

Economic Survey 2016-17 Volume 2
An Overview

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Why Volume 2, Why Now?

- Before this year, two volumes were released on the day before the Budget
 - Volume 1 was analytical and policy and ideas-oriented
 - Volume 2 featured a sectoral review and included historic data for first three quarters
- Pattern changed due to advancement of budget calendar
 - Split the release of two volumes
 - Only Volume 1 was released before the budget
 - Volume 2 to be released in July so that historic data covers the whole year
- Statistical Appendix (Historical Data) provided as Microsoft Excel files for ease of use

Survey Volume 2

1. State of the Economy: An Analytical Overview
2. Fiscal Developments
3. Monetary Management and Financial Intermediation
4. Price and Inflation
5. Climate Change, Sustainable Development and Energy
6. External Sector
7. Agriculture and Food Management
8. Industry and Infrastructure
9. Services Sector
10. Social Infrastructure, Employment and Human Development

Outline

- Encouraging developments for the medium term
- Deflationary impulses in the near term
- Outlook and policies

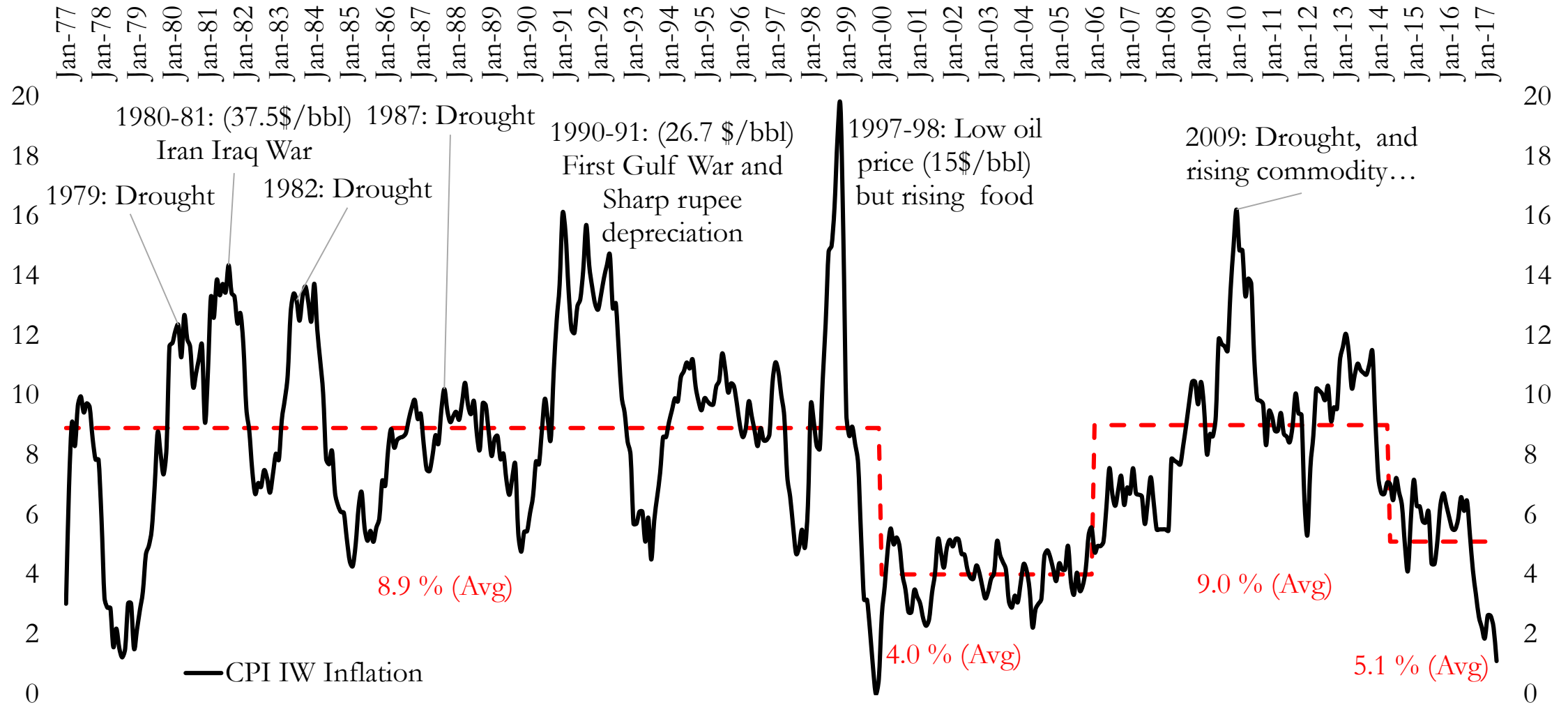
Encouraging (and Mixed) Developments

1. Rekindled optimism on structural reforms
2. Growing confidence that macro-economic stability – inflation and external balance – has become entrenched: Regime shift
3. Demonetization's long-term positive consequences
4. Demonetization's short-term costs
5. Extraordinary financial market confidence/exuberance

Encouraging Developments. Structural Reforms

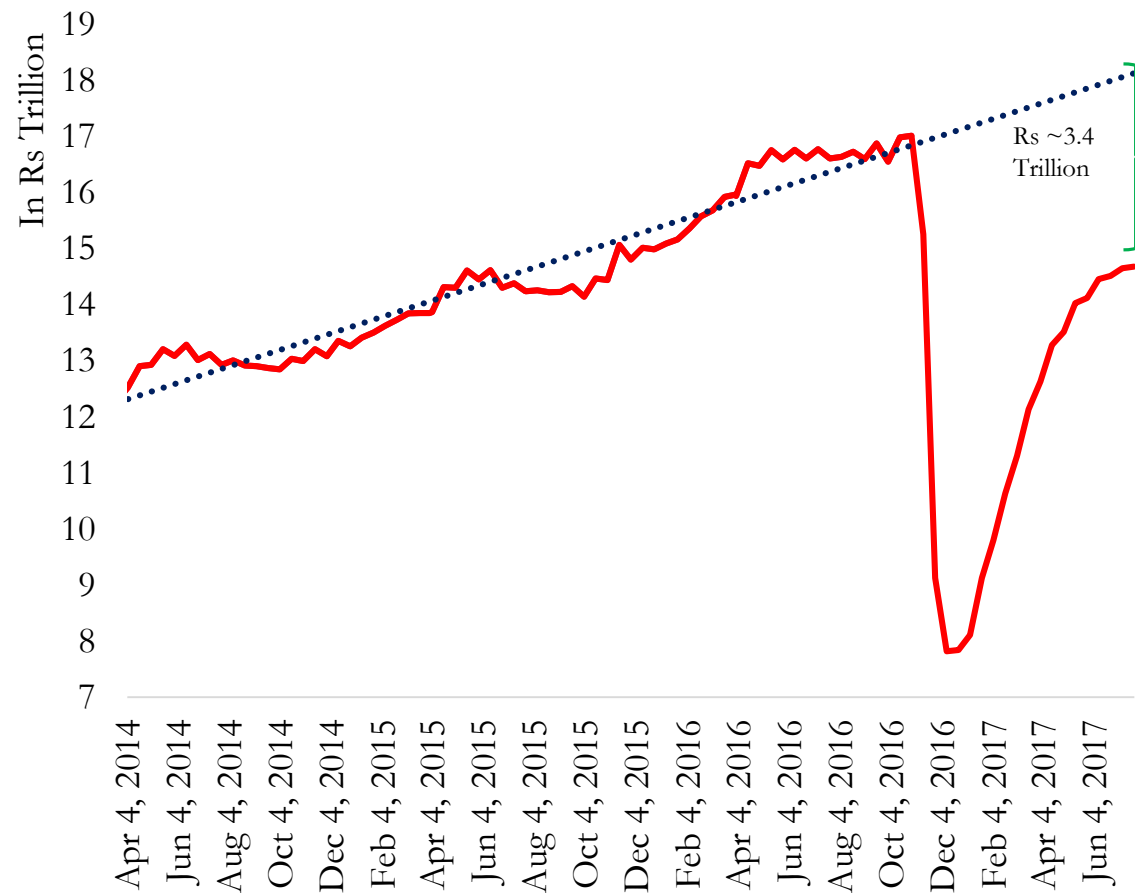
- Launch of the GST:
 - 13.5 lakh new registrants
- In-principle decision to privatize Air India
- Further rationalization of energy subsidies
- Actions to address the Twin Balance Sheet challenge

Encouraging Developments. Structural Downward Shift in Inflation: Changes in oil market and domestic agriculture

