ACCOUNTABILITY INITIATIVE

Where is India's Growth Story At?
Indications from Provisional Estimates of GDP

IN A GLANCE

July 2021

On 31 May 2021, the Ministry of Statistics and Programme Implementation (MoSPI) released provisional estimates on the performance of the economy in the fourth quarter (Q4) of the financial year (FY) 2020-21 (covering the period from January 2020 to March 2020) [1]. Provisional estimates for the complete financial year too were made public. Gross Domestic Product (GDP) [2] declined by 7.3 per cent for the year, but grew at 1.6 per cent over the last quarter of the year (Q4).

MAJOR TRENDS

- Real GDP rose by 1.6 per cent in Q4 of FY 2020-21 marking only the second time post Q3 in which a positive growth rate was registered. The overall annual rate of growth for FY 2020-21 was at -7.3 per cent.
- Gross Value Added (GVA) [3] at basic prices grew at 3.7 per cent in Q4 and at -6.2 per cent annually.
- Manufacturing (6.9 per cent), Electricity, Gas, Water Supply and Other Utility Services (9.1 per cent), and Construction (14.5 per cent), registered the highest growth in terms of value added to the economy in Q4.
- Private Final Consumption Expenditure (PFCE) declined by 9.1 per cent while Gross Fixed Capital Formation (GFCF) declined by 10.8 per cent in FY 2020-21. Government Final Consumption Expenditure (GFCE) grew at 2.9 per cent over the same period.
- The effects of the second wave may also be keenly felt in the first quarter of FY 2021-22. However, the low base effect could cushion some of the slowdown.

The performance over the last two quarters in FY 2020-21 is noteworthy as it has reflected the capacity of the economy to recover post the first nationwide lockdown in 2020. This explainer explores some data points indicative of trends that are: i) likely to persist through the current financial year; and ii) indicators that provide further insight into the performance of other underlying factors within the economy.

[1] Press Note on Provisional Estimates on Annual National Income and Quarterly Estimates of GDP http://www.mospi.nic.in/sites/default/files/press_release/Press%20Note_31-05-2021.pdf
[2] The real GDP is the monetary value of all the goods and services produced within a nation over a specified period of time, typically a year, adjusted for price changes.
[3] The Gross Value Added (GVA) is often used as a metric to understand the output side of the economy. It is the summation of the monetary value of all annual production of goods and services in different sectors such as agriculture, industry, corporates and services minus subsidies and taxes on them.

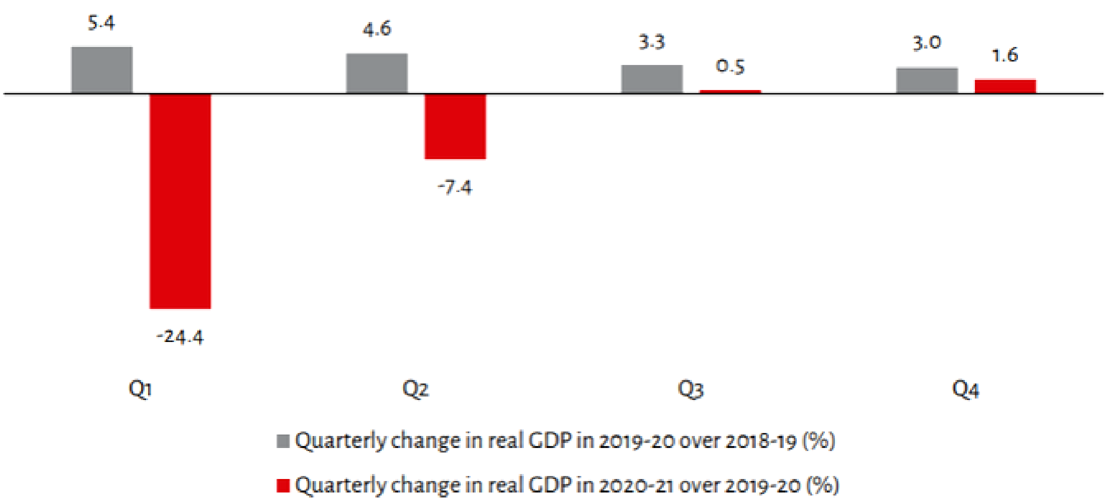
PERFORMANCE IN QUARTER 4

Annual rates of growth in an economy are measured by comparing output over the same period, in successive years. For example, growth in quarter 1 or Q1 of Financial Year (FY) 2021-22 is the change (increase or decrease) in total output (here, real GDP) in the months of April, May and June as compared to the total output over the same period in FY 2020-21.

