growth, India remains ahead of competing economies. But the devil lies in the detail.

Missing Private Sector

The remarkable GDP numbers for the December quarter were fuelled by the manufacturing, construction and utility sectors. Manufacturing grew 11.6% year-on-year this quarter, while construction and utility were up 9.5% and 9% respectively.

In emerging markets, witnessing these sectors firing on all cylinders should be cause for celebration. But that is not the case with India. You guessed it right, the spoilsport yet again is the missing private sector. While you have heard this story before, we are adding a few new layers of data for you. And the picture is definitely more worrying than just the absence of big-ticket private investment.

A look at the Index for Industrial Production (IIP) gives a hint as to what ails the Indian economy. The growth in IIP fell to 3.8% in January from 4.2% recorded in December. The January 2024 data on manufacturing, which covers 23 components, shows that 12 segments have still not managed to cross their pre-pandemic levels recorded in January 2020.

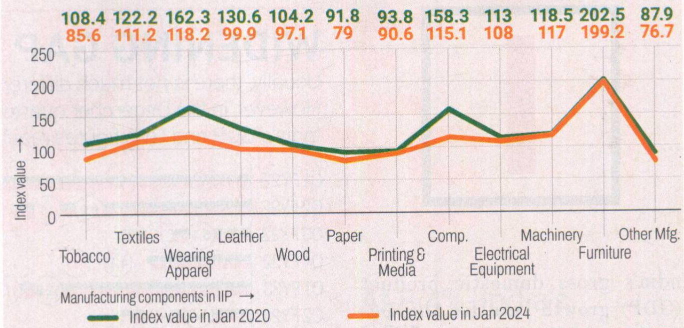
The manufacturing segments which are doing well include basic metals and transport equipment, driven by government capital expenditure (capex). But manufacturing of consumer-facing goods like computers and furniture is yet to see a revival, the IIP data reveals.

Data from credit rating agency CareEdge Ratings shows the government had a 63.1% share in projects under implementation and a 52.4% share in projects completed in the first half of 2023-24. The government's contribution to India's growth story is visible on stocks that are dependent upon government capex.

State-owned units in various sectors like capital goods, railways and energy have ruled the bourses in the past one year. Bharat Heavy Electricals (BHEL) has delivered 229% returns in the past one year. Rail Vikas Nigam, the construction arm of the railways ministry, has seen its stock price jump by 277% in the past one year. Indian Railways Finance Corporation's (IRFC) shares jumped over 398% during the same period. A similar story played out in the energy sector where power generator NTPC and Coal India have seen their shares gain over 92% and 104% respectively.

STILL PLAYING CATCH UP

The growth in IIP fell to 3.8% in January from 4.2% recorded in December. Several sectors are still to regain their pre-pandemic levels



Source: MoSPI

The Union government has made a big capex push in the past few years. Allocation in investment rose from Rs 3.4 lakh crore in 2019-20 to Rs 11.1 lakh crore in 2024-25, a surge of 226%. On the other hand, private investment went up to only Rs 8.5 lakh crore in 2023-24 from Rs 5.5 lakh crore in 2019-20.

"This substantial increase [in capex] in recent years is central to the government's efforts to enhance growth potential and job creation, crowd in private investments and provide a cushion against global headwinds," said Nirmala Sitharaman, Union finance minister while presenting the Budget in 2023. The follow-up question to the finance minister is why has this substantial capex push from the government for the past decade failed to invigorate private investment.

This question is baffling economists as well.

The sustainability of investment growth in the medium term hinges significantly on the strength of consumption growth

RAJANI SINHA
CHIEF ECONOMIST, CAREEDGE

Tepid Demand

Dharmakirti Joshi, chief economist at credit rating agency CRISIL, believes although conditions for private sector investments have become conducive in recent years, a broad-based recovery still not happening after 10 years of massive capex push is a cause for worry.

"The pick-up in private sector investments is buoyant in sectors such as steel and cement which are linked to government's infrastructure spending and housing sector pick up. Industrial policies like the PLI [production-linked incentive] are also bringing in some investments, in sectors like pharma and electronics. We expect investments in other new age segments like advanced carbon composite batteries, electric vehicles, semiconductors to pick up soon. Private investment is very gradually getting broad-based," he says.

For now, it is the government that is driving India's growth. But to sustain the momentum, it is imperative that the private sector steps in. But New Delhi has news! The Centre says private sector investment has begun.