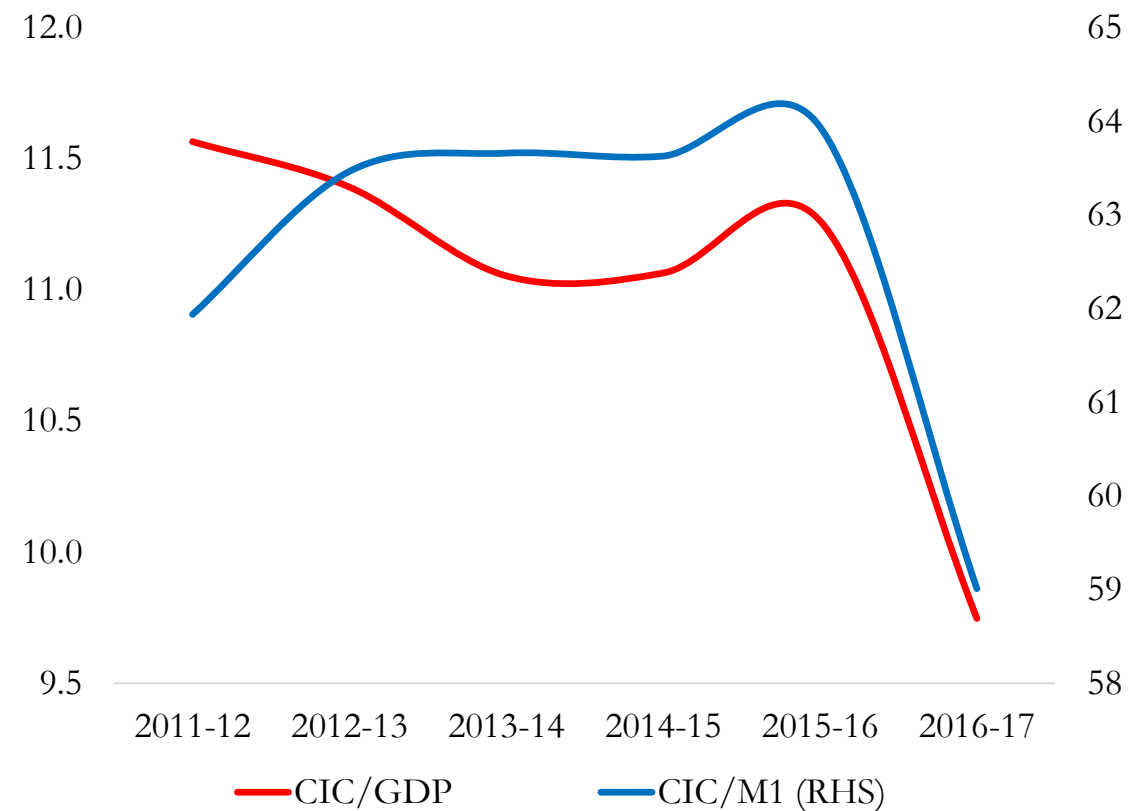


Encouraging Developments. Demonetization: Decline in equilibrium cash holdings

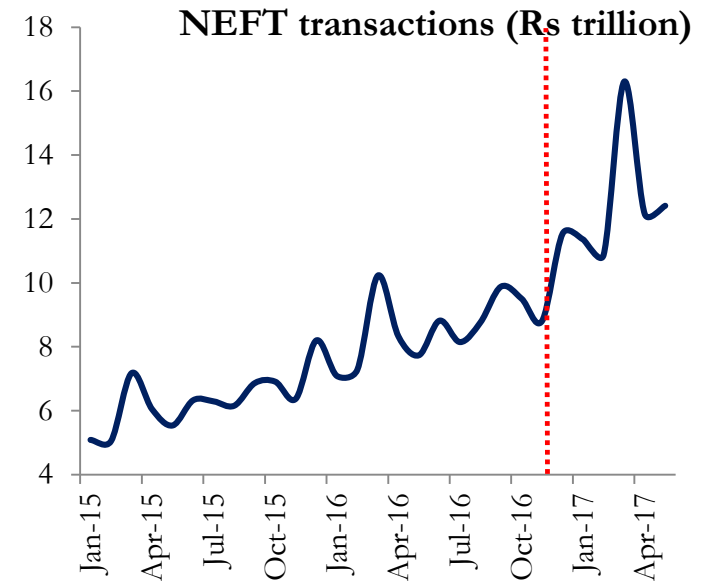
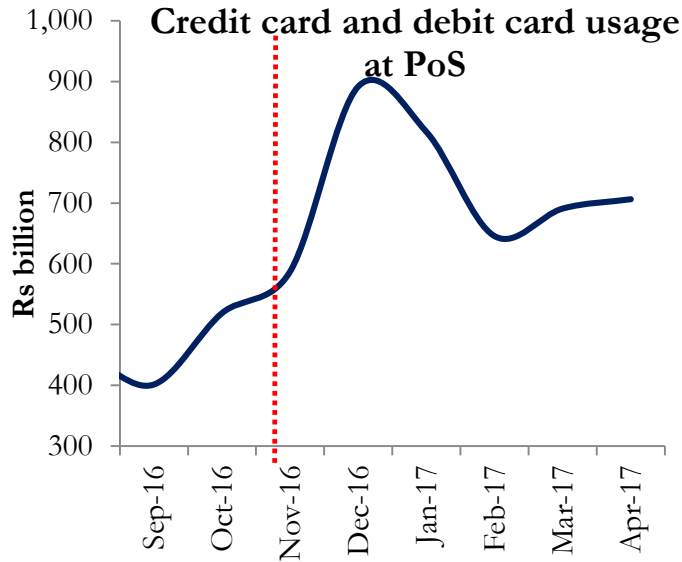
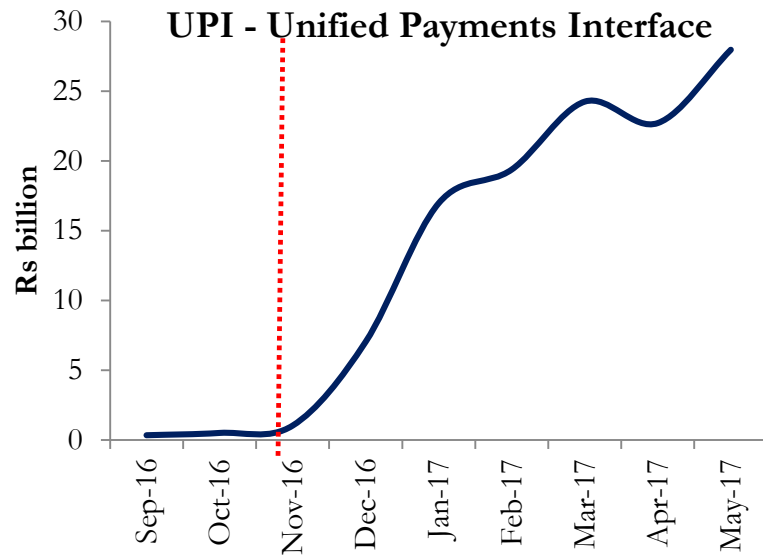
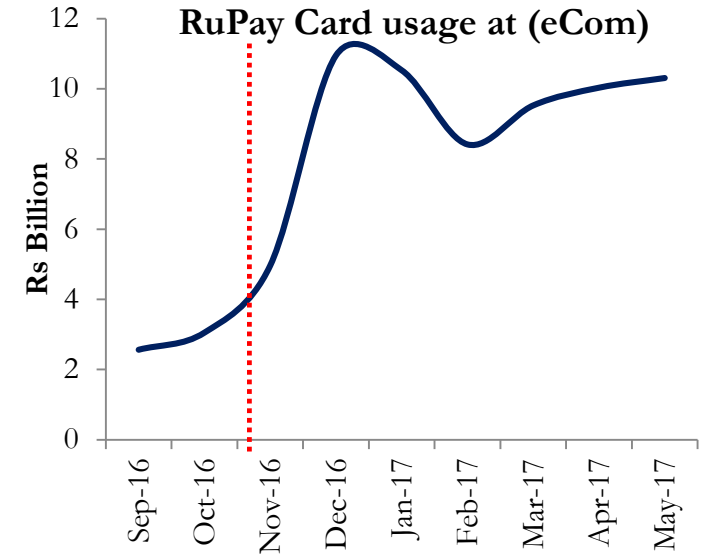
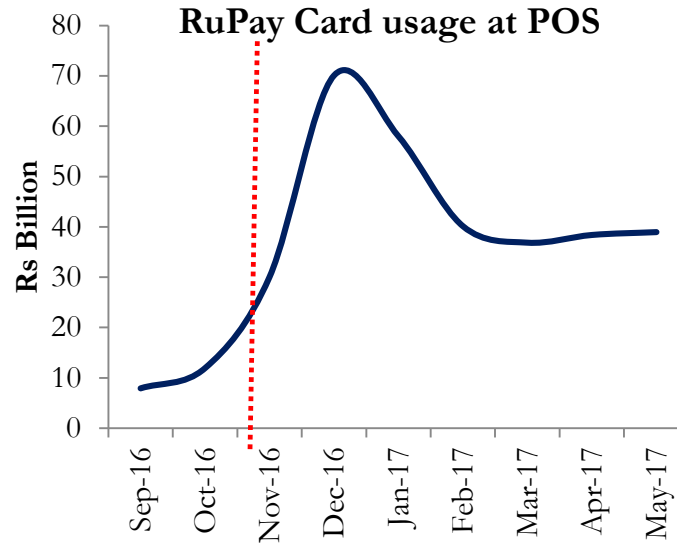
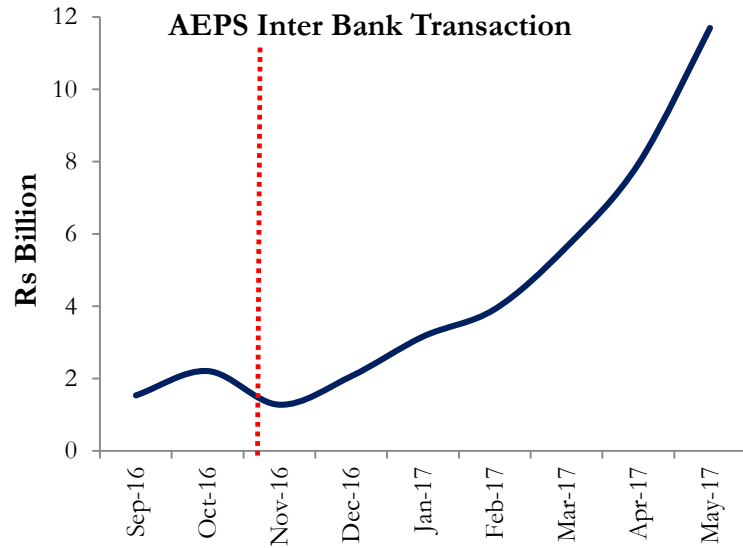
Cash Holdings



Currency in Circulation to GDP and M1



Encouraging Developments. Demonetization - Boost to digitalization for all users

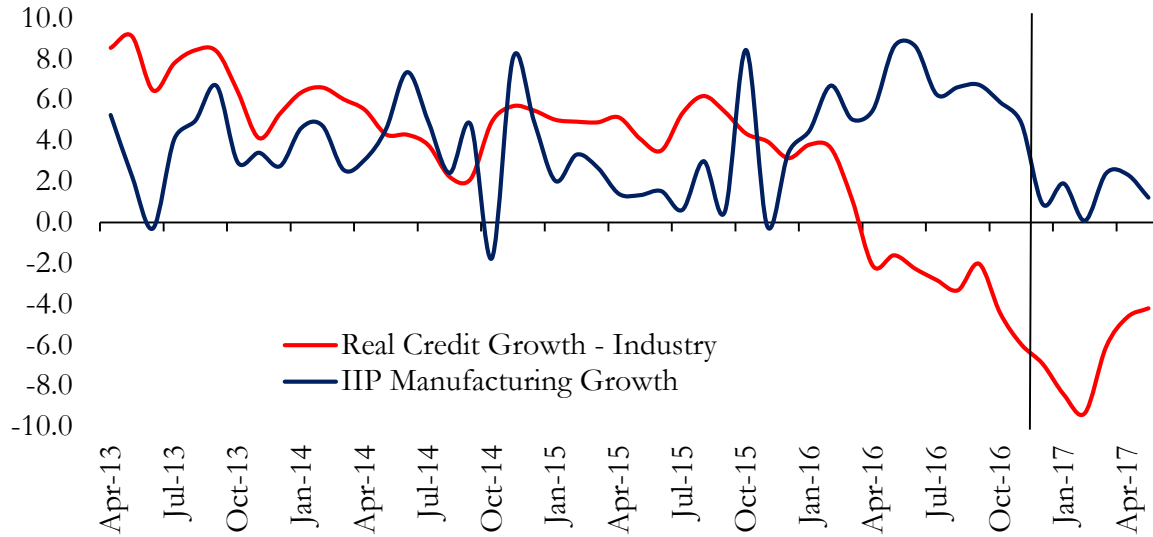


Encouraging Developments. Substantial increase in new tax payers

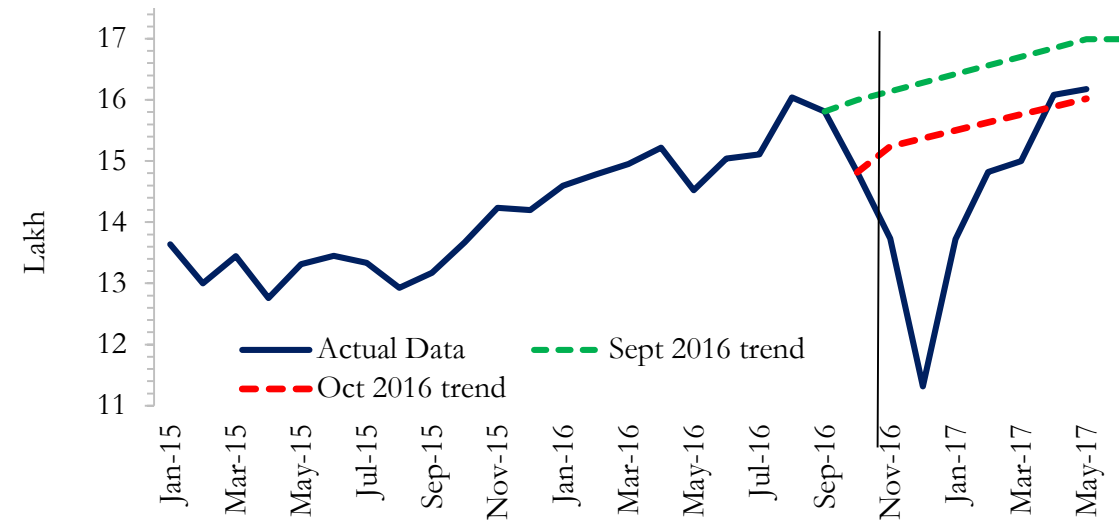
	FY: 2015-16	FY: 2016-17
Growth in New Tax Payers (%)	25.1	45.3
Possible additional taxpayers due to Demonetization (in Lakh) (calculated as excess over previous year's growth)		5.4
Growth in Returned Income (%)	38.6	54.3
Possible addition of Returned Income (in Crore)		10,587
Average Taxable Income (in Lakh)	2.5	2.7