The fourth quarter of FY 2020-21 registered the best performance for the year, with growth at 1.6 per cent. This marked the second time that the economy registered positive growth in a quarter, following a 0.5 per cent growth in Q3. (The first two quarters of the year had posted negative growth rates as India had entered into a period of technical recession following the pandemic.)

The fourth quarter posted an uptick at a time when the national viral case load had reached an all-time low after the explosive first wave had abated and lockdown measures had eased in almost all states. Most of the Q4 recovery was likely due to the opening up of the economy.

Graph 1: Percentage change in quarterly estimates of GDP at 2011-12 prices in FY 2019-20 and FY 2020-21



Source: MoSPI

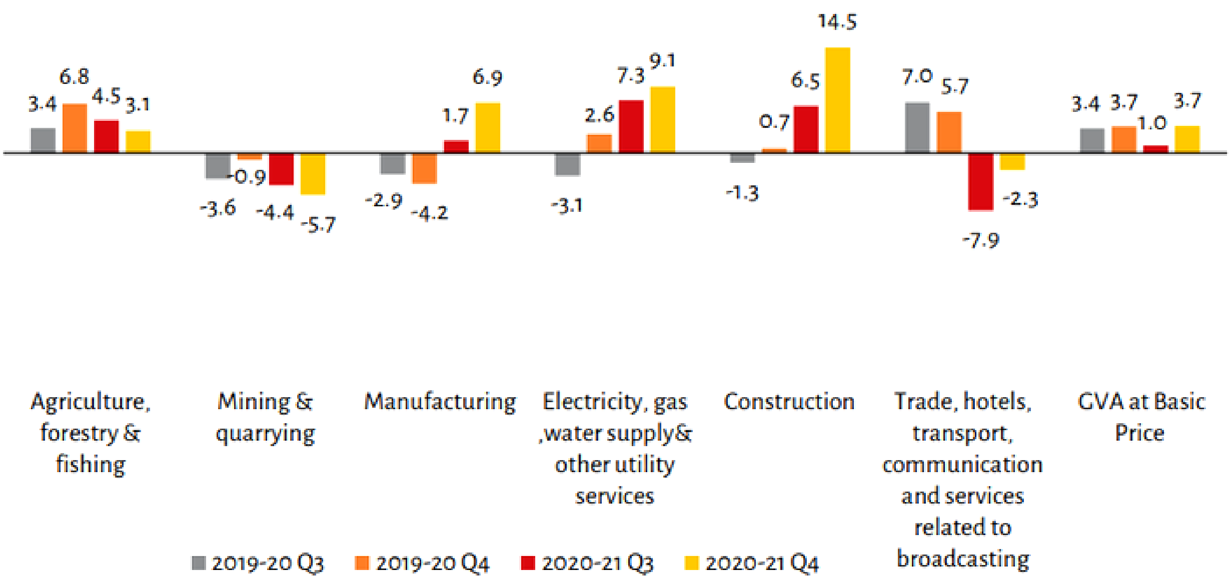
The gradual reopening in Q4 was underscored by the fact that GVA at basic prices was aided by the performance of three sectors. These were Manufacturing, Utility Services, and Construction, in which activity restarted following the first six months of the lockdown. (For the purpose of a simplified illustration, if the agriculture and services sectors produce goods worth ₹ 100 each, and industry and corporates produce ₹ 50 each, the total GVA in a simple economy would be ₹ 300 for the year.)

