MY VIEW | ECONOMIC GRAVITY

# Budget: It must aim to engineer India's economic transformation

*The target of Viksit Bharat by 2047 requires the budget to balance immediate challenges with long-term development goals*

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While annual budgets are routine affairs in advanced economies, they hold special significance in emerging markets, particularly in India. This colonial-era legacy has evolved from a mere accounting exercise to become a crucial platform for articulating the government's economic vision. As India approaches its budget for fiscal 2025-26, the stakes are particularly high, given the complex global and domestic challenges at hand.

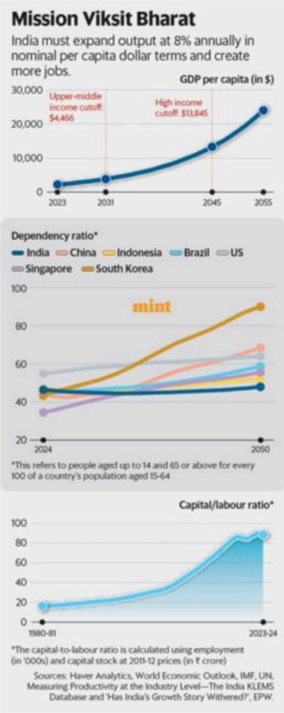
The international landscape presents multiple challenges. Ongoing geopolitical tensions from the Russia-Ukraine conflict, West Asian developments, recent US election outcomes and China's domestic issues all contribute to global economic uncertainty. These external factors can significantly influence India's economic planning and policy decisions.

At the same time, India's domestic economy faces several pressing issues. Economic growth has shown concerning signs, with the second quarter of 2024-25 recording a seven-quarter low of 5.4%. This slowdown prompted the Reserve Bank of India (RBI) to reduce its 2024-25 growth forecast downward by 60 basis points to 6.6%. Simultaneously, persistent inflationary pressures, particularly in food categories, have led to an upward revision of its inflation projection by 90 basis points to 4.8%. The situation is further complicated by the rupee's depreciation to historic lows, substantial equity market outflows and volatile oil markets. RBI's recent adjustments to CRR (cash reserve ratio) requirements reflect its efforts to manage tightening liquidity conditions.

Against this backdrop, the 2025-26 budget must address three critical pillars that will shape India's journey towards developed-nation status, each presenting unique challenges and opportunities that demand careful policy calibration.

*First*, India would need to maintain an 8% growth rate in nominal per capita dollar terms to achieve 'Viksit Bharat' by 2047, a target that requires a sustained focus beyond short-term economic fluctuations. This growth trajectory would enable the country to reach upper middle-income status by 2031 and high-income status by 2045. Assuming about 1% population growth, 2-3% depreciation, this would be equivalent to 11-12% nominal GDP growth. While this target aligns with India's average growth over the past two decades, sustaining such rates for another 20 years presents a significant middle-income-trap challenge.

*Second*, on employment, there is an often-overlooked connection between India's labour market challenges and its international trade position. India is a labour-abundant country, and is still expanding its productive cohorts while advanced economies and other emerging markets are contracting. Yet, India's production and exports are becoming increasingly specialized in capital-intensive industries, seemingly contradicting the basic yet powerful principle of 'comparative advantage.' According to this principle, a labour-abundant country must specialize and export goods in labour-intensive industries, and importantly also import goods which it can produce only at comparatively high 'opportunity cost.'

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The solution to this paradox would be essential to generate high-quality employment opportunities. We could benefit from a strategic focus on sectors that combine strong export potential with significant job creation capabilities, particularly in the textile industry, and in high value agricultural production.

The assembly sector presents a significant opportunity too, despite concerns about low domestic value addition. If India can achieve scale in assembly operations, the total domestic value added and employment benefits could be substantial. Success in this area requires establishing stable positions in global value chains.

*Finally*, India's public finances warrant ongoing monitoring. Despite the government's laudable efforts at fiscal consolidation and implementation of transparent and prudent budgetary frameworks, the country's debt-to-GDP ratio continues to exceed that of comparable economies. The Centre currently allocates close to 40% of its revenues to debt servicing, significantly above the emerging market average of 10%. This situation necessitates careful deleveraging, which can also improve sovereign ratings and create more fiscal space for development initiatives.

The time may also be right to consider establishing an independent Fiscal Council, as recommended by the FRBM Review Committee and the 15th Finance Commission. Such a body could complement government efforts by providing independent forecasts of key macroeconomic variables and by monitoring fiscal developments, enhancing the credibility of India's fiscal framework.

Overall, the 2025-26 budget represents a crucial opportunity to signal India's economic direction and vision. Achieving developed-economy status is possible through sustained macroeconomic and political stability, coupled with continued investment in physical and digital infrastructure. However, success will ultimately depend on effective implementation of policy decisions.

The budget must balance immediate economic challenges with long-term development goals. While maintaining fiscal prudence, it needs to create conditions for sustainable growth, employment generation and structural transformation. Most importantly, the focus must be on swift and effective implementation of policies and reforms.

The decisions made in this budget can significantly influence India's development trajectory over the next two decades. As India aspires to become a developed nation, the mantra must be 'implement, implement, implement,' turning vision into reality through decisive action and efficient execution. Best wishes for 2025 to all Economic Gravity readers.

*These are the author's personal views.*

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