Tackling synchronized downturn
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President elect Obama must have known that the US economy had declined by 0.5 percent when introducing his economic team to the press. The writing on the wall is clear. The US economy is in and this will perhaps extend well into 2009. It is therefore, rather puzzling and in fact dismaying that none of our senior economic policy makers cared to mention the likely impact of a synchronized downturn in the US, Japan and the EU on Indian economic prospects even once in their meetings with economics editors. In my view this state of denial in refusing to face up to the seriousness of the crisis we are now faced with can cost us dear. To continue to talk of achieving 8 percent growth as the Prime Minister did in the Hindustan Times summit and for the Planning Commission not to revise down its Eleventh Plan growth targets, leave me perplexed. I just hope that the task force established by the Prime Minister is seized of the severity of the situation and is preparing a credible and effective plan to prevent the downturn from becoming longer and deeper than it already threatens to be.

There will be a tendency, when external demand is set to shrink, to try and protect the domestic market for our indigenous industry by raising tariffs and even bringing back some of the non-tariff barriers to restrict imports. In industries such as steel and edible oils where imports duties were brought down to compensate for the extraordinarily high international prices, it is justified to take them back to their original levels. This has been done already. It will, however, be a mistake to now extend this to other industry segments even if this is being lobbied for by industry associations or specific industry segments. This has to be resisted at all costs. Instead if the Indian industry has to achieve the much needed higher productivity and lower cost levels, only on the basis of which can it achieve higher growth rates. An immediate issue quite expectedly, is with manufactured imports from China which are apparently available at unbelievably low prices. These imports are gaining market share even in industry segments, that are relatively technology and design intensive, and in which Indian firms were hitherto seen as being more competitive as demonstrated by their net export earnings. The reason for the surge in Chinese imports is not always that these exports are hugely subsidized by the Chinese government as is often claimed by our industry representatives. In cases in which this can be established, anti-dumping measures must be taken and with far greater alacrity than is the case now. The entire system needs thorough revamping through a coordinated action between the Departments of Commerce and Industry, both of which are thankfully under the same minister. But for the great majority of imports from China, we must face the reality that they are cheaper because of the enormous economies of scale that are being achieved by Chinese manufacturers. As a recent study in ICREIR on Chinese manufacturers (by Rajeev Anataram) done as part of a larger ADB project, shows, Chinese firms are able to achieve these scales as a direct result of close collaboration between the firms and government agencies at all levels including the central, provincial, local and often with help from the PLA in providing large orders to sustain production at higher levels. These huge capacities in Chinese firms created to support their sizzling growth are now relatively underutilized and so it is natural for them to look to fresh large markets to which these can be exported often at marginal variable costs. Can we stand up to this competition or should we simply accept that the Chinese have now made it impossible for India to retain its manufacturing base?

Some will tend to argue that it does not matter if jobs come from manufacturing or services or agriculture sector as long as enough of them are being generated. The same group of people also tend to argue, despite all recent evidence to the contrary, that markets and private entrepreneurs, if left to themselves will find a way forward to achieving full employment. This is simply balderdash. Markets need to be effectively regulated and private entrepreneurs need the fullest support of the government if they are to become globally competitive and even retain their share in domestic markets. But this support, unlike what my friends in our industry associations may say, is neither effective and certainly not efficient if given in the form of higher tariffs and non tariff barriers.

Instead all attention must now be focused on identifying the constraints across the 'full value chain' that add to costs and make specific industry segment uncompetitive. Public policy has to be directed at all those constraints. These are often but not always in the nature of government procedure, red tape, unnecessary laws and regulations which can never be complied with despite best efforts, and better access to formal credit at rates which are internationally comparable. But detailed industry specific inquiry is required. Such a review is urgently needed and could start with sectors where India's relative comparative advantage is clearly established. Coordinated action by the three ministries of industry, commerce and finance and their related agencies will be key to successfully taking this forward. I suppose this could be a useful mandate of the Prime Minister's task force on tackling the economic downturn.

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