Manufacturing posted a 6.9 per cent growth rate which was far higher than 1.7 per cent in Q3. Utility services such as electricity, gas, and water supply registered a 9.1 per cent growth rate in Q4, up from 7.3 per cent in the previous quarter. The biggest leap was made by Construction at 14.5 per cent, far higher than the Q3 increase of 6.5 per cent, possibly indicating the resumption of projects and informal labour returning from their home states. Overall, GVA grew at 3.7 per cent, higher than the 1 per cent growth posted in the previous quarter.

The Services related sectors such as trade, hotels, transport, communications, and broadcasting continued to languish at -2.3 per cent, a marginal improvement from -7.9 per cent in the previous quarter. Some of this may be attributed to mobility constraints — sectors that were severely affected were ones that required the observance of strict social distancing norms. Additionally, services in the unorganised sector may have suffered a severe shortage in demand [4] due to which an immediate rebound may have remained subdued.

Other sectors that continued to falter through Q4 were mining and quarrying, which declined by 5.7 per cent, registering a deeper plunge than the 4.4 per cent decline in Q3. Growth in this sector had been deteriorating even in FY 2019-20. The Federation of Indian Mineral Industries (FIMI) has noted a combination of factors leading to this, such as the ban on mining activity due to ecological concerns, poor policy implementation, and high taxation [5]. Sector-specific legislative and taxation reforms are awaited in FY 2021-22 [6].

Graph 2: Percentage change in estimates of GVA at 2011-12 prices in the third and fourth quarters of FY 2019-20 and FY 2020-21



Source: MoSPI

[4] Prabhu, N. (2021, May 19). 'States floating global tenders for vaccines will lead to higher cost, says economist Govinda Rao'. *The Hindu*. https://www.thehindu.com/news/national/karnataka/states-floating-global-tenders-for-vaccines-will-lead-to-higher-cost-says-economist-m-govinda-rao/article34593309.ece

[5] Banerji, S. (2019, September 2). 'Slowdown Blues: Mining sector stares at a slump; lakhs of jobs on the line', *BusinessToday.in*. https://www.businesstoday.in/current/slowdown-blues/mining-sector-stares-slump-lakhs-of-jobs-on-the-line/story/376712.html

[6] Bhaduri, A. (2020, December 28). 'India's Mining Sector to witness reforms, flurry of activities in 2021'. *Hindustan Times*. https://www.hindustantimes.com/business-news/india-s-mining-sector-to-witness-reforms-flurry-of-activities-in-2021/story-HH7Crj9hFhCumGoIkFLG5O.html

Even though there is some assurance in the resurgence of economic activity in the Q4 numbers, it should still be viewed with caution. This is because of two reasons. Firstly, the second wave can well undo the recovery made by certain sectors in the coming months. Secondly, the annual performance of the economy indicates underlying concerns which are discussed in the following section.

PERFORMANCE FOR THE FINANCIAL YEAR 2020-21

GDP (at 2011-12 prices) registered a negative annual rate of growth at -7.3 per cent, indicating the firm hold of a recession. It is the first full year of contraction registered since 1979-1980 [7]. The economy did marginally better than the projected rates of growth by the International Monetary Fund at -8.0 per cent in the April World Economic Outlook. The Survey of Professional Forecasters published in February had also projected a decline of 7.6 per cent.

Despite this, the macroeconomic trends point to more sustained areas of concern.

1) Decelerating consumer sentiments and persistent unemployment could be markers of an economy in crisis

Private Final Consumption Expenditure (PFCE)

The expenditure side of national income accounting showed two worrying trends. One was the substantial annual decline of PFCE. To illustrate simply, the PFCE is the sum of all expenditure on final goods and services that a typical household will incur in a year. So, for example, if a household spent most of its income on buying a new car or on eating out, this will be part of its private final consumption. However, if they bought a second hand car, the cost incurred is not calculated as part of PFCE. This is because the car was already on the market and was not newly manufactured that year.

PFCE has long been a major component of domestic expenditure, accounting for approximately 56 per cent of the GDP. Consumption demand, as measured by the PFCE, is often observed as a proxy for income, salaries, and jobs. When PFCE declines, it indicates the possibility that a larger proportion of households are suffering from constrained finances and job losses.

