Indian Elections: What policies should the new government put in place to boost business?

- India was the **fastest-growing economy** among G20 countries in 2018 with +7.4% GDP growth, above China (+6.6%). However, since the end of last year, the **economy has weakened** significantly: growth slowed (+6.6% y/y) below potential (+7%) in Q4 2018. Euler Hermes' new Now India Index points to further deceleration with a projected +6.2% in Q1 2019.
- However; if India manages to take advantage of the next cycle and avoid any policy mistakes, **the economy could reach the size of Germany's (USD4tn+) by 2025.**
- India's next government should seek to adjust policy settings to focus on **openness, infrastructure and strengthening private consumption to boost business and ensure stronger and sustainable growth over the long term.**

Paris, May 20th 2019 – With the results of India's general election, which began on last month, due on May 23rd, Euler Hermes identifies three steps the new government needs to take to boost business and ensure stronger and sustainable growth over the long-term.

A turning point for the Indian economy

India was the fastest-growing economy among G20 countries in 2018 with +7.4% GDP growth, above China (+6.6%), thanks to a better management of macroeconomic policies and clearer policy direction. However, Euler Hermes' Now India Index (NII)[1] suggests that **growth momentum slowed to +6.2% in Q1 2019** due to weaker private demand and uncertainties around the outcome of the general election.

But India's economic model is still well positioned to take advantage of the next cycle. The economy could reach the size of Germany (USD4tn+) by 2025. There are three things the next government needs to do to boost business:

Open markets to foreign capital and reduce protectionist measures

Despite the Modi administration's efforts to open the market to foreign capital, there's still a long way to go to address financial shortcomings and provide opportunities abroad.

Financial resources are limited as public debt is high (general government debt at around 70%) while the banking sector is constrained by high non-performing assets and savings are too low compared to investment. That is why maintaining the pace of reforms will be important to continue to draw investors' interest and maximize country's potential.

"*With an investment productivity of 3 (i. e. 3 units of capital are needed to create 1 unit of GDP) and a credit intensity of 1.4, India's potential returns on investment are higher than those in China, which score 6 and 3, respectively*" explains **Alexis Garatti, Head of Macroeconomic Research at Euler Hermes.**

In order to boost trade, a significant reduction of protectionist measures would also be necessary. Currently, India's tariffs are among the highest in the world (for e. g., 13.8% simple average Most Favored Nation applied, compared to 9.8% for China in 2017) and foreign companies still struggle to access the markets of goods and services.

[1] Euler Hermes' Now India Index (NII) tracks Indian economic activity based on five indicators: bank credit, air cargo freight, infrastructure output, cellular subscriptions and domestic vehicles sales figures

Implement a joint infrastructure industrial (I&I) strategy, with a strong focus on digital transformation

In parallel, a radical improvement of infrastructure will be crucial to boost domestic trade and accelerate an economic catch up. This has been difficult over the years because of a lack of financing and difficulty in execution.

The Modi government estimated that the country would need infrastructure investment of USD150bn per year between 2017 and 2022 to create a sustainable growth environment. "*However, based on the World Bank Infrastructure needs simulation tool, we calculated a much higher need of USD 203bn per year with significant needs in energy-related infrastructure and transport*", Garatti adds.

A further liberalization of the financial market could ease this financial burden by allowing foreign private investors to help in financing needed infrastructure projects.

Moreover, while India has the second-largest number of mobile phone and internet subscriptions in the world, only 37% of the population had access to the internet in 2018, compared to 53% worldwide. The country could still improve its edge on digitization as it has a huge potential considering the current growth rates (+17% growth in the number of internet users in FY2017-2018). Supporting digitization would benefit various sectors and infrastructure builders could take advantage from a rise in sales.

Strengthen private consumption

This is the last pillar for ensuring sustainable growth as it would provide a persistent boost to demand. While the joint infrastructure and industrial strategy will support a rise of the number of jobs and total income, a cost-effective redistribution strategy will be needed to address growing inequalities.

Authorities should provide more resources to the demand side of the economy by investing further in education and health. Furthermore, setting a minimum income guarantee could help strengthen private consumption.

B2C sectors, such as household electronics and electric equipment, the automotive sector, pharmaceuticals and consumer services, will directly also benefit from this redistribution strategy.

[You can find the full study here.]

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