Demonetization: Short term impacts on real economy and informal sector

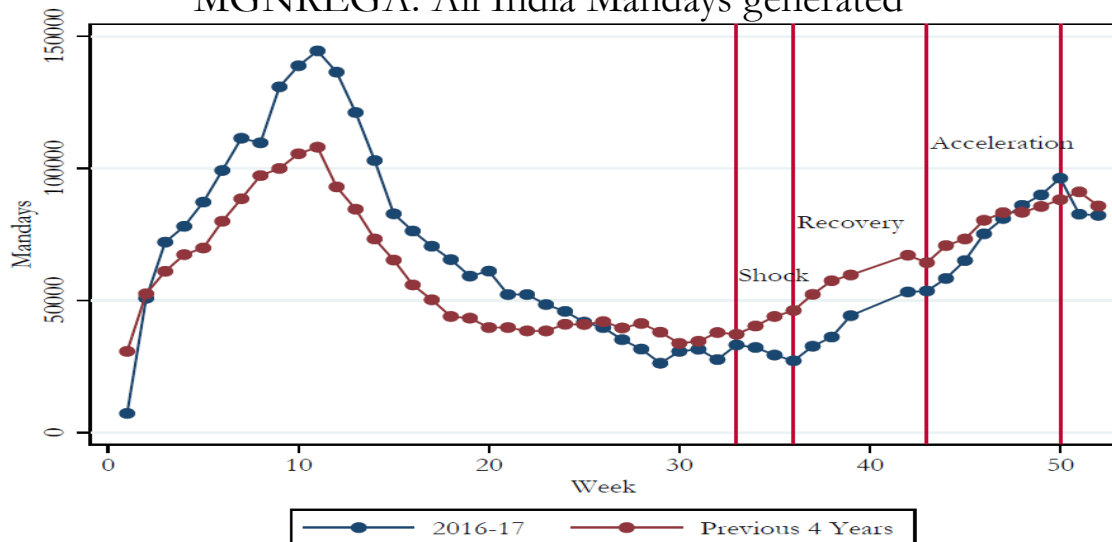
High Frequency Macro Economic Indicators



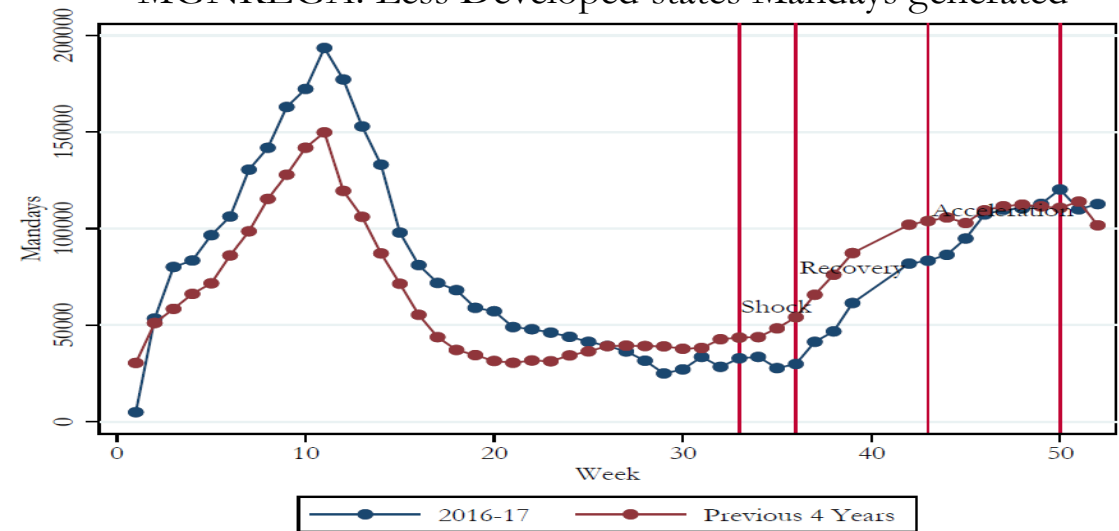
Number of Two Wheelers Sold in the Domestic Market



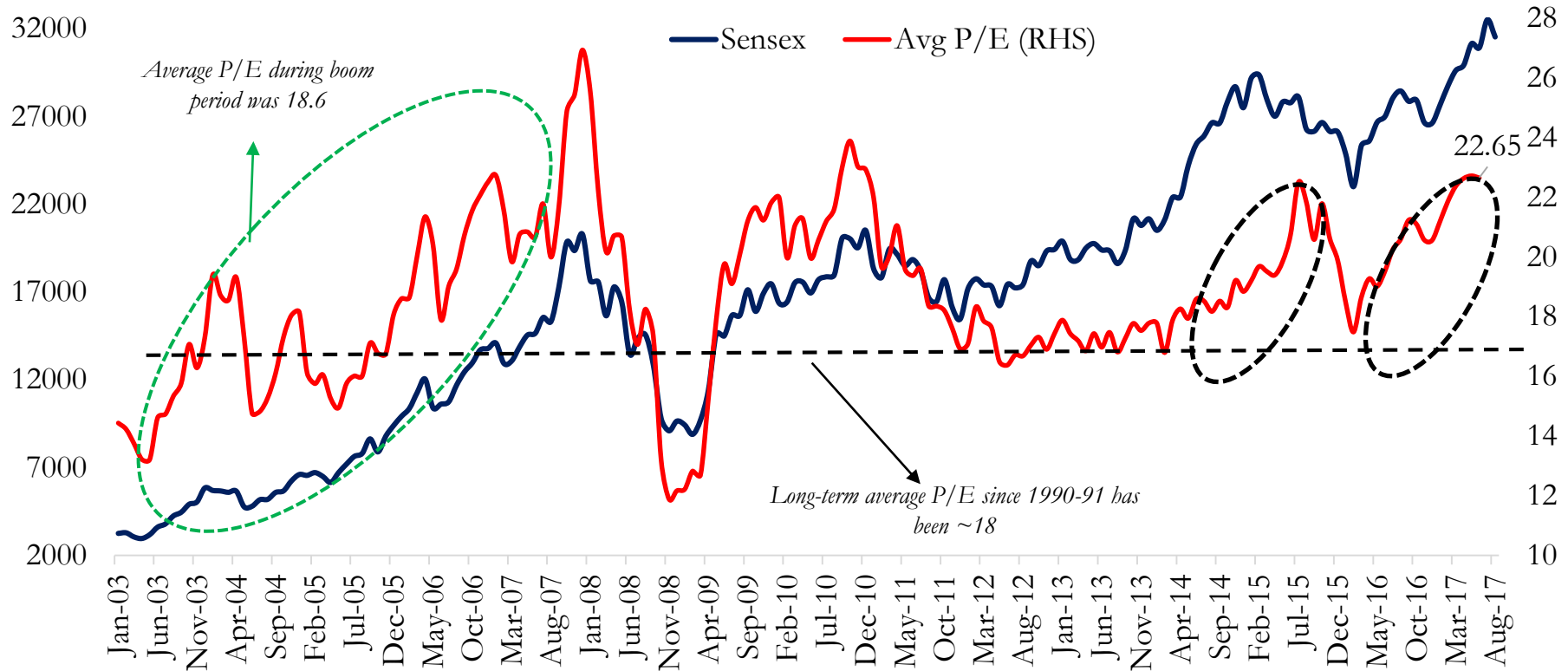
MGNREGA: All India Mandays generated



MGNREGA: Less Developed states Mandays generated



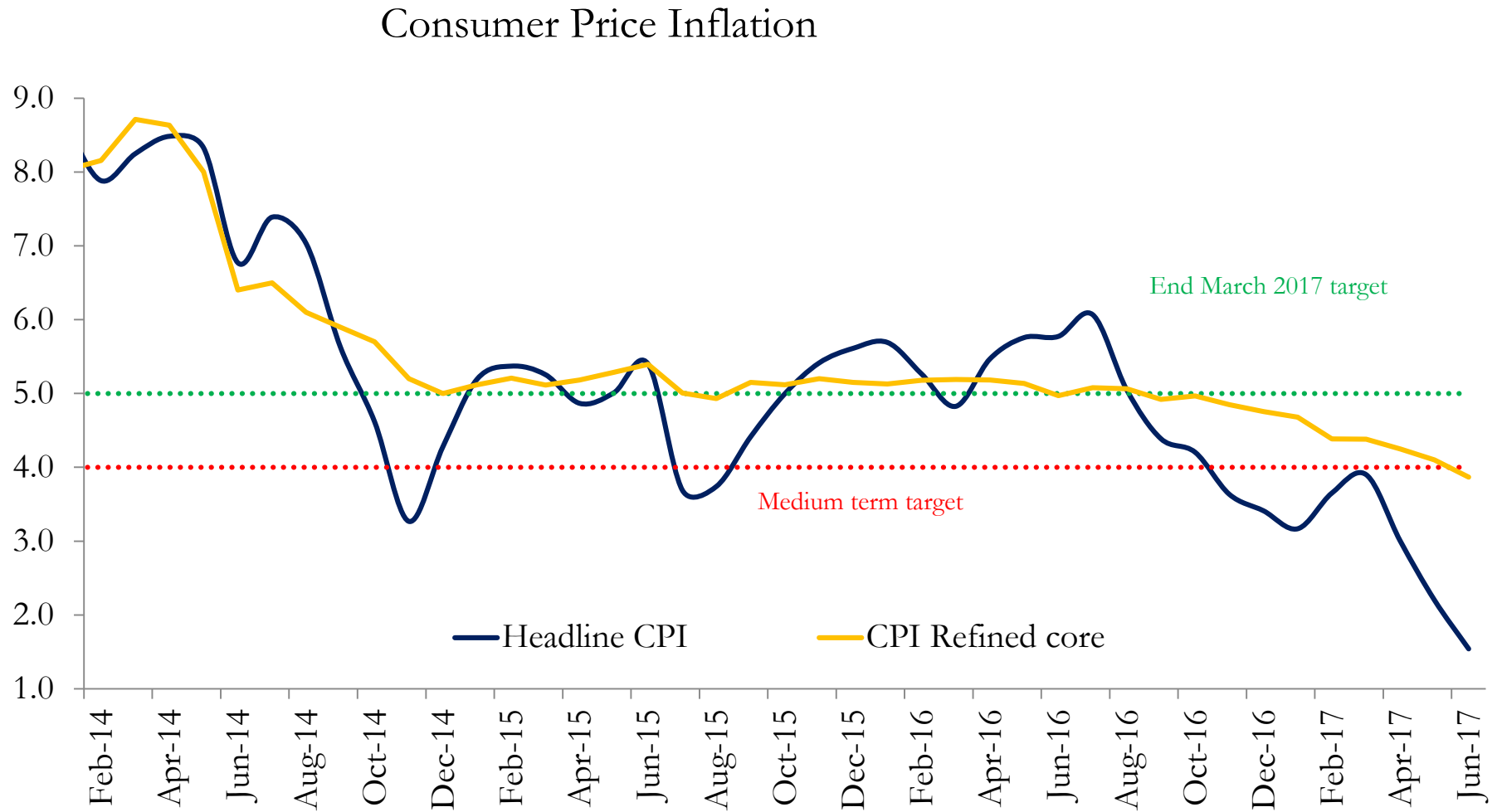
Encouraging Developments. Financial Markets exuberance decoupled from real economy related to international excess liquidity