The PFCE at 2011-12 prices showed that average expenditure by households declined substantially. It contracted from 83.2 lakh crore in FY 2019-20 to 75.6 lakh crore in FY 2020-21, a decline of 9.1 per cent. Crucially, the Q4 performance of PFCE too remained subdued at 2.7 per cent. This underlines the sustained dampening of consumer sentiments that may take a much longer time to revive.

Additionally, lower consumer sentiments are also likely reflected in relatively lower rates of growth in services as discussed in the previous section. Presumably less people were going out to eat or choosing to travel for leisure at this time.

[7] Web Team and Agencies. (2021, May 31). 'India's GDP grows 1.6% in fourth quarter, contracts 7.3% in FY 21'. *Business Standard*. https://www.business-standard.com/article/economy-policy/india-s-gdp-growth-slows-to-1-6-in-fourth-quarter-contracts-7-3-in-fy21-121053101001_1.html

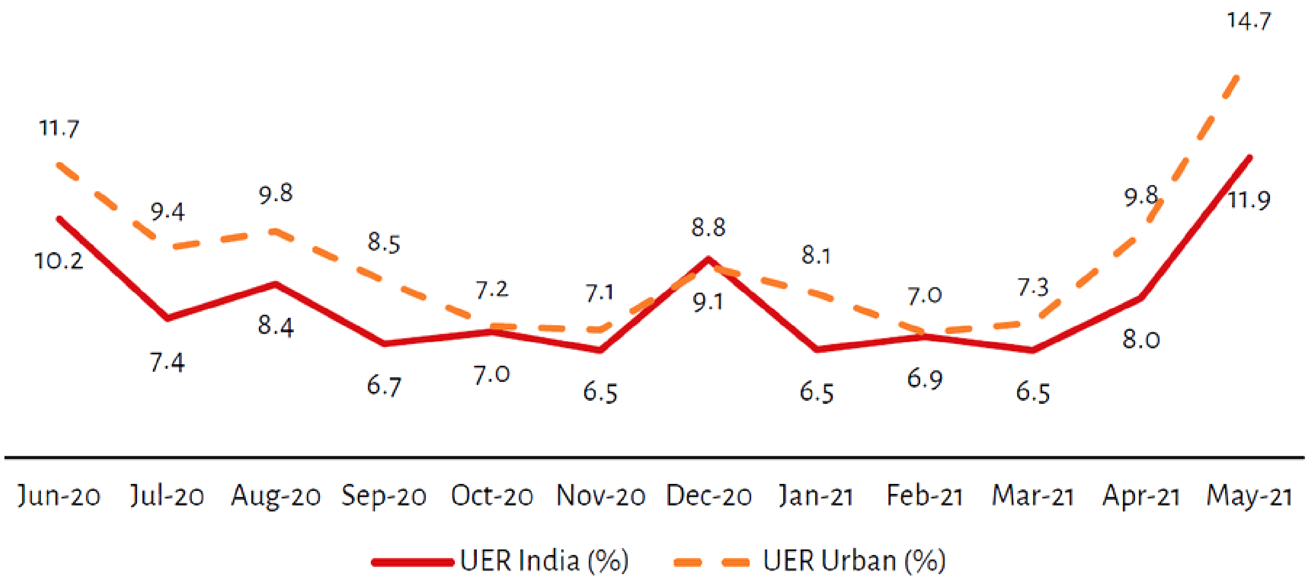
2) Unemployment

The unemployment rate (UER) as per the Centre for Monitoring Indian Economy (CMIE) has been shown in Graph 3. It can be observed that the UER has been high throughout FY 2020-21. Post the lockdown period, through the months of June-March 2020-21, the unemployment rate has, on average, been about 7.5 per cent. Urban unemployment has been particularly high through this period at 8.5 per cent. This is also telling because the first wave ravaged urban areas significantly more than rural areas.

