Will Budget Look Beyond Corporate Sector?

By S Gurumurthy | Published: 29th June 2014 09:05 AM Last Updated: 30th June 2014 11:20 AM

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Of all governments since Independence, the Narendra Modi government has perhaps aroused the highest expectations of people – the kind of aspiration not easy for any government to satisfy. Modi regime's first major test is the Budget for 2014-15, just 10 days away. Budgets have long ceased to be just printing and presenting annual financial data. Over time they have become policy setting or resetting instruments. Like in 1991, given the global and national economic conditions, there is now a compelling need for reassessing and resetting the direction of the economy in the Budget. This Budget has necessarily to be very different one from the Budgets of the last two decades. Why?

No "Fit -All' economic model

It will need going back to 1991. When India set out to liberalise then, it chose to follow the US way to frame policies, preferring not to look at the other successful German and Japanese ways. From then on, the national focus shifted to celebrating and promoting private corporate sector particularly big companies, multi-national and national in that order. But, now the US model has been heavily questioned in the US itself after the 2008 global meltdown. Till then the US claimed to have the theoretical lead for all countries.

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After 2008, the truth un-admitted by the guild of economists in India is that the world is without a reliable, Fit-all economic theoretical frame work. At least one leading Indian economic thinker Dr Rathin Roy, who heads the National Institute of Public Finance and Policy, had the guts to say in a seminar in Chennai in March 2014 that any economist who denies that truth was either ignorant or dishonest.

Not many did notice that even before the global meltdown, in 2005 itself when the US model was seen to be doing very well, world financial bodies had washed off their hands saying that they have no Fit-all economic model and each country has to find its own way. Yet India continued to imitate the US way.

1991-2011 a look back

Now, with the economy nearly incapacitated, the economic establishment seems to have run out of ideas. The prescriptions of the US seem outdated. The US-led policies did produce high growth rates of over 9 per cent in the first edition of UPA rule and this persuaded our establishment to trust that that was the right way. But that growth has now proved deceptive. It has concealed the terrible truth that that was just phoney money growth which not only did not yield jobs but actually reduced jobs! The employment added in six years between 2004-5 and 2010 was just 2.7 million as compared to over 60 million jobs generated in the five years preceding. This truth has rudely shaken the economists. This alone is adequate to question the economic thoughts that have guided the government in the last 10 years. Also, two decades is a vantage point high enough to look back and assess what the post-1991 theories and policies – which have focussed almost exclusively on private corporates, particularly, the listed corporates as the escalator for growth – have yielded. Now look at how the private corporates have responded to government's benevolence. This exercise calls for data-based analysis and the reader has to bear with some numbers.

Rs 47.6 lakh cr yields 2.2 m jobs!

With most of the Indian economy opened for foreign investment, since 1991 and till 2011 the corporate economy had received close to $317 billion of foreign investment – $176 billion through stock market and $141 billion as direct investment. The non-government external debt – read borrowings of public sector and private sector corporates in dollars – jumped by over 10 times to $179 billion. The bank lending to corporates grew up by 43 times to almost `20 lakh crore. Corporate and personal tax rates had halved, making India rank among world's least taxed nations. What did all these monies do? The Sensex vaulted by 20 times from 1,000 to over 20,000 in 2011 with stock market-cap touching $1.6 trillion (`96 lakh crore). Result, Indian corporate promoters now constitute a fifth of world's billionaires with a tally of 70 – none in 1991 – and Mukesh Ambani leading the pack with $18 billion wealth and a billion dollar house. Despite the tsunami of billions of dollars and trillions of Rupee into the corporate sector, its share of GDP improved by just 3 per cent in 20 years to 15 per cent. Foreign investment was celebrated because it would generate jobs. And how much jobs the $317 billion foreign investment, $160 billion foreign borrowing, and `19 lakh crore bank credit – all adding to `47.6 lakh cr – that flowed into the corporates generate directly? Believe it. Just 2.2 million jobs in 20 years since 1991! A little over a lakh of jobs a year, according to the Economic Survey 2012-13. The private corporate sector added 3.7 million jobs over 76.7 million in 1991, but the public corporates dropped 1.5 million jobs reducing the net job addition to 2.2 million. Contrast this with socialist India's record in the pre-reform period. In the 30 years from 1961 to 1991, the private corporate sector added 2.7 million jobs and public corporate sector's 12 million – growth of 5 lakh a year. That was five times the annual rate of job growth in the corporate sector in the post-reform period. Question inevitably arises why FDI invited to generate growth and jobs and why private corporates pampered to generate jobs miserably failed.

Rs 30 lakh cr tax foregone

This is not the end of the story. Look at more facts. Not just that the private corporates received foreign investment and loans and bank credit totaling `47.6 lakh crore. They also received bonanza of tax cuts of `30 lakh crore in seven years from 2006-7 to 2012-13. The cuts averaged annually `2.6 lakh crore till 2007-8. But when the global meltdown occurred, the UPA government almost doubled the tax cuts to `5 lakh crore a year to stimulate the economy. These huge cuts dented the Budget with a deficit of almost `22 lakh crore between 2008-9 and 2012-13. But the corporates swallowed the stimulus tax cuts without passing it on to the consumer. Consequently, far from falling with the decline of national economy, the corporate profits rose by over `9 lakh crore in this period. But the corporates did not even invest their high profits to grow their business. Their investment actually slowed as their profits increased from 2007-8 to 2010-11.

Banks preferred over stocks

Now look at the stock market which spins capital for the corporate sector. The BSE Sensex, which closed at 5,740 in 2004-5 rose to 18,815 by 2013-14. Now it is over 25,000. What caused the Sensex to vault by over four times in 10 years – particularly when the national economy was in distress since 2009 and Indian families invested very little in stocks. The Indians are much like the Germans and Japanese who also do not risk their savings in stocks. In 1970s, Indian families invested 2% of their savings in stocks. In 1980s, 6%. In 1990s, 11%. Between 2000 and 2005, just 2%. Between 2005-2011, it was 4%. The Reserve Bank of India Working Group on Savings during the 12th Five-Year Plan (2012-17) has projected Indians to invest just 1.3% of their savings in stocks. Since 1991, the government had been cutting interest rates partly to dissuade the savers away from banks. Dr Manmohan Singh even asked the Indian families to buy stocks and not bank their money. But the Indian families did not pay heed to him and persisted with bank deposits.

As liberalisation deepened, the Indian families, instead of moving into stocks as the policies persuade them to, moved away. Rejecting the US model, which opts stocks over banks, Indians like Germans and Japanese prefer banks over stocks. The founding premise that liberalisation and globalisation would shift savers from banks to stocks has miserably failed in India. The result is bank-based – not market based – macro economic financial structure of the Indian economy – totally unlike the US. The bank deposit to GDP ratio in India actually doubled during the reform period – from 34% in 1991 to 68% 2012. It is clear that people's lifestyle and financial habits produce economic model and not government policies. What is the contribution of corporate sector – public and private together – to India's GDP? According to Credit Suisse Asia Pacific/India Equity Research Investment Strategy paper (July 2013), the share of corporates in GDP is just 15 per cent and that of listed corporates is trivial, 4 per cent. In terms of employment or value addition or exports or manufacture the corporate sector is not a significant player. The Budget needs to look beyond the corporate sector and look at what really sustains India if it has to lift the Indian economy. What is that which sustains India? Await the next part.