The Gathering Storm Clouds of Recession*

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The Index of Industrial Production has for the first time since June 2013 contracted in absolute terms by 0.1 percent in March 2019 compared to a year ago. This comes on top of a mere 0.07 percent increase in February, a 1.7 percent increase in January, a 2.6 percent increase in December, and a 0.3 percent increase in November. Industrial growth in short has been slowing down for some time now and the latest figure only reaffirms this trend emphatically.

Within industrial production, the manufacturing sector which has a weight of 77.6 percent, declined by 0.4 percent in March compared to a year ago, and this arose because of a decline of 8.7 percent in capital goods, a decline of 5.1 percent in consumer durables, a decline of 2.5 percent in intermediate goods and a rise by 0.3 percent in consumer non-durables. For the financial year 2018-19 as a whole, the growth in the index of industrial production was a mere 3.6 percent, which is lower than the 4.4 percent of 2017-18; but it is in the later months of the financial year that the recession has gathered momentum.

This recession in a sense is inevitable. It is a symptom of the fact that the Indian economy, like other economies of the world, is caught in a limbo, with neo-liberalism having reached a dead-end and no other economic regime based on the home market having come to replace it.

The world economy has been witnessing a slowdown which has now begun to affect economies like India and China via a lower growth rate of exports. But the lower growth-rate of exports is not even partially counterbalanced by any stepping up of growth of the domestic market. On the contrary the home market is also shrinking at the same time because of rural distress, because of the second-order effects of the slowing down of export growth, and also because of the growing weight of non-performing assets, also on account inter alia of the slowing down of industrial growth, which squeezes credit availability for undertaking larger expenditure. The slowing down of export growth in other words, far from being counterbalanced, is further compounded by a shrinking of the home market.

This is clear from the fact that the consumer durables sector has shrunk and the consumer non-durables sector has remained virtually stagnant in April compared to the previous April. And the contraction in capital goods output which comes on top of a contraction that had already occurred in February, suggests that investment in the economy is falling.

The Reserve Bank of India has already twice announced cuts in the Repo Rate, of 25 basis points each; but this is unlikely to make much difference. What is holding up credit disbursement is not so much the cost of credit as its availability, which has got impaired by its being locked up in non-performing assets. Of course even if credit was easily available it is not clear how much of a difference that would have made, but with credit availability itself being subject to some tightness, a mere lowering of the rates will not increase credit disbursement to any significant extent.

What is needed is fiscal expansion, but here we come to the nub of the matter. In this election season the various political parties have been promising larger transfers to the rural poor, which would certainly expand the home market and cause some revival in industrial output. The Modi government's budget had promised Rs.6000 per capita annually to about 12 crore persons belonging to small peasant families. The Congress has gone much further in its election manifesto. It has promised under its NYAYA scheme to give Rs.6000 per month, i.e. Rs.72000 per year, to the bottom quintile of the households, which is about 5 crore households.

While these schemes, especially the NYAYA scheme, which is much more ambitious, will help in expanding the home market, the question is how the resources for it can be raised. Taxing the rich, especially through wealth taxation which is virtually absent in India and which can therefore raise substantial revenues precisely because it is absent in India, is the obvious way of mobilizing resources; but this is going to be stoutly opposed by international finance capital. Manmohan Singh had said, rather diplomatically when the NYAYA scheme was being launched, that there should be no problems about raising the resources; but finding resources for it within a neo-liberal regime will be exceedingly difficult.

Likewise if the scheme is even partially financed by an increase in the fiscal deficit, then the magnitude of the fiscal deficit will exceed its target of 3.4 percent of GDP, and this is likely to lead to a downgrading of India's credit-rating, making it extremely difficult to finance the current account deficit on the balance of payments. This problem will become even more acute if India falls in line with the American demand to stop buying oil from Iran, which is cheaper than the spot oil prices that India would otherwise have to pay. The Modi government has already indicated its willingness to fall in line with the American demand; if it comes back to power then it will simply reiterate this position.

Oil prices are already firming up, which will widen the current deficit; if the US sanctions against Iran are also taken into account, then the current deficit will widen further. And if in addition the fiscal deficit figure exceeds its target, then the inflow of finance will dry up as India's credit rating will drop, and there will be little hope of meeting this deficit in the normal course.

We therefore are in a bizarre situation. If the government tries to overcome the gathering recession, then it will find it difficult to meet the current account deficit; on the other hand if it does nothing to counter the recession, then the unemployment situation which is already grim, will become even grimmer.

The grimness of the unemployment situation has been hidden from public view because the government has simply refused to publish any data on unemployment for over two years. But a leaked report from the Statistical Office of the government puts the unemployment rate at 6.1 percent which is the highest in the last 45 years. The Centre for Montirong the Indian Economy has put the unemployment rate at 7.6 percent in April. It should be noted that while movements in the unemployment rate give an indication of the direction of movement of unemployment, the rate itself does not capture the magnitude of the problem. This is because employment rationing in India takes the form of most people being employed for only a part of the time, rather than some being fully employed and others being fully unemployed.

Clearly therefore the government will have to do something to ameliorate unemployment; but doing anything will destabilize the balance of payments within the neo-liberal paradigm. The neo-liberal chickens in short are finally coming home to roost.

Since neo-liberalism itself is running into a dead-end, this should have been an ideal time to disengage from it by introducing trade and capital controls. As the United States is introducing trade controls already, India could have introduced such controls in the shadow of US action. And with such controls in place, it could have introduced a wealth tax, and an inheritance tax. It could then have delivered on its promise of making transfer payments to the poor households, and thereby expanded the domestic market, and followed it up by taking steps to increase the rate of growth of foodgrain production. A drying up of financial inflows in such a situation would not have made much of a difference to the country's ability to finance its current account deficit which would have narrowed anyway because of trade controls.

But the Modi government appears to have little awareness of the fact that neo-liberalism has reached a dead-end. And the Congress party which was the architect of India's neo-liberal reforms, despite promising the NYAYA scheme, will not have the temerity to act upon it. The industrial recession therefore is likely to accentuate.

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