In January 2021-22, at the time of peak 'unlockdown', the urban rate of unemployment was still at 8.1 per cent. What is also of significance is that the labour force participation among women was less than 11 per cent in FY 2020-21. During September-December 2020, when the economy registered a positive growth, the unemployment rate among women was as high as 15.06 per cent compared to 6.1 per cent for men. **The urban unemployment rate was even higher for women at 20.8 per cent whereas for men it was only 6.5 per cent.**

However, the high UER is particularly worrying going into Q1 of FY 2021-22. Both urban and rural unemployment have soared with the overall UER at 11.9 per cent for May 2021 [8]. **These Q1 trends in unemployment indicate that the PFCE, which had declined in FY 2020-21, is likely to decline further into FY 2021-22 as India battles the aftermath of the far more lethal second wave.**

Graph 3: Rate of unemployment in percentage



Source: CMIE

[8] A new Pew Research Center analysis finds that the number of people who are poor in India is estimated to have increased by 75 million because of the COVID-19 recession. https://www.pewresearch.org/fact-tank/2021/03/18/in-the-pandemic-indias-middle-class-shrinks-and-poverty-spreads-while-china-sees-smaller-changes/

3) Is government expenditure filling in for expansion in other sectors?

Another indicator that may not bode well for a sustained recovery are the low rates of GFCF. This is an indicator measuring investments in fixed assets and is a crucial factor in generating final goods, services and income in the future. Expenditure on infrastructure such as roads and bridges, investments in new factories, expenditure on technology for higher manufacturing productivity, and expenditure on replacement machinery to combat depreciation, all constitute the GFCF.

The GFCF at 2011-2012 prices declined by 10.8 per cent for FY 2020-21, even though it registered a moderate uptick in Q3 and Q4. In terms of gross comparison, GFCF contributed ₹47.3 lakh crore in FY 2019-20. In FY 2020-21, that figure stood at ₹42.2 lakh crore.

The revival in Q3 and Q4 in employment-heavy sectors such as Manufacturing and Construction does not seem to have boosted household consumer sentiment or employment. This may indicate three possibilities. One is that there may be a delay in how consumer sentiments and unemployment respond to the positive growth in these sectors (a lagged response). The Consumer Confidence Index as measured by the RBI showed that weak sentiments continued through January 2021 [9].

Second is that government consumption expenditure may be accounting for a larger share of the expenditure than before [10]. The Government Final Consumption Expenditure (GFCE) has gone up considerably in Q4. The GFCE is conceptually similar to expenditure on final goods by the private sector. However, the items on which the government spends and the method of calculating the GFCE differ considerably. For example, the costs incurred by the government in providing services to individual households, such as education and social security, would be included in GFCE. Compensation to employees in providing these services, intermediate costs, and depreciation account for some of the ways in which the GFCE is estimated

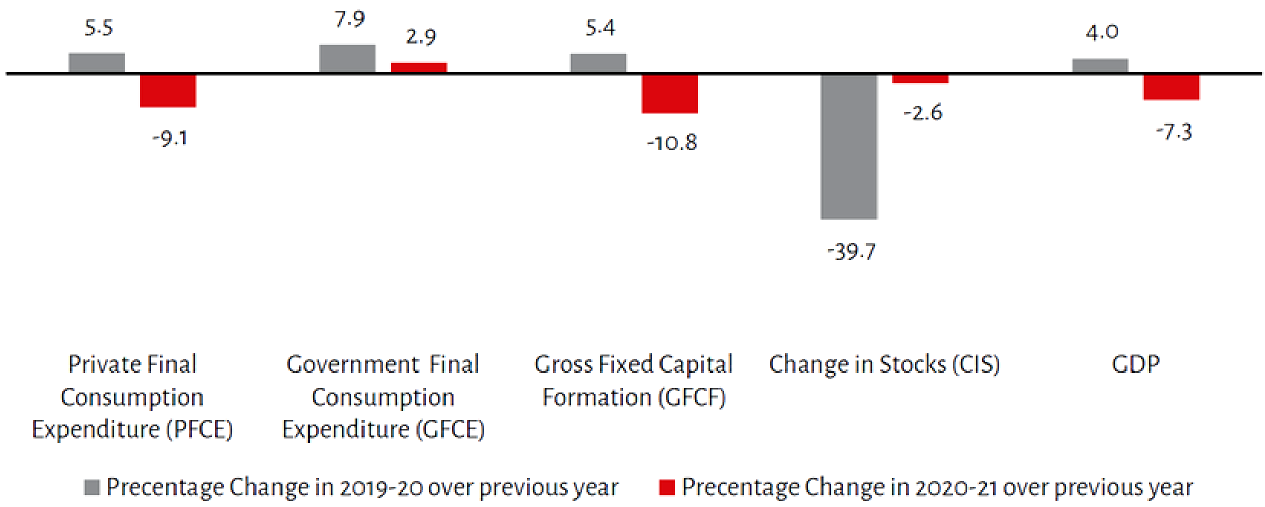
The third possibility is that the higher GDP may also indicate a clearing out of inventories and less of actual production on consumer goods. The Change in Stocks (CIS) has also revived in Q4 by 12 per cent [11].