Source: BSE, RBI

Deflationary Impulses: Outlook for Inflation and Growth

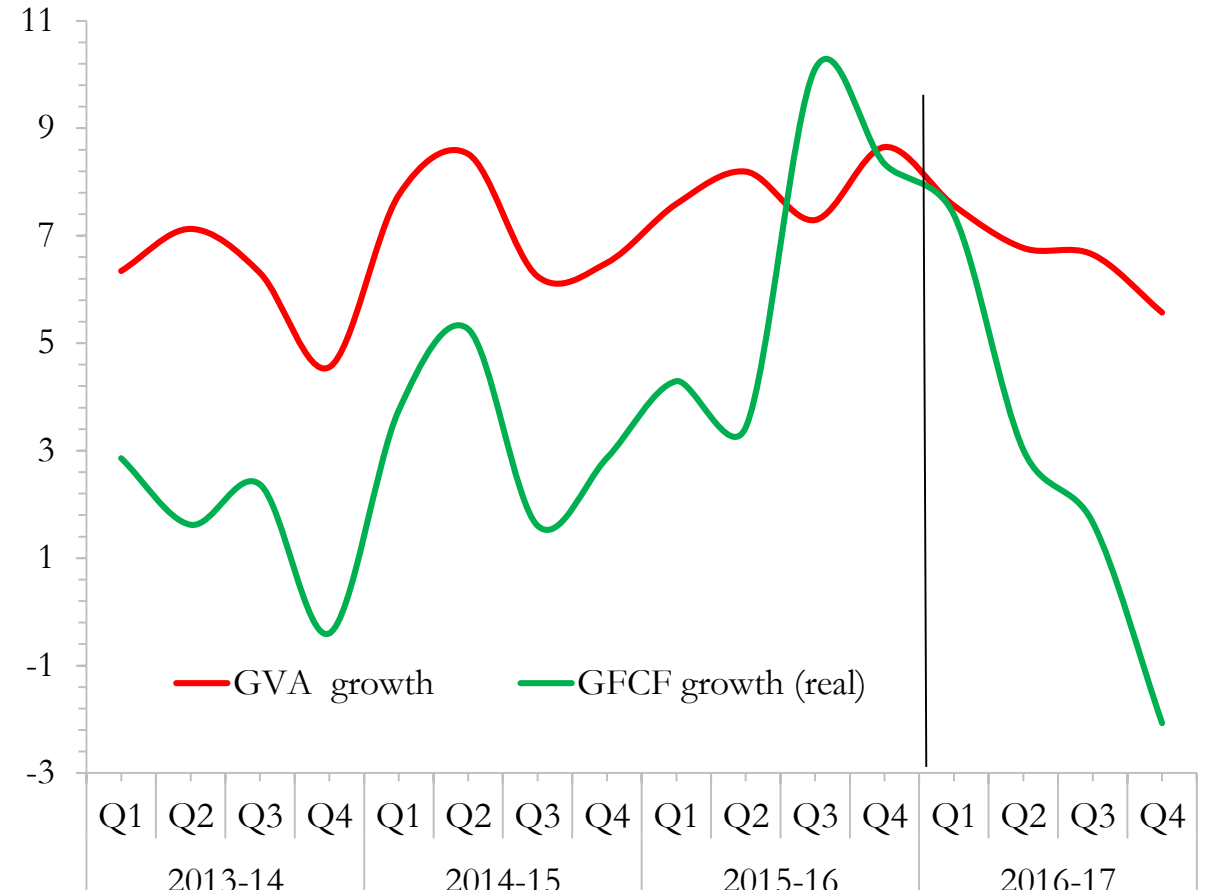
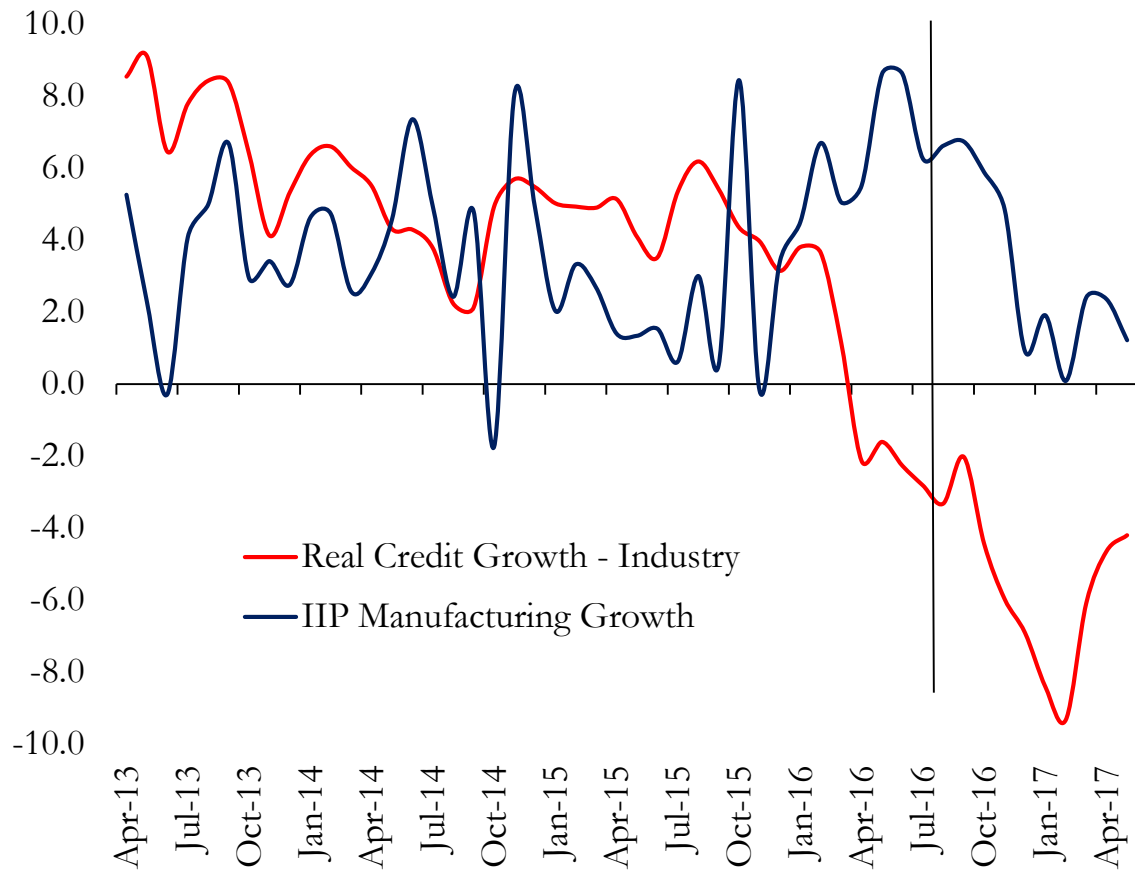
Inflation : Substantial overachievement



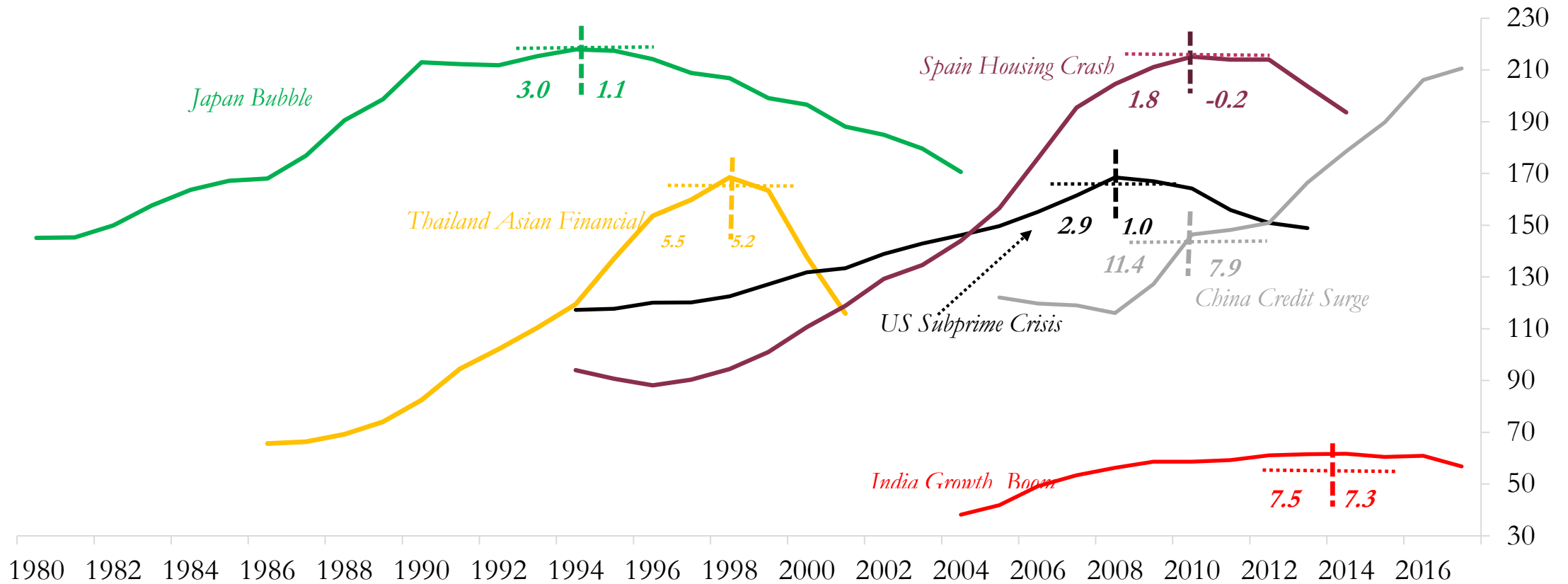
Inflation Outlook: Determining factors

- Outlook for capital flows and the exchange rate
 - Influenced by the outlook and policy in advanced economies, especially the US
- Recent nominal exchange rate appreciation
- Good monsoon but bottlenecks in fruits and vegetables
- Introduction of the GST
- 7th Pay Commission awards
- Farm loan waivers
- Output gap
- End-period inflation within target; average inflation below target