"Now, that the private investments are happening at scale, the lower borrowings by the central government will facilitate larger availability of credit for the private sector," said Sitharaman in her Budget speech.

"Perhaps the government has

more information than we have. They know who is approaching them for various approvals. When that fructifies and starts showing in the numbers, then we will be on the same page," says Devendra Kumar Pant, chief economist at India Ratings and Research.

One of the reasons that explains lagging private investments is the tepid demand in the Indian economy. In the December quarter, the private final consumption expenditure (PFCE), a measure of the final consumption of goods and services by resident households, showed a growth rate of 3.5%, substantially lower than the headline GDP number—8.4%—for the same quarter.

This seems to be an anomaly. Consumption growth is typically at the same level as GDP growth or slightly lower, according to Pronab Sen, India's former chief statistician.

The relatively low consumption number comes at a time when net financial savings of households were recorded at nearly a five-decade low of 5.1% of GDP in 2022–23.

Economists at Nomura, a brokerage, say the Indian economy still relies heavily on public expenditure, while private expenditure and consumption remain restrained. Moreover, the firm said in a note that underlying growth needs to be analysed to see the true picture. It looked at core GDP, which is GDP without valuables, inventories and discrepancies. The data reflects how private consumption expenditure, government expenditure, export-import and fixed capital formation grew in a specified period.

Nomura's data showed that in the third quarter, core GDP slowed to 4% from 4.7% in the second quarter. This reflected a similar trend in the slowdown recorded in GVA. "The moderation in core GDP growth and in GVA growth suggests growth remains uneven," the note said.

Based on these numbers, economists are of the view that the increase in incomes is not in line with the growth story, and has resulted in weak demand, making India non-lucrative for private sector investment.

PSU STOCKS ON FIRE

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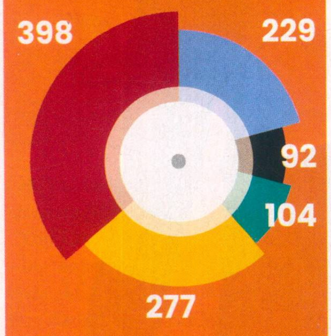

One-year returns (%), Data till March 12
Source: NSE

The wages of agriculture workers and non-agriculture workers in rural areas experienced minimal yearly growth of 0.6% and 0.3%, respectively during the first half of 2023–24, according to data by India Ratings. In contrast, urban wages surged by 5.6%, while corporate India witnessed a robust growth of 7.9%.

"The sustainability of investment growth in the medium term hinges significantly on the strength of consumption growth," says Rajani Sinha, chief economist at CareEdge.

Debt Burden

What should worry all the backers of the India growth story is the fact that the Centre has accumulated a substantial debt on its books to keep the GDP growth at an enviable rate. India's debt-to-GDP ratio has gone over 82% in 2023 from 70% in 2018. The Centre has benefitted from rise in GST collections at a compound annual growth rate (CAGR) of 10.9% in the past five years, but it is unlikely to sustain it in the long run.

A significant increase in debt burden can be a factor for recession in any economy. Countries such as Greece and Argentina faced crises due to unsustainable levels of public debt stemming from excessive borrowing and economic mismanagement. Argentina's public debt-to-GDP ratio jumped from 54% in 2001 to 153% at the end of 2002, while Greece's public debt levels equated to over 155% of GDP in 2008.

India's fiscal deficit estimate in 2023–24 is 5.8%, down from 9.2% in 2020–21. According to the Union government's fiscal consolidation glide path, it would want the deficit to come down to 5.1% in 2024–25.

The government's fiscal pipeline is drying up. In the interim budget presented in February this year, the Centre increased the budget for capex by just 17% at Rs 11.1 lakh crore for 2024–25 compared to a CAGR of 30% between 2019–20 and 2023–24. The limits of government capex are beginning to show.

An economist, speaking on condition of anonymity, cautioned that India could attract scrutiny from global investors if the government fails to maintain fiscal conservatism, especially following the inclusion of the country's bonds in the JP Morgan Emerging Markets Bond Index and Bloomberg Bond Index.

The expansion of India's exposure to global investors occurs as the impetus driving growth momentum may diminish. Weak private consumption, which consequently hinders private investment, has emerged as a significant flaw in India's growth narrative.