[9] https://www.rbi.org.in/Scripts/PublicationsView.aspx?id=20320

[10] As part of the stimulus package announced in FY 2020-21, the government had tried to boost investments by announcing the National Infrastructure Pipeline and the National Asset Monetisation Pipeline.
https://www.moneycontrol.com/news/trends/india-gdp-data-gross-fixed-capital-formation-rate-sees-decline-in-2020-21-6962921.html

[11] Chakravarty, A. (2021, June 1). 'India's GDP Fall: Low Household Consumption is a Cautionary Tale'. *The Quint*.
https://www.thequint.com/voices/opinion/india-gdp-data-modi-govt-economic-crisis-recession-slow-recovery-mass-unemployment-low-household-consumption#read-more

Graph 4: Percentage change in components of expenditure and GDP at 2011-12 prices for FY 2019-20 and FY 2020-21



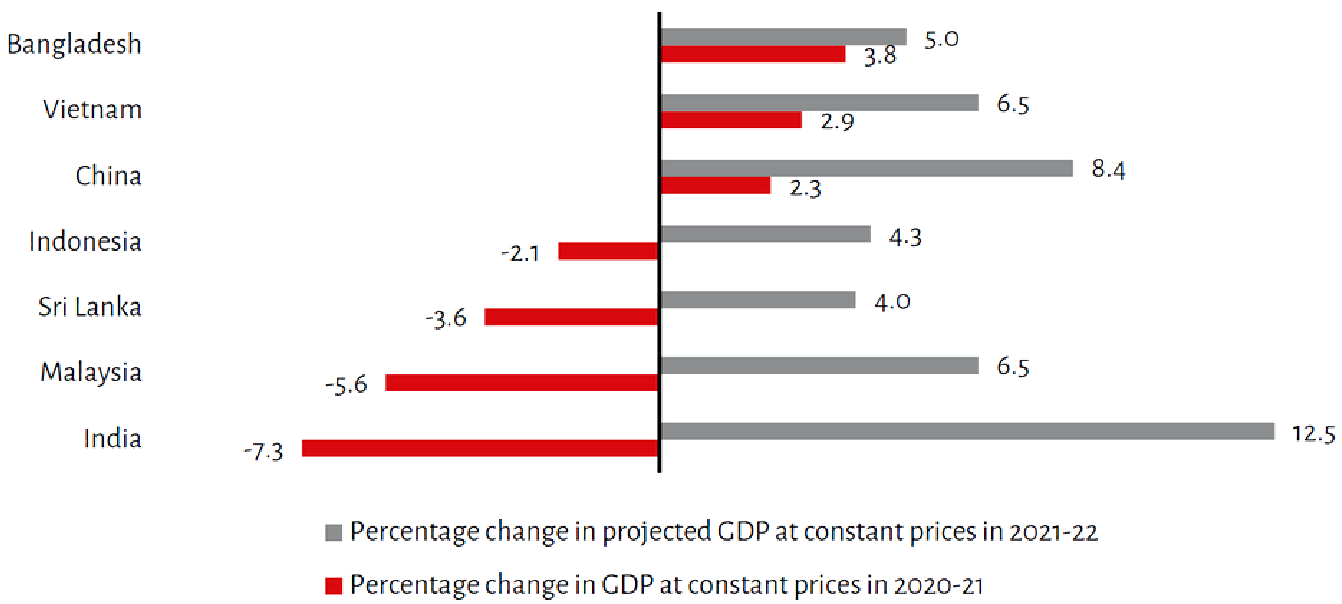
Source: MoSPI

How does India's growth in FY 2020-21 compare with the rest of the world?

As per the April World Economic Outlook [12], it was estimated that India's growth would decline by 8 per cent in FY 2020-21. Even though India performed better than expected, it still emerged as one of the worst-performing middle-income economies as compared to the estimates of the April database for other countries by the IMF.

Bangladesh grew at 3.8 per cent as per IMF estimates while Vietnam grew at 2.9 per cent. Among countries that suffered a technical recession like India, the deceleration has been at a lower rate than India.

Graph 5: Percentage change in estimated GDP for 2020-21 and 2021-22 for select countries



Source: World Economic Outlook Database for April 2021

The per capita GDP at basic prices for India in FY 2020-21 had fallen by 8.2 per cent from ₹1.08 lakh to ₹0.99 lakh.

[12] https://www.imf.org/en/Publications/WEO/weo-database/2021/April

Future Outlook: Recovery in growth despite or because of the base effect?

In spite of a significant improvement in Q4 of FY 2020-21, there are several worrying trends that were discussed in this explainer. Chief among them is the crashing of consumer sentiments and accelerating unemployment both in the rural and urban areas. Another area of worry is the low rate of fixed capital formation (GFCE). Taken together, these indicate that the recessionary trends are far from over.