Growth: Across the board deceleration in real activity since Q2 FY 2017



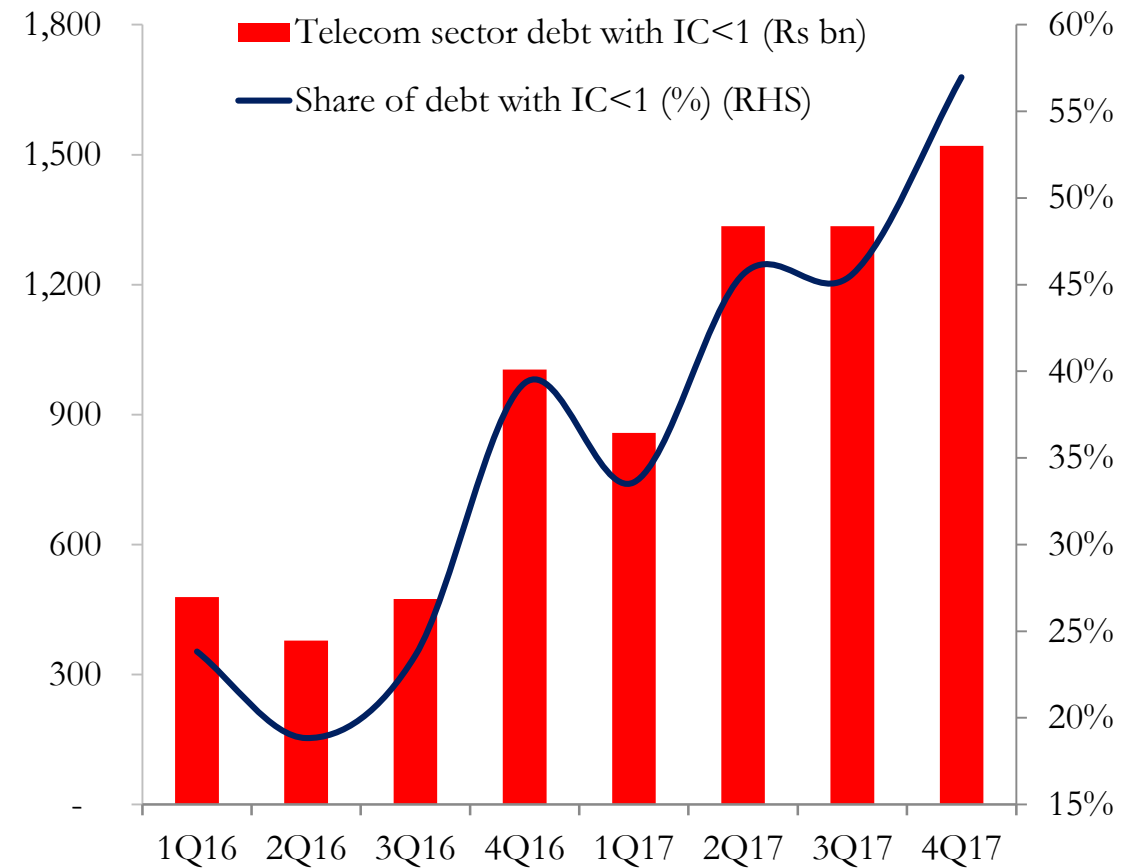
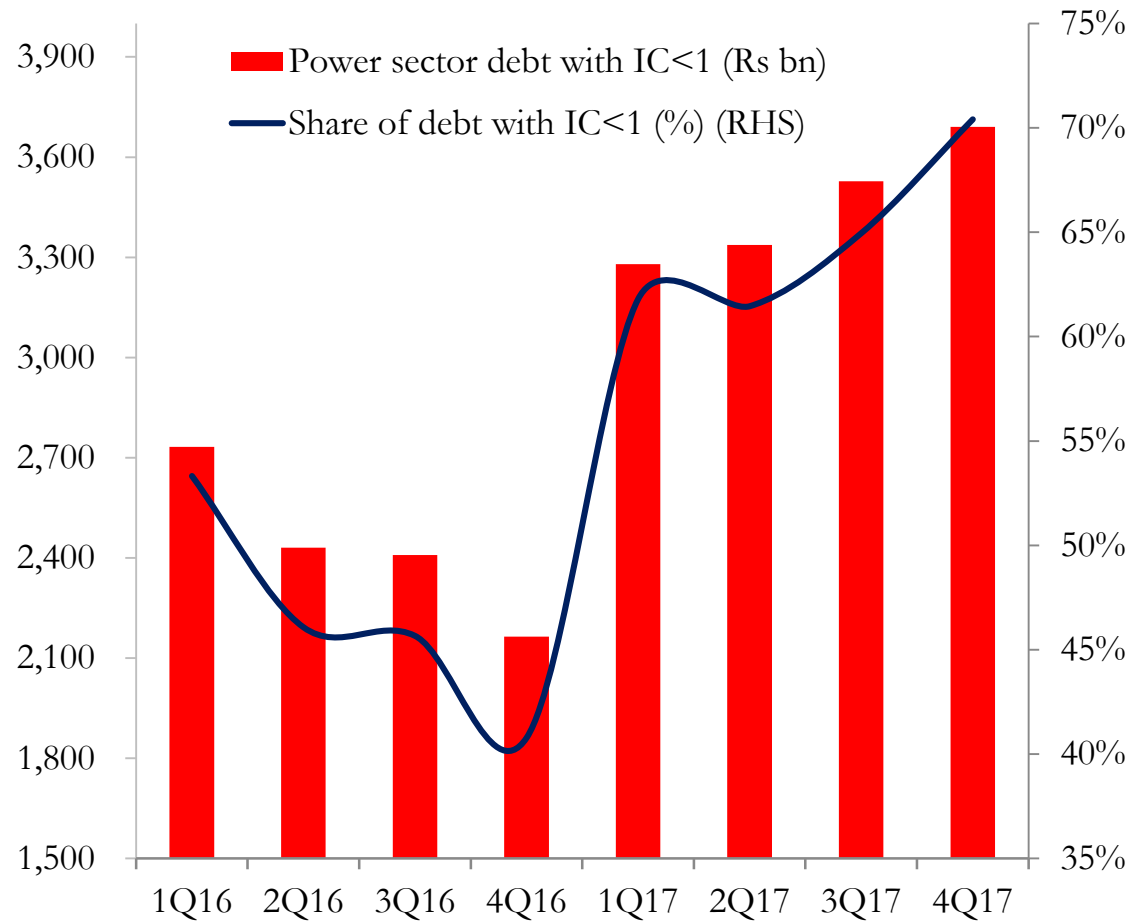
Growth outlook from a Twin Balance Sheet perspective: Need for deleveraging



Farm Loan Waivers: Deflationary not Inflationary

- Likely magnitude: 1.25 lakh crore- for states which have already announced; 2.7 lakh crore – if all states implement
- Deflationary because of FRLs of States: for example, UP has slashed capital expenditure to accommodate waiver
- Potential impact on demand: 58 thousand crore - states which have already announced; 1.14 lakh crore – if all states implement
- State fiscal impact: reduction by 0.35 percent of GDP - states which have already announced; reduction by 0.7 percent of GDP – if all states implements

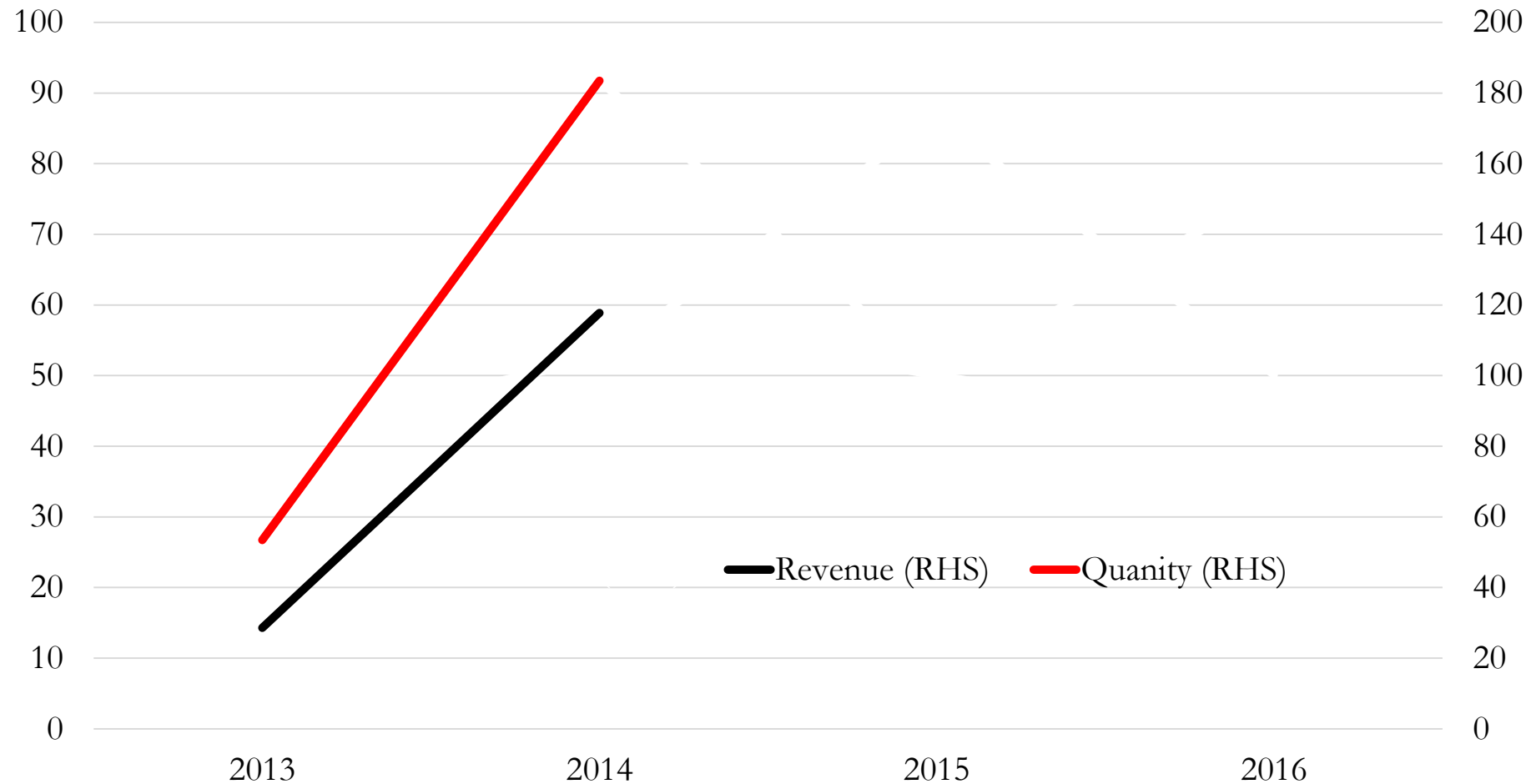
TBS: Rising Stress in Power and Telecom Sectors



Agriculture Puzzle: Reduced farm revenues in non-cereal crops despite good monsoon

