ECONOMIC SURVEY 2020-21

VOLUME-1

SUMMARY

STRATEGY BOFFINS

CH 1 - SAVING LIVES AND LIVELIHOODS AMIDST A ONCE-IN-A-CENTURY CRISIS

After all, pushing down on the accelerator while the brakes are clamped only wastes fuel.

Key Points

Covid-19

- Government imposed the most stringent lockdown at the very onset of the pandemic. This enabled flattening of the pandemic curve and, thereby, provided the necessary time to ramp up the health and testing infrastructure.
- Survey infers that the lockdown had a causal impact on saving lives and the economic recovery. India thus benefited from successfully pushing the peak of the pandemic curve to September, 2020 through the lockdown.

Economy

- While there was a 23.9 per cent contraction in GDP in Q1, the recovery has been a V-shaped one as seen in the 7.5 per cent decline in Q2 and the recovery across all key economic indicators.
- A slew of structural reforms were announced; together, these would help to expand supply significantly in the medium to long term. On the demand side, at the onset of the pandemic, India's policies focused purely on necessities.

Source: https://www.indiabudget.gov.in/economicsurvey/

CH 2 - DOES GROWTH LEAD TO DEBT SUSTAINABILITY? YES, BUT NOT VICE- VERSA!

As the COVID-19 pandemic has created a significant negative shock to demand, active fiscal policy is needed

Key Points

- Growth leads to debt sustainability in the Indian context but not necessarily vice-versa. This is because the interest rate on debt paid by the Indian government has been less than India's growth rate by norm, not by exception.
- Debt sustainability depends on the "interest rate growth rate differential" (IRGD), i.e. the difference between the interest rate and the growth rate in an economy. In advanced economies, the extremely low interest rates, which have led to negative IRGD, on the one hand, and have placed limitations on monetary policy, on the other hand, have caused a rethink of the role of fiscal policy. The same phenomenon of a negative IRGD in India – not due to lower interest rates but much higher growth rates –must prompt a debate on the saliency of fiscal policy, especially during growth slowdowns and economic crises.
- As the IRGD is expected to be negative in the foreseeable future, a fiscal policy that provides an impetus to growth will lead to lower, not higher, debt-to-GDP ratios.

Source: https://www.indiabudget.gov.in/economicsurvey/

CH 3 - DOES INDIA'S SOVEREIGN CREDIT RATING REFLECT ITS FUNDAMENTALS? NO!

India's fiscal policy must not remain beholden to a noisy/biased measure of India's fundamentals.

Key Points

- Never in the history of sovereign credit ratings has the fifth largest economy in the world been rated as the lowest rung of the investment grade (BBB-/Baa3)
- Within its sovereign credit ratings cohort – countries rated between A+/A1 and BBB-/Baa3 for S&P/ Moody's – India is a clear outlier on several parameters, i.e. a sovereign whose rating is significantly lower than mandated by the effect on the sovereign rating of the parameter. These include GDP growth rate, inflation, general government debt (as per cent of GDP), cyclically adjusted primary balance (as per cent of potential GDP), current account balance (as per cent of GDP), political stability, rule of law, control of corruption, investor protection, ease of doing business, short-term external debt (as per cent of reserves), reserve adequacy ratio and sovereign default history.
- Credit ratings map the probability of default and therefore reflect the willingness and ability of borrower to meet its obligations. India's willingness to pay is unquestionably demonstrated through its zero sovereign default history. India's forex reserves stood at US$ 584.24 as of January 15, 2021, greater than India's total external debt (including that of the private sector) of US$ 556.2 bn as of September 2020.
- Despite this compelling statistic, India is an inexplicable outlier in its ratings cohort. Past episodes of rating changes have no or weak correlation with macroeconomic indicators. Despite ratings not reflecting fundamentals, noisy, opaque and biased credit ratings damage FPI flows.

Source: https://www.indiabudget.gov.in/economicsurvey/

CH 4 - INEQUALITY AND GROWTH: CONFLICT OR CONVERGENCE?

Redistribution is only feasible in a developing economy if the size of the economic pie grows

Key Points

- Inequality is no accident but an essential feature of capitalism? The relationship between inequality and socio-economic outcomes, on the one hand, and economic growth and socio-economic outcomes, on the other hand, is different in India from that observed in advanced economies.
- By examining the correlation of inequality and per-capita income with a range of socio-economic indicators, including health, education, life expectancy, infant mortality, birth and death rates, fertility rates, crime, drug usage and mental health, the Survey highlights that both income per capita (as a proxy for economic growth) and inequality have similar relationships with socio-economic indicators. Thus, unlike in advanced economies, in India economic growth and inequality converge in terms of their effects on socio-economic indicators.
- Economic growth has a far greater impact on poverty alleviation than inequality. Therefore, given India's stage of development, India must continue to focus on economic growth to lift the poor out of poverty by expanding the overall pie. Note that this policy focus does not imply that redistributive objectives are unimportant, but that redistribution is only feasible in a developing economy if the size of the economic pie grows.

