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Cover Story

EXCLUSIVE INTERVIEWS

"The Main Risks to The Economy are External"

Alok Sheel, Secretary, Ministry of Finance, Government of India

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B&E: Both internal and external factors are threatening India's GDP growth. What is your projection for the Indian economy by 2012?

Dr. Alok Sheel (AS): The growth rate of the Indian economy has declined slightly over the last few quarters, but this decline has to be placed in the context of global developments as we are part of a very integrated global economy. Global economic growth has also declined during this period. During the recent global recession, only two big economies escaped; one was China and the other was India. Both these economies performed reasonably well. Chinese growth rate was sustained by a huge stimulus programme. In comparison, India's stimulus was comparatively modest. But our economy grew at 6.7% in the worst year. This is because the Indian economy is one of the most balanced amongst the major economies, as its drivers of growth are basically domestic demand, savings and investment. Currently the main risks to the Indian economy are external, with the headwinds to growth coming from outside; such as elevated commodity prices, low external demand, continuing instability in global financial markets, a major disaster in Japan and the uncertainty deriving from sovereign debt concerns in Europe.

B&E: Given the fact that fiscal deficit is a foremost problem for India, is the country adequately equipped to tackle the deficit problem?

AS: India's major concerns are its fiscal deficit and public debt overhang. Nevertheless, current levels of economic growth make these less of a concern than what they were formerly. This is why, unlike in advanced countries that have seen a sharp fall in growth, India's public debt as a percentage of GDP is declining despite the fiscal stimulus during the financial crisis. India's debt bearing capability has increased over the time. The concern is not so much the level of the fiscal deficit or public debt, but whether the fiscal space created by high growth is being adequately leveraged for investment to bridge the huge infrastructure deficit necessary to sustain current levels of high growth, especially since most of this investment would need to come, directly or indirectly, from public resources, as it has in most parts of the world.

B&E: The US recession affected India much against expectations in 2008. Is there a chance that Eurozone's sovereign debt crisis may create an impact on Indian economy?
AS: As Indian economy is inter-connected to global economy, if Eurozone's debt crisis escalates, it would certainly impact India. At the same time, as we saw in the wake of the collapse of Lehman Brothers, India may be less affected than most other countries because its growth drivers are primarily domestic, and these drivers are mostly intact, unlike in developed countries that have seen a major decline in demand on account of deleveraging. We need to get investment back on track. Especially India needs huge investment on infrastructure. We need to push the reform process forward to attract more investments into the country.

B&E: Is there any probability that India might see recession by 2012?
AS: Recession technically means negative GDP growth in two consecutive quarters and nobody really envisages that would happen in India even in the worst case scenario. If there is another global recession, or a second dip, India cannot escape. However, while its growth rates might fall by a few percentage points, it is highly unlikely, given its domestic growth drivers and a well regulated financial system, that it will see negative growth.

B&E: If India faces a recession or dramatic slowdown, do you think that the Indian government is prepared enough to tackle that?
AS: As I said earlier, the trend in the reduction of the public debt ratio has been very encouraging. At the same time, interest rates have been repeatedly raised by RBI. Therefore, unlike advanced countries, India has both fiscal and monetary space to respond to another severe global downturn, although it would be more difficult this time. Also, monetary space is more than the fiscal space, since the fiscal deficit is coming down more slowly.

B&E: What steps need to be taken globally to tackle such a crisis as it affects all nations?
AS: A discussion on global imbalances is going on in the G20. There are major seven systemically important economies in this premier global forum for international cooperation that individually comprise more than 5% of G20 GDP at either market exchange rates or at PPP. These countries are US, UK, Germany, France, China, Japan and India. All these countries have large imbalances. US and the UK have big current account deficits; and China, Germany and Japan have huge current account surpluses. India has only a 2-3% current account deficit though, a level that can be financed on a sustainable basis over the medium to long term, especially in view of our large hard currency reserves.

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