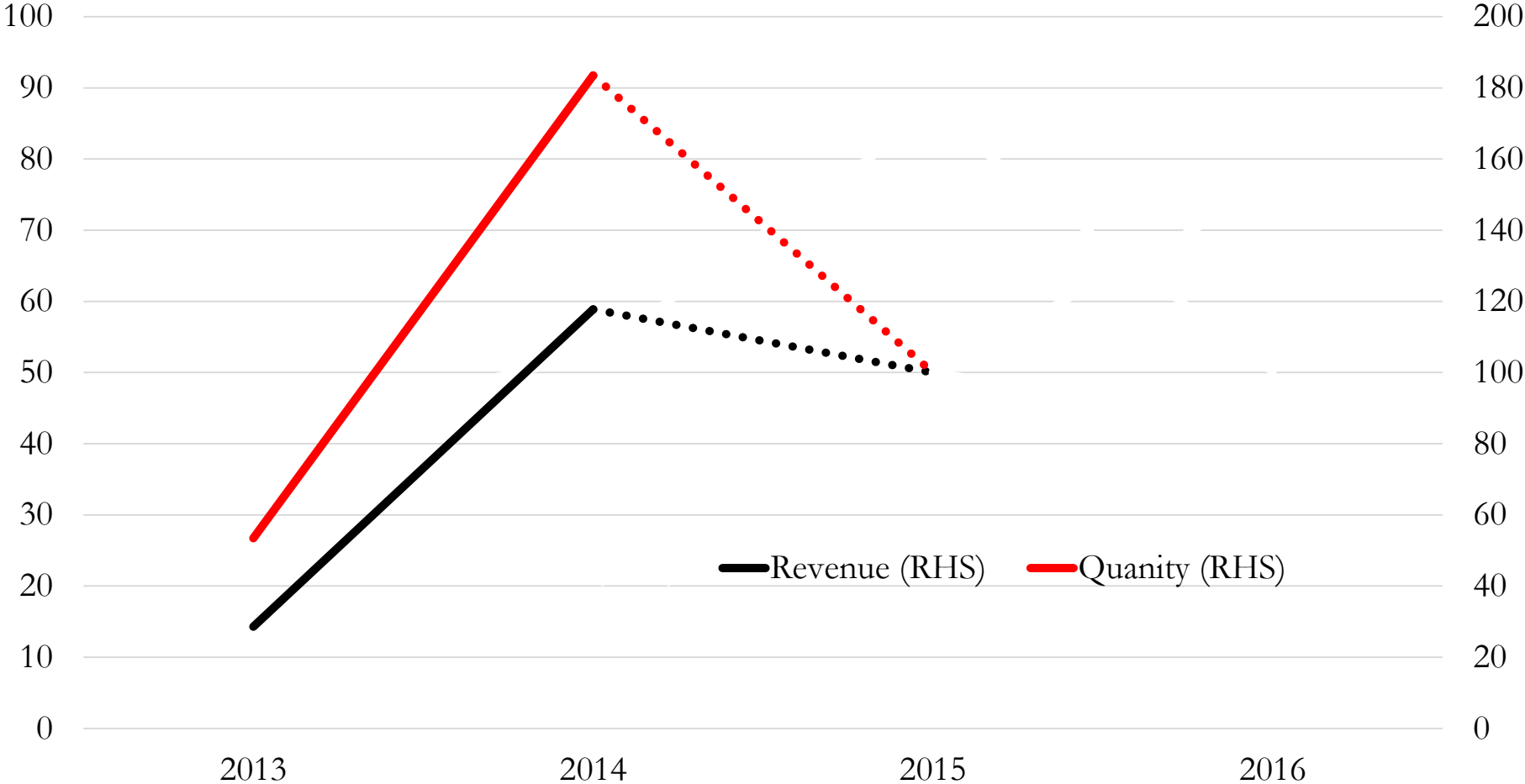
Revenue, Quantity and Price Movement of Arbar

Phase 1: As quantity goes up total revenue goes up



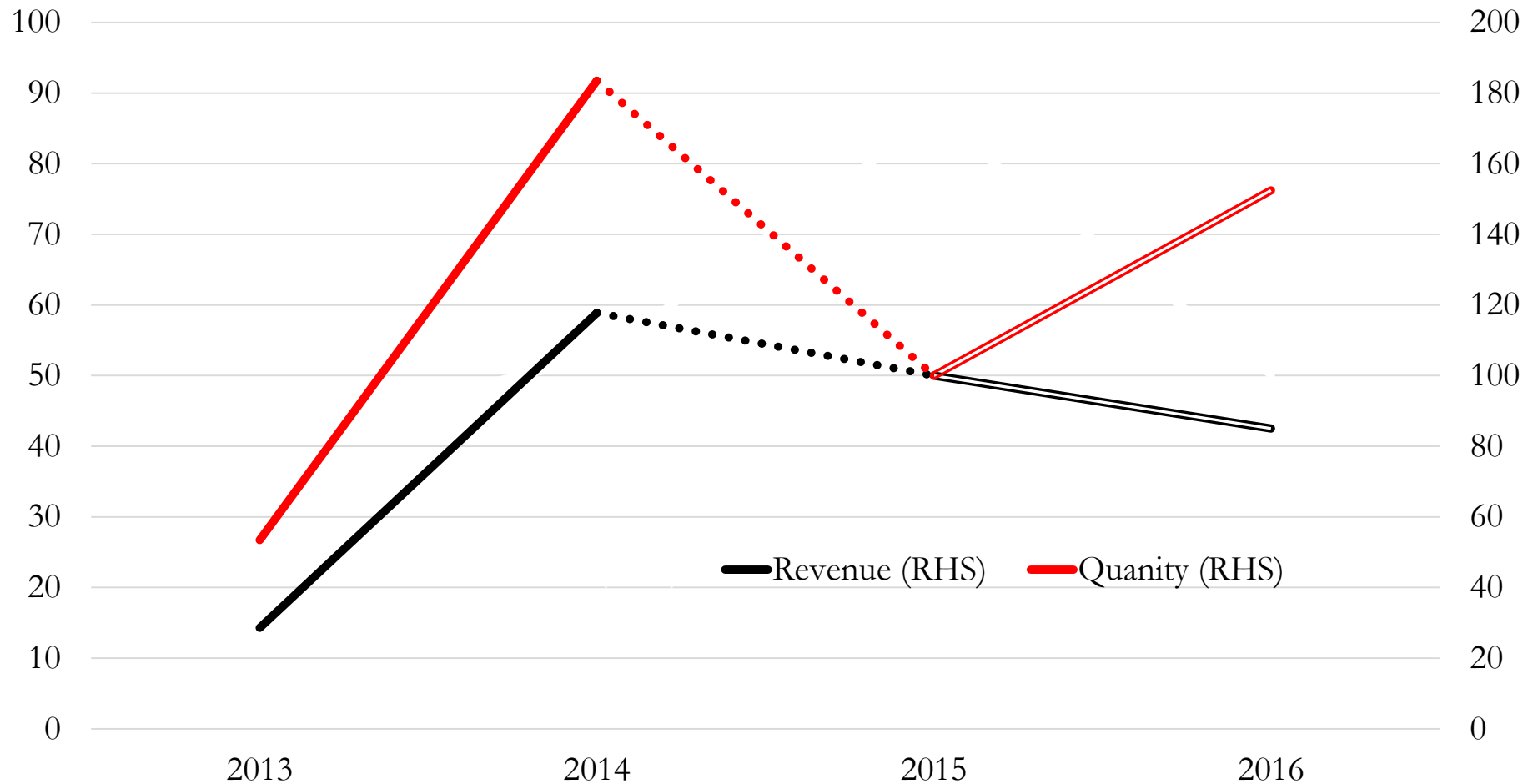
Revenue, Quantity and Price Movement of Arbar

Phase 2 : As quantity declines total revenue goes down



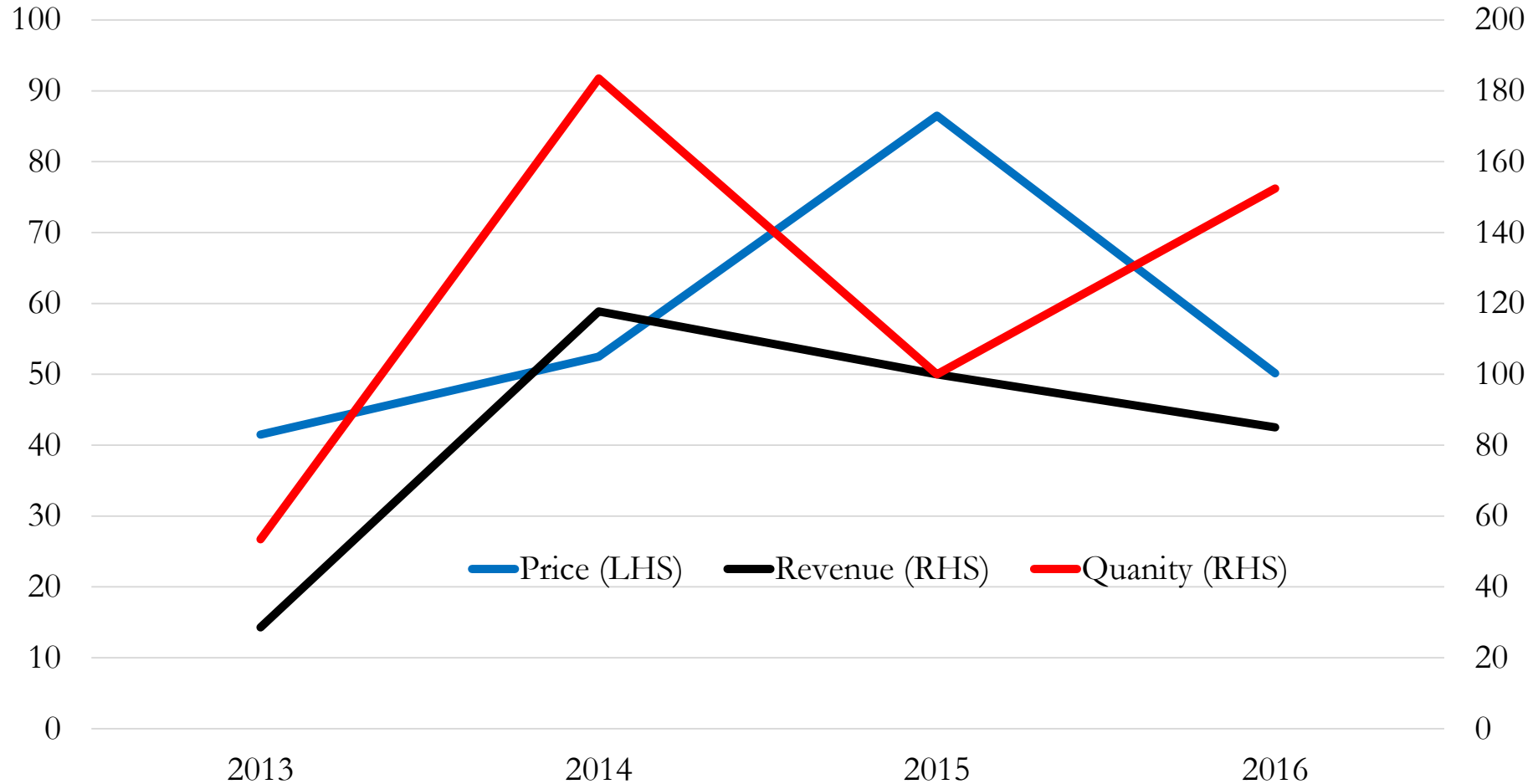
Revenue, Quantity and Price Movement of Arbar