Source: https://www.indiabudget.gov.in/economicsurvey/

CH 5 - HEALTHCARE TAKES CENTRE STAGE, FINALLY!

India must take steps to improve healthcare accessibility and affordability in the country

Key Points

- The ongoing pandemic has showcased how a healthcare crisis can get transformed into an economic and social crisis.
- The next health crisis may not possibly involve a communicable disease. Therefore, India's healthcare policy must continue focusing on its long-term healthcare priorities. To enable India to respond to pandemics, the health infrastructure must be agile
- Given its potential to provide healthcare access in remote areas, telemedicine needs to be harnessed to the fullest by especially investing in internet connectivity and health infrastructure.
- The National Health mission (NHM) has played a critical role in mitigating inequity as the access of the poorest to pre-natal and post-natal care as well as institutional deliveries has increased significantly. Therefore, in conjunction with Ayushman Bharat, the emphasis on NHM should continue.
- With limited visibility into patients' medical records and no standardised treatment protocols, insurance companies have a risk of adverse selection at the time of policy issuance and a risk of moral hazard at the time of claims. To safeguard against this risks, insurance companies resort to high premiums and restriction of services covered in the insurance policy. Addressing this information asymmetry can help lower premiums, enable the offering of better products and help increase the insurance penetration in the country.
- A sectoral regulator to undertake regulation and supervision of the healthcare sector must be considered given the market failures stemming from information asymmetry.

Source: https://www.indiabudget.gov.in/economicsurvey/

CH 6 - PROCESS REFORMS

The problem is that policymakers, by default, tend to favour prescriptive regulation over supervision.

Key Points

- Unlike supervision, regulation can be easily measured. After all, regulations provide criteria or checklists, making it easier for regulators to follow and reduce their accountability later on. In contrast, it is difficult to quantify the amount and quality of supervision.
- Real-world regulation is inevitably incomplete because of the combination of: (i) bounded rationality due to “unknown unknowns”, (ii) complexity involved in framing “complete” contracts across all possible contingencies, and (iii) the difficulty for a third party to verify decisions. This makes some discretion unavoidable in decision making. The evidence shows that over-regulation, not simpler regulation, leads to opaque decision making.
- The issue of over-regulation is illustrated through a study of time and procedures taken for a company to undergo voluntary liquidation in India. Even when there is no dispute/ litigation and all paperwork is complete; it takes 1570 days to be stuck off from the records. This is an order of magnitude longer than what it takes in other countries.
- The optimal solution is to have simple regulations combined with transparent decision making process. Having provided the government decision maker with discretion, it is important then to balance it with three things- improved transparency, stronger systems of ex-ante accountability (such as bank boards) and ex-post resolution mechanisms.

Source: https://www.indiabudget.gov.in/economicsurvey/

CH 7 - REGULATORY FORBEARANCE AN EMERGENCY MEDICINE, NOT STAPLE DIET!

Treat emergency measures as such and not to extend them even after recovery: when an emergency medicine becomes a staple diet, it can be counterproductive.

Key Points

- Regulatory forbearance for banks involved relaxing the norms for restructuring assets, where restructured assets were no longer required to be classified as Non-Performing Assets (NPAs henceforth) and therefore did not require the levels of provisioning that NPAs attract.
- During the 2008 Global Financial Crisis (GFC), forbearance helped borrowers tide over temporary hardship caused due to the crisis and helped prevent a large contagion. However, the forbearance continued for seven years though it should have been discontinued in 2011, when GDP, exports, IIP and credit growth had all recovered significantly. Yet, the forbearance continued long after the economic recovery, resulting in unintended and detrimental consequences for banks, firms, and the economy. Given relaxed provisioning requirements, banks exploited the forbearance window to restructure loans even for unviable entities, thereby window dressing their books. The inflated profits were then used by banks to pay increased dividends to shareholders, including the government in the case of public sector banks. As a result, banks became severely undercapitalized. Undercapitalization distorted banks' incentives and fostered risky lending practices, including lending to zombies. As a result of the distorted incentives, banks misallocated credit, thereby damaging the quality of investment in the economy. Firms benefitting from the banks' largesse also invested in unviable projects. By the time forbearance ended in 2015, restructuring had increased seven times while NPAs almost doubled when compared to the pre-forbearance levels.
- The prolonged forbearance policies following the GFC thus engendered the recent banking crisis that brought down investment rates and thereby economic growth in the country.

