The Eight Per Cent Solution

A Strategy for India's Growth

Nikhil Gupta

Email id: nikhilgupta.gipe@gmail.com

What constitutes an Economy? Four participants and three activities

Four institutional participants, namely

1. The Government (Center and states)
2. Corporate sector (including private and public, financial and non-financial companies)
3. Household sector (the residual), and
4. The external/foreign sector

Three activities, namely

01 Consumption (Government and households)

02 Investments (all three domestic participants),

03 Foreign trade

Seven key learnings & lessons to remember

- #1: Differentiate between the gross and net impact of a policy. The latter is relevant for the economy
- #2: Financial savings are different from physical investments, and there is no concept of financial investments in the national accounts
- #3: Remember the 'Theory of Everything' identity in economics, which says: ***Total investments = Domestic savings + Current account deficit***
- #4: The corporate sector is much bigger than listed companies
- #5: Targeting fiscal deficit in isolation is likely an ineffective strategy
- #6: No external policy works without affecting the domestic equilibrium
- #7: Cross-country comparisons may be exciting but could be of limited utility

Four key findings

- Indian household sector’s financial position has weakened dramatically in the 2010s decade
- Listed companies strong, but aggregate corporate sector has weakened
- Fiscal consolidation means weak growth in government spending in the 2020s decade
- Exports are unlikely to be the new growth driver, given other discordant economic policies

Gazing into the future: Possible outcomes

- For the household sector, only two possible scenarios:
  a) they may continue to prefer consumption over savings, adding on more debt, or
  b) they change the course and build-on their (financial) savings.

  The former could lead to faster growth for a short period of time (like 2010-15) and the latter may lead to slower growth followed by high sustainable growth (say, 2000-07)
- Assuming unchanged deficit targets (7%/6% of GDP by FY26/FY30), fiscal spending growth will be slower than the pre-2019 period.
- Could corporate investments and exports offset weak consumption growth? Unlikely without a vision and plan to achieve this.

Eight key recommendations: Accept 2020s as the Healing decade

- India's gross domestic savings (GDS) must rise, led by higher household savings, higher corporate profits and lower fiscal deficit.
- Only two ways to achieve higher household savings: lower consumption and/or higher income growth. The more the share of financial savings, the better it is
- Although household leverage is low in India, its debt service ratio is very high. Must find ways to extend the maturity, as lower savings constrain to reduce interest rates materially
- Serious deliberations are required to push corporate investments – how to make it more profitable?
- The fall in fiscal deficit must be in line with lower household financial savings. Higher financial savings will help to keep interest rates low.
- Hope for an export-led growth may be a futile exercise unless the domestic demand is suppressed and substituted with external demand.

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- To mitigate the risks emerging from a volatile global economic environment, RBI must distance itself from the currency markets and focus primarily on domestic government securities markets.
- An investment rate of 32-33% of GDP must be enough to achieve 8% growth with an improvement in efficiency. But it is highly uncertain and not a substitute for the strengthening of financial positions.

Thank You