Phase 3 : The relationship doesn't hold this year: Output up, revenue down

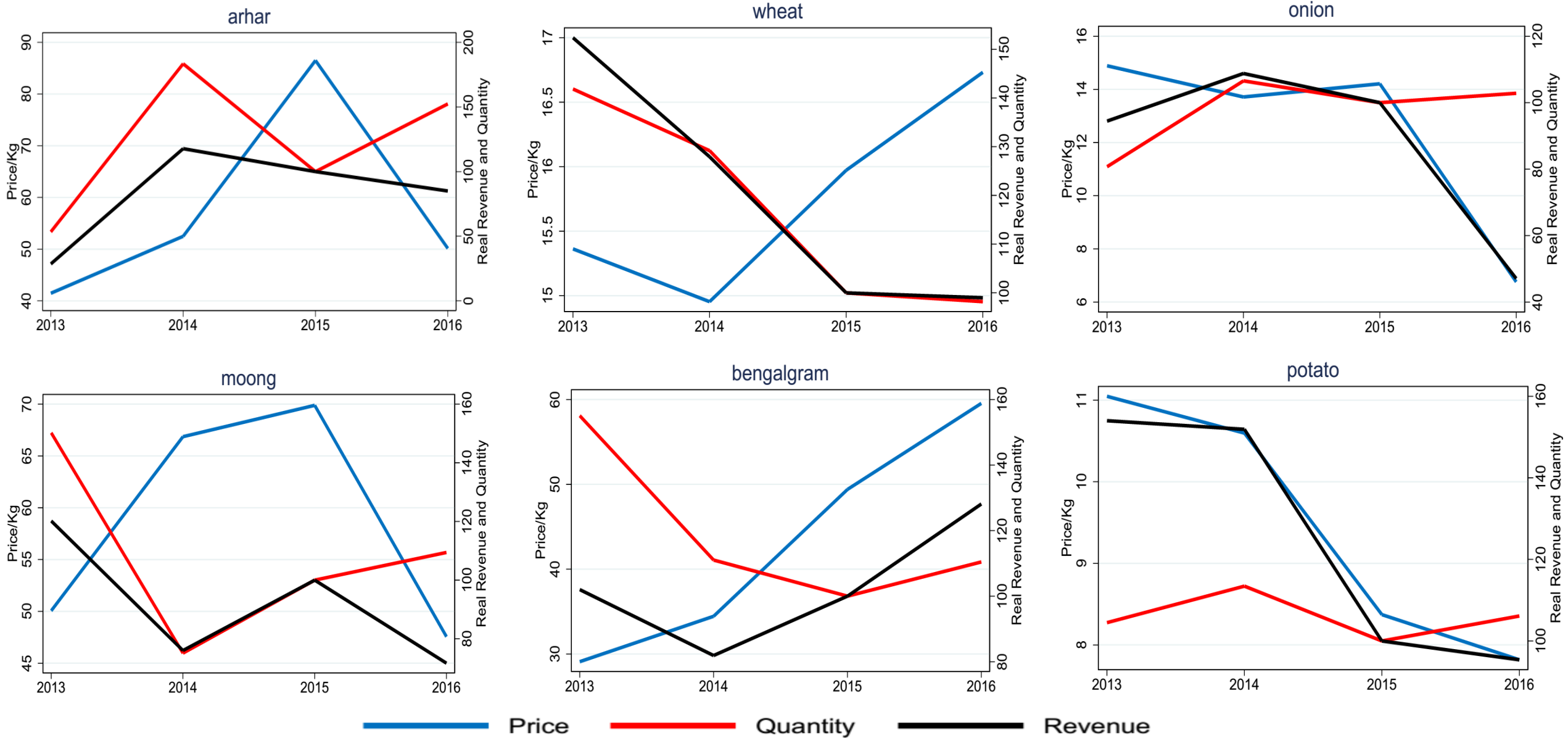


Revenue, Quantity and Price Movement of Arbar

The relationship doesn't hold because of sharp decline in prices

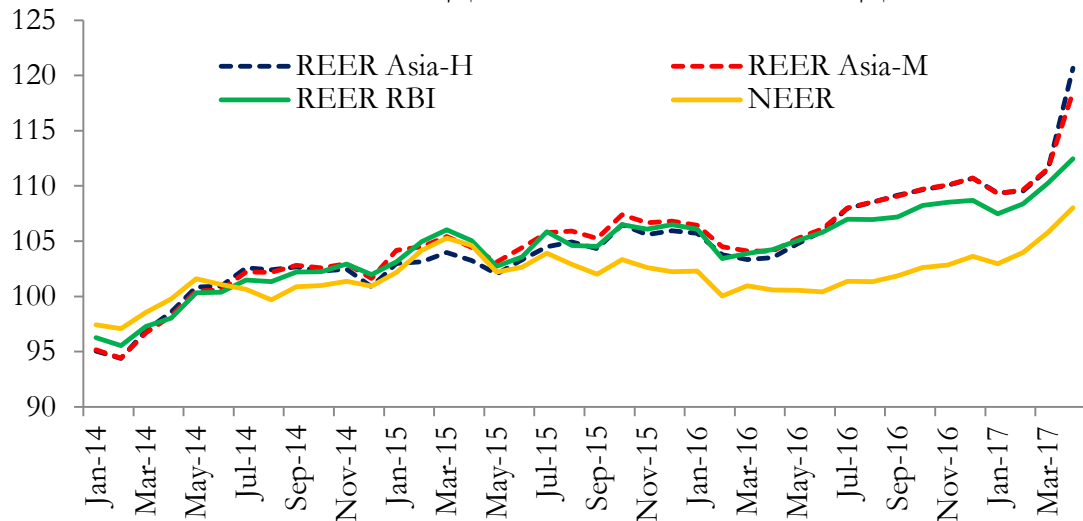
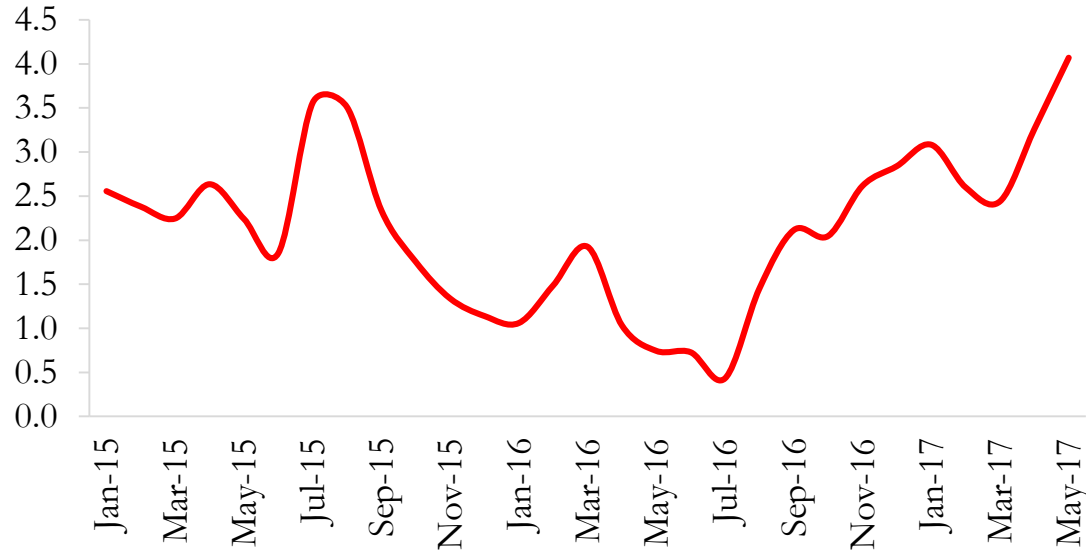


Selected Agricultural Commodities: Real Revenues, Quantities and Prices

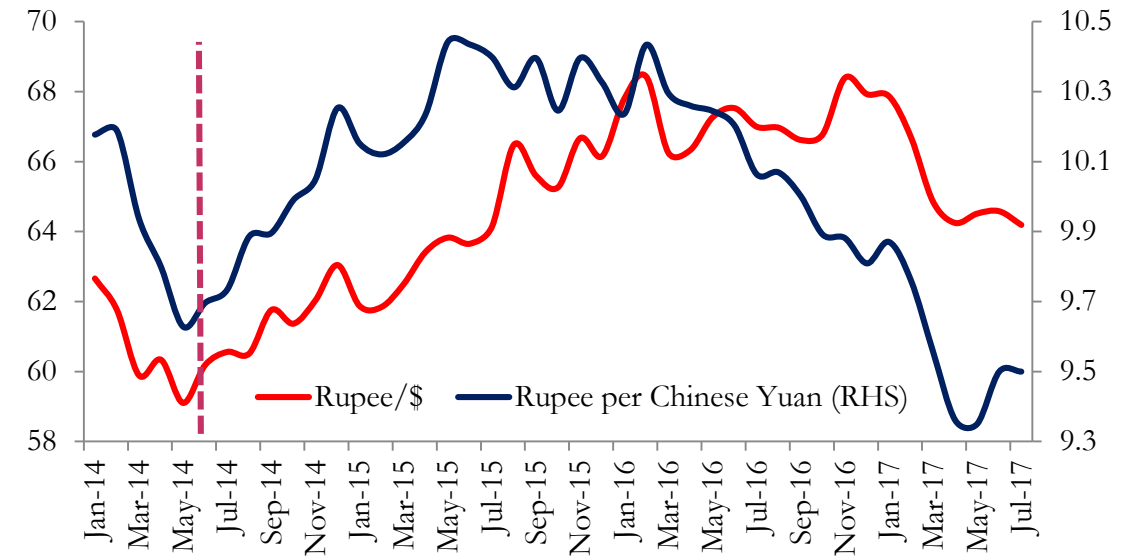
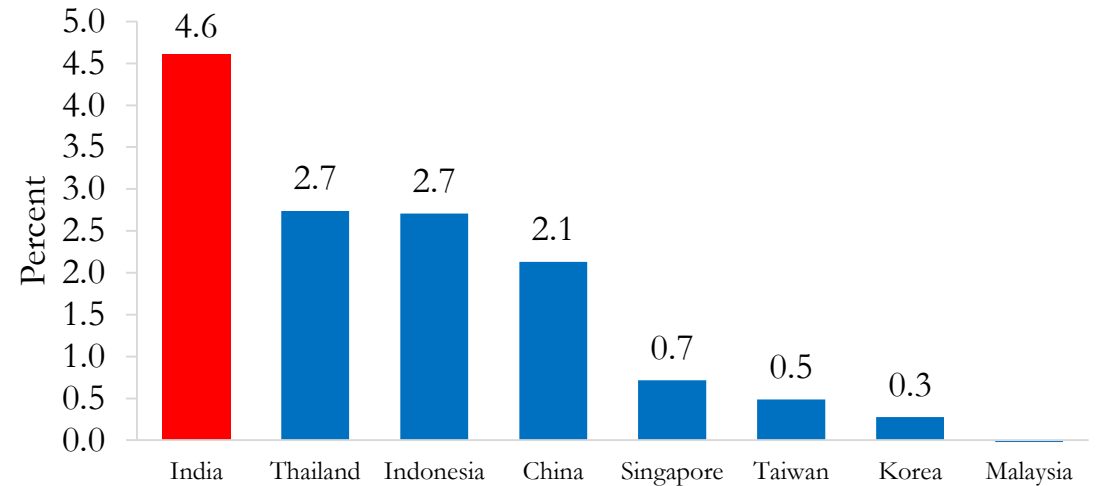


High real rates and deteriorating competitiveness

Real Interest Rate (per cent)