Source: https://www.indiabudget.gov.in/economicsurvey/

CH 8 - INNOVATION: TRENDING UP BUT NEEDS THRUST, ESPECIALLY FROM THE PRIVATE SECTOR

India's gross expenditure on R&D at 0.65 per cent of GDP is much lower than that of the top 10 economies

Key Points

- As the 5th largest economy, India's aspiration must be to compete on innovation with the top ten economies.
- India entered the top 50 innovating countries for the first time in 2020 since the inception of the Global Innovation Index (GII) in 2007, by improving its rank from 81 in 2015 to 48 in 2020.
- The business sector in India contributes much less to gross expenditure on R&D (about 37 per cent) when compared to businesses in each of the top ten economies (68 per cent on average). This is despite the fact the tax incentives for R&D were more liberal in India when compared to those in the top ten economies.
- The Government does a disproportionate amount of heavy-lifting on R&D by contributing 56 per cent of the gross expenditure on R&D, which is three times the average contributed by governments in the top ten economies.
- Indian business sector's contribution to the total R&D personnel (30 per cent) and researchers (34 per cent) in the country is the second lowest amongst the top ten economies (over 50 per cent on average).
- Indian residents contribute only 36 per cent of patents filed in India as compared to 62 per cent on average in the top ten economies. Indian firms also perform below expectation on innovation for their level of access to equity finance, which is the most crucial for innovation.
- India must significantly ramp up investment in R&D if it is to achieve its aspiration to emerge as the third largest economy in terms of GDP current US$.

Source: https://www.indiabudget.gov.in/economicsurvey/

CH 9 - JAY HO: AYUSHMAN BHARAT'S JAN AROGYA YOJANA (JAY) AND HEALTH OUTCOMES

As healthcare represents a critical public good, successive governments have committed to achieve universal health coverage (UHC).

Key Points

- As free markets under-provision public goods, a vital role of a government is to provide public goods to its citizens, especially to the vulnerable sections in a society. While the rich can seek private alternatives, lobby for better services, or if need be, move to areas where public goods are better provided for, the poor rarely have such choices.
- PMJAY is being used significantly for high frequency and low cost care consisting with the general utilisation of healthcare services. Using the distribution of claims, we find that the distribution is a long-tailed one that peaks in the range of INR 10,000-15,000. The scheme provides for healthcare of up to INR 5 lakh per family per year on a family floater basis, which means that it can be used by one or all members of the family. The scheme provides for secondary and tertiary hospitalization through a network of public and empanelled private healthcare providers. General medicine – the overwhelmingly major clinical specialty accounting for over half the claims - exhibited a V-shaped recovery after falling during the lockdown and reached pre-COVID-19 levels in December 2020.
- Across all the states, the proportion of households with health insurance increased by 54 per cent for the states that implemented PM-JAY while falling by 10 per cent in states that did not. The comparison reflects significant improvements in several health outcomes in states that implemented PM-JAY versus those that did not. Relative to states that did not implement PM-JAY, states that adopted it experienced greater penetration of health insurance, experienced a reduction in infant and child mortality rates, realized improved access and utilization of family planning services, and greater awareness about HIV/AIDS.

Source: https://www.indiabudget.gov.in/economicsurvey/

CH 10 - THE BARE NECESSITIES

There should be effective targeting of the needier population be they in urban or rural areas or across states.

Key Points

- Access to “the bare necessities” such as housing, water, sanitation, electricity and clean cooking fuel are a sine qua non to live a decent life.
- Bare Necessities Index (BNI) summarises 26 indicators on five dimensions viz., water, sanitation, housing, micro-environment, and other facilities. The BNI has been created for all states for 2012 and 2018 using data from two NSO rounds viz., 69th and 76th on Drinking Water, Sanitation, Hygiene and Housing Condition in India. Compared to 2012, access to “the bare necessities” has improved across all States in the country in 2018. Access to bare necessities is the highest in the States such as Kerala, Punjab, Haryana and Gujarat while it is the lowest in Odisha, Jharkhand, West Bengal and Tripura.
- Access to “the bare necessities” has improved disproportionately more for the poorest households when compared to the richest households across rural and urban areas. The improvement in equity is particularly noteworthy because while the rich can seek private alternatives, lobby for better services, or if need be, move to areas where public goods are better provided for, the poor rarely have such choices.
- Government schemes, such as the Jal Jeevan Mission, SBM-G, PMAY-G, may design appropriate strategy to address these gaps to enable India achieve the SDG goals of reducing poverty, improving access to drinking water, sanitation and housing by 2030.

Source: https://www.indiabudget.gov.in/economicsurvey/