

THE FOUNTAINHEAD OF INDIA'S ECONOMIC MALAISE

Relevant for: Indian Economy | Topic: Issues relating to Planning & Economic Reforms

The state of India's economy is deeply worrying. I say this, not as a member of the Opposition political party, but as a citizen of this country and as a student of economics. By now, the facts are evident to all — nominal GDP growth is at a 15-year low; [unemployment is at a 45-year high](#); household consumption is at a four-decade low; bad loans in banks are at an all-time high; growth in electricity generation is at a 15-year low — the list of highs and lows is long and distressing. But the state of the economy is worrying not because of these disturbing statistics. These are mere manifestations of a deeper underlying malaise that plagues the nation's economy today.

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A nation's state of the economy is also a function and reflection of the state of its society. The functioning of any economy is the result of the combined set of exchanges and social interactions among its people and institutions. Mutual trust and self-confidence are the bedrock of such social transactions among people that foster economic growth. Our social fabric of trust and confidence is now torn and ruptured.

There is a palpable climate of fear in our society today. Many industrialists tell me that they live in fear of harassment by government authorities. Bankers are reluctant to make new loans, for fear of retribution. Entrepreneurs are hesitant to put up fresh projects, for fear of failure attributed to ulterior motives. Technology start-ups, an important new engine of economic growth and jobs, seem to live under a shadow of constant surveillance and deep suspicion. Policymakers in government and other institutions are scared to speak the truth or engage in intellectually honest policy discussions. There is profound fear and distrust among people who act as agents of economic growth. When there is such distrust, it adversely impacts economic transactions in a society. When transactions among people and institutions are negatively impacted, it leads to a slowdown of economic activity, and eventually, stagnation. This perilous state of fear, distrust and lack of confidence among citizens is a fundamental reason for our sharp economic slowdown.

Groping in the dark on the economy

There is an air of helplessness too. Aggrieved citizens find nowhere to go to air their grievances. Public trust in independent institutions, such as the media, judiciary, regulatory authorities and investigative agencies, has been severely eroded. With the erosion of trust, there is a lack of a support system for people to seek refuge against unlawful tax harassment or unfair regulations. This makes entrepreneurs lose their risk appetite even further for undertaking new projects and creating jobs. This toxic combination of deep distrust, pervasive fear and a sense of hopelessness in our society is stifling economic activity, and hence, economic growth.

The root cause of this rupturing of our social fabric is the Modi government's 'mala fide unless proven otherwise' doctrine of governance. The premise of the government's policy framework seems to be that economic participants have mala-fide intent unless they can prove otherwise. This suspicion that every industrialist, banker, policymaker, regulator, entrepreneur and citizen is out to defraud the government has led to a complete breakdown of trust in our society. This has halted economic development, with bankers unable to lend, industrialists unable to invest and policymakers unable to act.

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The Modi government seems to view everything and everyone through a tainted prism of suspicion and distrust due to which every policy of previous governments are presumed to be of bad intent, every loan sanctioned considered undeserving and every new industrial project deemed to be crony in nature. And the government has positioned itself as some saviour, resorting to foolhardy moral-policing policies such as demonetisation, which have proved to be ill-thought-out and catastrophic. Wrongful evil characterisation of everyone and a 'good-vs.-evil governance' doctrine cannot be a recipe for healthy economic growth.

The role of social trust in economic development has been well-documented, right from the times of Adam Smith to the modern-day discipline of behavioural economics. The tearing of our social fabric of trust is the fountainhead of our current economic malaise. For economic growth to revive, it is very important that our torn social fabric of fear and distrust be stitched and knitted together to enthuse trust and confidence. It is very important for businessmen, capital providers and workers to feel confident and exuberant rather than being fearful and nervous. This is possible only if the government sheds its 'mala fide-unless-proven-otherwise' doctrine and begin to trust India's entrepreneurs.

India's economy is perched in a precarious state currently. Incomes are not growing. Household consumption is slowing. People are dipping into their savings to maintain similar levels of consumption. Headline GDP growth is accruing almost entirely to the creamy layer at the top.

The real worrying trend is that the [most recent retail inflation numbers](#) have shown a sharp increase, especially the food inflation figure. Retail inflation is expected to rise even further in the coming months. Continued increase in inflation combined with stagnant demand and high unemployment will lead to what economists term as 'stagflation', a dangerous territory from which it becomes very hard for large economies to recover. While we are currently not in stagflation territory yet, it is prudent to act quickly to restore consumption demand through fiscal policy measures since the impact of monetary policy seems muted.

It is my belief that India's fragile economic situation calls for the twin policy actions of boosting demand through fiscal policy and reviving private investment through 'social policy' by inspiring trust and confidence in the economic participants in our society.

India is now a \$3-trillion global economic powerhouse driven largely by private enterprise. It is not a tiny command and control economy that can be bullied and directed at will. Nor can it be managed through colourful headlines and noisy media commentary. Shooting down messengers of bad news or shutting off economic reports and data is juvenile and does not behave a rising global economic powerhouse. No amount of subterfuge can hide the performance and analysis of a \$3-trillion market economy of 1.2 billion people. Economic participants respond to social and economic incentives, not diktats or coercions or public relations.

Sadly, this self-inflicted economic wound comes at a time when there is a unique and opportune moment in the global economy for India to capitalise. The slowing down of China's economy and exports has opened up a large export opportunity for India to fill. India should aim to garner an elephant's share of this export opportunity by fostering a climate of confidence and economic dynamism away from the current climate of fear, distrust and pessimism. With the government having an absolute majority in the Lok Sabha and the global oil prices being low, this is a once-in-a-generation economic opportunity to catapult India to the next phase of economic development and create new jobs for hundreds of millions of our youth. I urge the Prime Minister to set aside his deep-rooted suspicion of industrialists and entrepreneurs and nurse us back to a confident and mutually trustworthy society that can revive the animal spirits and help our

economy soar.

Dr. Manmohan Singh was the Prime Minister of India from 2004 to 2014

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