Cross-country Real Bond Yield (per cent) as of May 2017



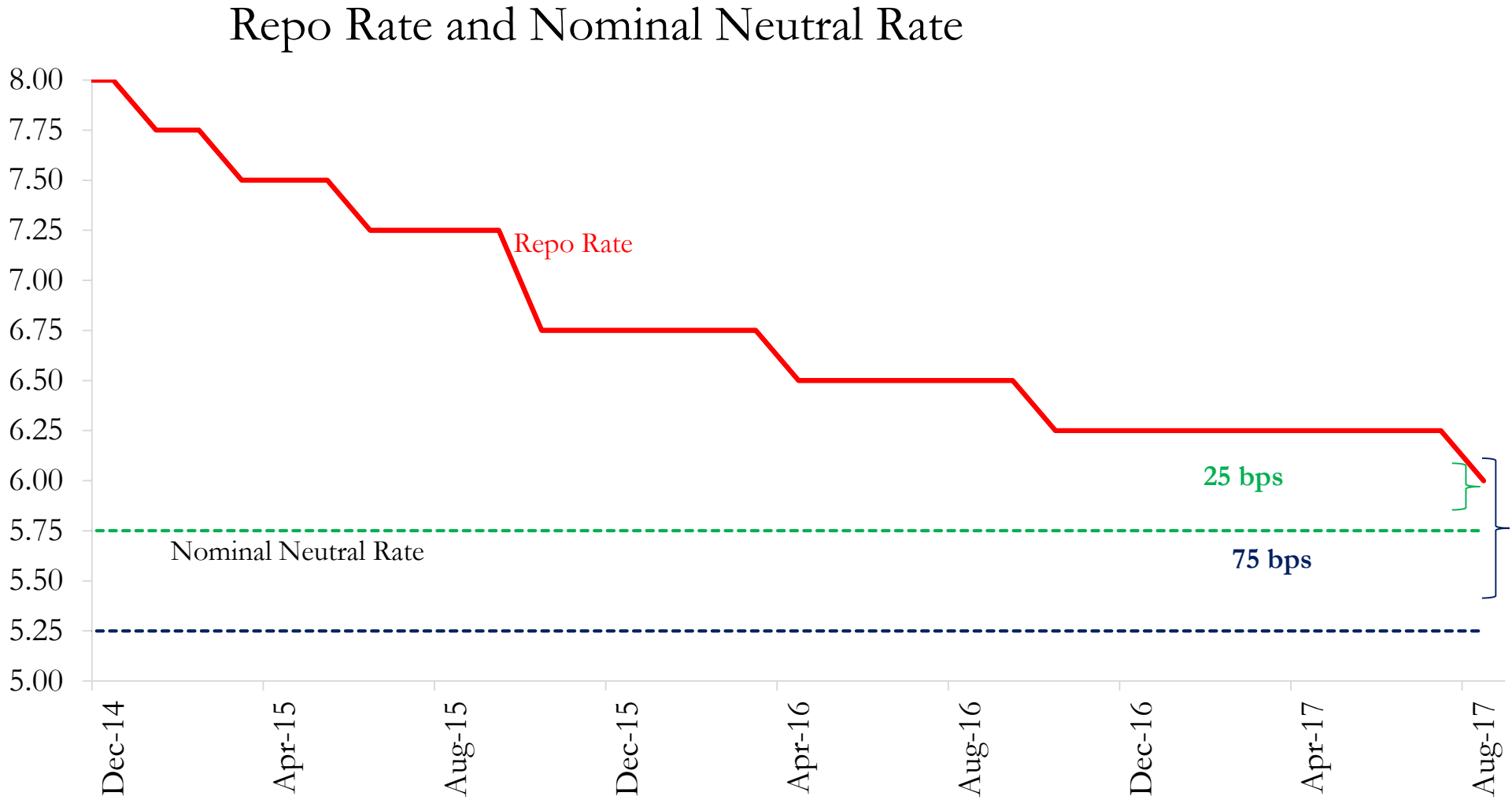
Growth Outlook: Summary

- Balance of risks to growth has shifted to the downside
- Balance of probability has correspondingly shifted away from the upper end of the growth forecast in February

Monetary policy: Technical assessment

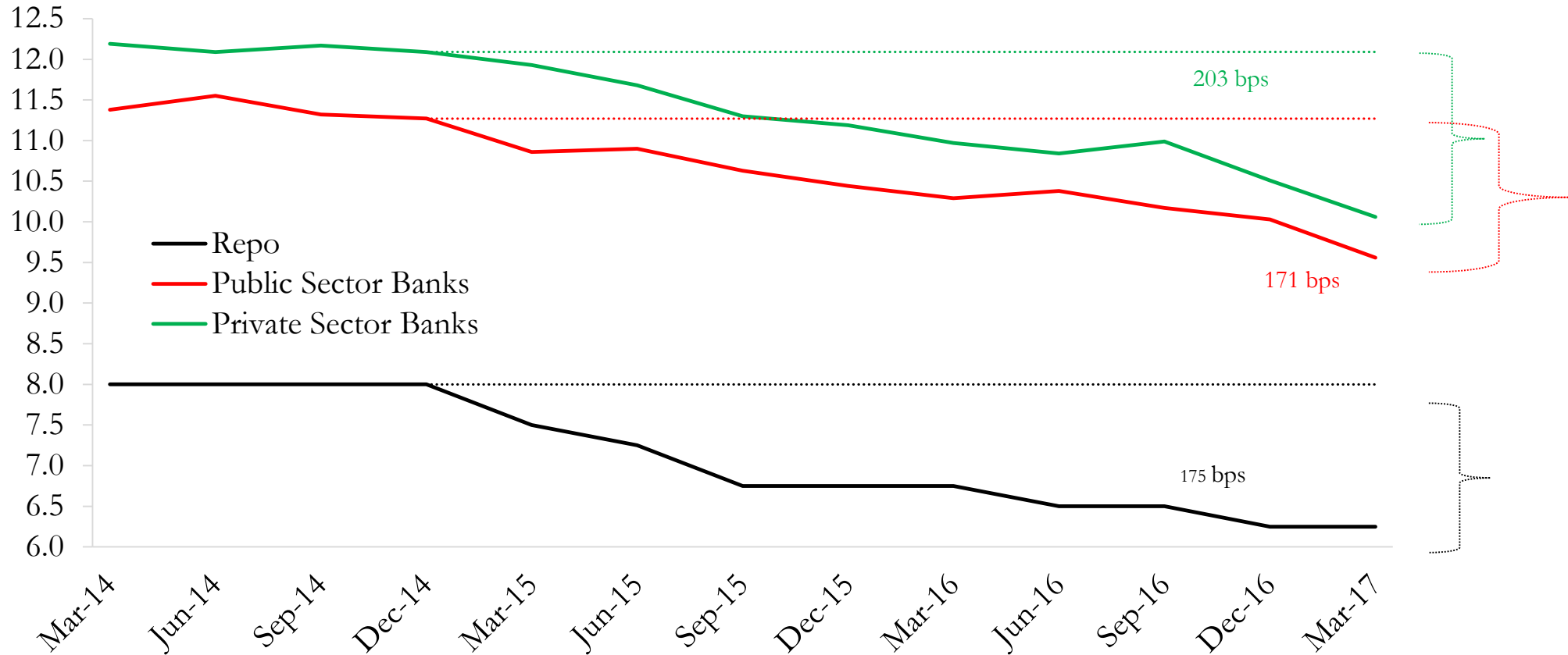
- Structural decline in inflation and inflation outlook create scope for lower rates
- Temporary factors reduce scope for lower rates
- Neutral nominal rates based on RBI studies of neutral real rates between 5.25 and 5.75 percent
- But economic cycle must be factored in (Taylor rule): if growth below potential and there is economic slack, actual rate must be below neutral

Monetary Policy: Technical assessment



Monetary Policy. Technical assessment: Policy cuts are reflected in incremental lending, especially private banks

Repo Rate and Bank Groupwise Weighted Average Lending Rates on Fresh Rupee Loans

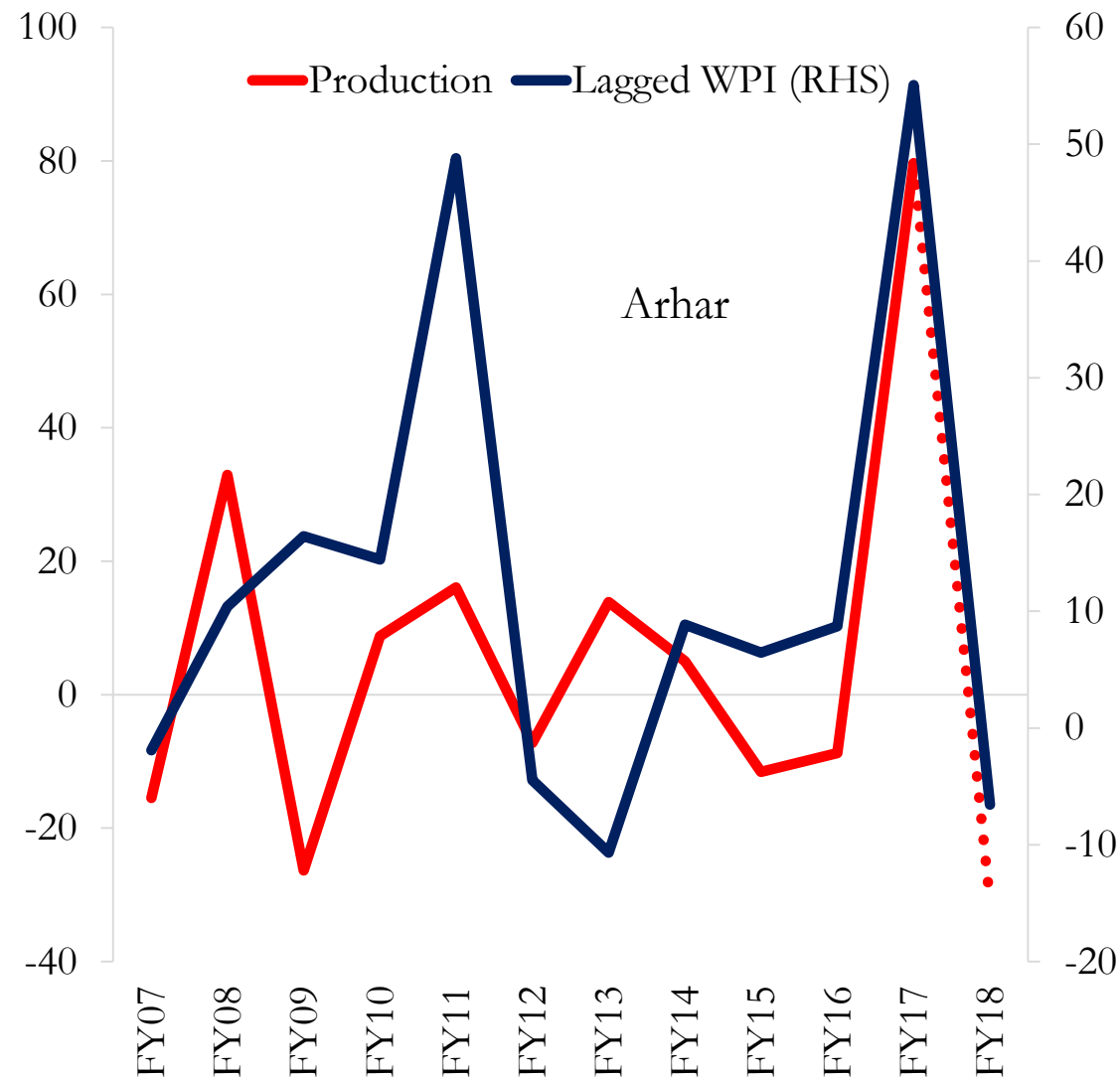


Fiscal Outlook

- Downside risks include GST receipts, growth outlook, spectrum receipts, 7th Pay Commission
- Upside potential include compliance benefits from the GST and Demonetization
- Magnitude and pace of final consolidation relative to the commitments made may need to be assessed going forward

Agriculture: Over longer horizons, there is no necessary opposition between farmer and consumer interests

Crop	Lakh hectare		Growth	
	2016-17	2017-18	2016-17	2017-18
Rice	266.93	280.03	2.1	4.9
Pulses	116.95	121.28	35.0	3.7
Moong	28.31	28.89	39.2	2.1
Tur	45.19	37.51	54.7	-17.0
Coarse Cereals	156.81	156.95	3.2	0.1
Oilseeds	165.49	148.88	6.3	-10.0
Sugarcane	45.64	49.71	1.6	8.9
Jute & Mesta	7.55	7.04	-2.3	-6.9
Cotton	96.48	114.34	-8.7	18.5
Total	855.85	878.23	5.2	2.6



Agricultural policies

- Remunerative MSPs backed by effective procurement
- Eliminate restrictions that impede realization of better prices: Stock limits, export restrictions, impediments to the implementation of e-NAM
- Time also ripe to consider whether direct support (as opposed to indirect support) can be more effective