However, what these numbers also indicate for Q1 of FY 2021-22 going forward is crucial. The second wave that ravaged the country from April 2021 onwards will likely exacerbate the negative impact on the economy.

The forthcoming FY 2021-22 Q1 numbers may also, possibly, be misleading. This is because of the low base effect. Since GDP declined from April-June 2020-21 by -24.4 per cent, growth in Q1 for FY 2021-22 will have to be compared to historically low bases. **In all probability, growth in Q1 FY22 may hit double digits despite a very moderate recovery in reality.**

Economists are warning that the possibility of a sharp recovery as last year is less since economic activity for the current fiscal did not come to a standstill as it did in FY 2020-21 [13]. The World Bank has slashed the FY22 annual forecast for India from 10.1 per cent to 8.3 per cent [14].

At this point, a national stimulus package may not provide a solution unless the states and the Union government coordinate to identify and fix both supply and demand side constraints such as improving the implementation of tax policies and boosting consumer sentiments [15].

Above all, universal vaccinations at a rapid rate has widely been considered as the only solution to preventing a potential third wave. However, if the lack of coordination among governments and vaccine supply shortages is anything to go by, sustainable recovery may yet be elusive in the days to come.

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[13] Malhan, A. (2021, June 2). ' If uncertainty persists, second wave may do more damage than first: Pronab Sen'. *The Economic Times Online*. https://economictimes.indiatimes.com/news/economy/indicators/if-uncertainty-persists-second-wave-may-do-more-damage-than-first-pronab-sen/articleshow/83165669.cms

[14] *PTI*. (2021, June 9). ' Covid impact: World Bank slashes India's FY22 GDP growth forecast to 8.3%'. *Business Standard*. https://www.business-standard.com/article/economy-policy/world-bank-projects-india-s-fy22-gdp-growth-at-8-3-121060801290_1.html

[15] Special Correspondent. (2021, June 28). 'Govt. unveils ₹6.28 lakh cr stimulus post second COVID wave'. *The Hindu*. https://www.thehindu.com/business/Economy/nirmala-sitharaman-unveils-new-covid-recovery-package-expands-credit-relief/article35020572.ece