What recent data says about how our economy is doing

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While some headline economic indicators suggest a recovery, we must not overlook weaknesses in employment-intensive sectors and still-worrisome joblessness that point to persistent distress.

The official estimates of India’s gross domestic product (GDP) for the first quarter (Q1) of 2021-22, together with other recent information, enable us to form a fairly comprehensive picture of how India is doing and the outlook going forward on different aspects of the economy: growth, employment, inflation, investment, trade, and so on.

The second wave of covid was four times worse than the first wave in terms of peak levels of new daily cases and daily deaths. There was great concern about how it would impact economic activity. Hence, the high 20.1% growth registered during Q1 of 2021-22 brought great cheer all around. The high growth was no doubt helped by the absence of a stringent, nationwide lockdown as seen during the first wave. However, it largely reflected the base effect of the unprecedented 24.4% contraction during Q1 of 2020-21. The level of Q1 GDP in 2021-22 at ₹32 trillion was still nearly₹4 trillion less than the ₹36 trillion GDP registered during Q1 of 2019-20, the last normal year before the pandemic.

Since the contraction itself was reduced during the second, third and fourth quarters of 2020-21, the base effect will also be weaker in these quarters. Hence the year-on-year growth may be progressively lower during the next three quarters. By the end of the year, India’s GDP for 2021-22 will probably have just caught up with the 2019-20 level, with two years lost to the pandemic. If the Reserve Bank of India’s (RBI) forecast of 9.5% growth in 2021-22 turns out to be correct, the level of output might even be a little higher than it was in 2019-20. But that assumes no major adverse impact of a third covid wave, an optimistic assumption.

Underlying the aggregate Q1 growth rates, there are significant inter-sectoral variations. Agriculture was not much affected by the pandemic. It grew by 3.5% during Q1 last year and 4.5% in Q1 this year. With the rainfall deficit more or less made up by now, we can expect a normal rabi harvest and annual agricultural growth of around 4%. In industry, all sub-sectors registered very high growth during Q1, led by manufacturing and construction. However, the high growth rates again largely reflected the strong base effect of the huge contraction during

Q1 of 2020-21. The contraction was also very large in services, but less than in industry, hence the base effect in 2021-22 is also weaker. The output level of the services-sector is trailing well behind that of 2019-20's Q1, mainly on account of a shortfall of ₹2 trillion compared to Q1 of 2019-20 in the sub-sector 'trade, hotels, transport, communications & broadcasting' (THTC).

The slow recovery of THTC is particularly concerning because this is an employment-intensive sub-sector, with many of the employed comprising low-wage, informal workers who have been hit hardest by the pandemic. At the aggregate level, the Centre for MonitoringIndian Economy data, as of 13 September, indicates that India's unemployment rate is still hovering around 8%, with the urban rate even higher at over 9%. In some states, the unemployment rates are astonishingly high: 36% in Haryana and 27% in Rajasthan, for example. Thus, the prevailing level of distress is not difficult to imagine, even though high-frequency indicators suggest that economic recovery has been sustained even during Q2 inmost sub-sectors of industry and services.

On the prices front, the wholesale price index (WPI) is now rising at the double-digit inflation rate of 11.4% year-on-year. The headline consumer price Index (CPI) inflation rate and core CPI inflation (excluding food and fuel) are significantly lower but close to the RBI target ceiling of 6%. RBI is confident that the price situation will ease. Hopefully, it is right.

Because if inflationary pressures persist while the output level is yet to catch up with the pre-pandemic level two years ago, that will make macroeconomic policy very challenging.

India's growth outlook going forward will depend on some key drivers. A rise in the investment rate from 24% to 32% of GDP marks a revival of the investment cycle, and it has to be sustained. Consumption demand is still trailing the 2019-20 level and this too needs urgent revival. For this to happen, the compression of government expenditure needs to be reversed during the rest of the year, keeping in view the buoyant growth of tax revenues (including GST). In this context, expenditure by state governments, which is collectively much larger than central government expenditure but subject to hard budget constraints, is even more important than central expenditure. Despite a rapid rise in revenues, governments may still need large borrowings. Hence, RBI will need to maintain its accommodative monetary policy stance, but this needs to be carefully calibrated to ensure that inflation is contained within its target band. Finally, robust global growth, especially for India's major trade partners, is essential to sustain high export growth and turn the trade deficit around.

I have emphasized demand-side factors because recent data sets do not point to any critical supply-side bottlenecks at the present juncture. However, there is still the risk of a third covid wave. To minimize that risk, an aggressive vaccination drive will remain the most critical determinant of an economic revival.

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