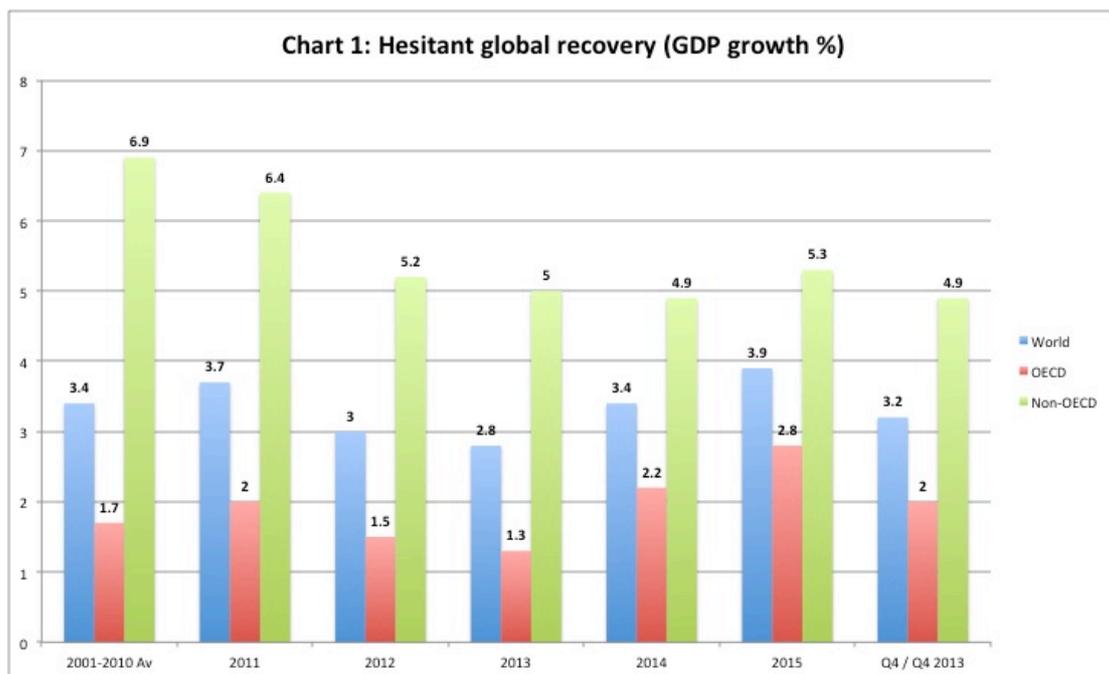


No Help from Abroad

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With India's integration with the global economy through trade and investment flows having increased significantly over the last quarter of a century, the days when domestic economic performance was relatively insulated from global trends are over. So as the new government begins its tenure and there is much anticipation about what it would deliver in the short and medium term, it may be useful to consider the global environment it faces. That environment influences both policy space and economic outcomes through many routes: through capital flows and its impact on currency value, through its impact on export performance, and through the cost of imports, to name a few.

The OECD Secretariat has just recently put out a set of estimates and [projections of global growth](#). Its projections are optimistic and predict a revival of growth over 2014 and 2015. But the background to those projections suggest that this may be one more of the many instances in the recent past when forecasters proclaimed that green shoots of recovery had been sighted, but were proved wrong as the recession persisted.



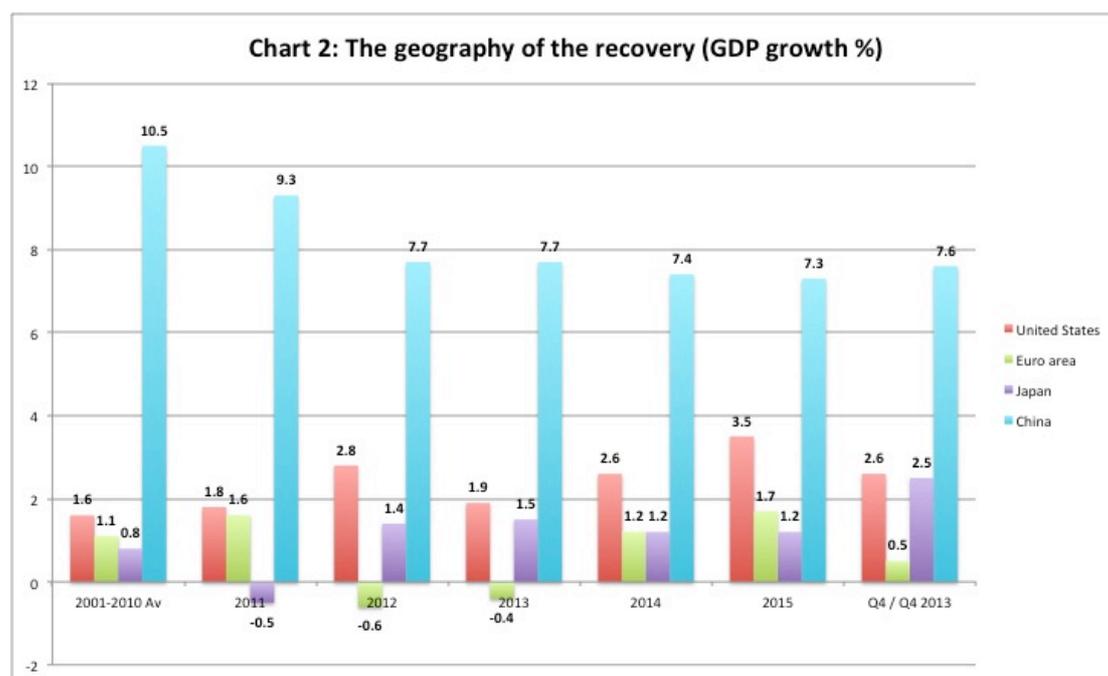
Thus, as Chart 1 shows, the OECD projects growth in 2014 at 3.2 per cent and that in 2015 at 3.9 per cent.

That is a definite improvement from the 2.8 per cent recorded in 2013. A close reading indicates that two factors seem to explain the OECD's optimism. First, the figures on growth of real global GDP points to a decline from 3.7 per cent in 2011 to 3 per cent in 2012 and 2.8 per cent in 2013. The continuous decline is disconcerting, suggesting that the withdrawal of fiscal and monetary stimulus packages in most OECD countries as part of a return to a 'business-as-usual' policy scenario has stifled the recovery that the packages had delivered. The root causes of the recession have not been addressed it would appear. But, what seems to have provided the OECD Secretariat some reason for comfort is the fact that the extent of decline in the rate of

growth has shrunk from 0.7 of a percentage point between 2011 and 2012 to 0.2 of a percentage point between 2012 and 2013. This is perhaps, rather hastily, being read as evidence of a bottoming out of the recession.

A second factor that is possibly providing the grounds for the OECD's growth optimism is that global growth in the fourth quarter of 2013 (relative to the corresponding quarter of 2012) had 'risen' to 3.2 per cent as compared to 2.8 per cent over 2013 as a whole. But this may not be reflective of a trend. In fact, already there is evidence from the United States that it does not. According to the "second" estimate released by the Bureau of Economic Analysis of the US government, real gross domestic product decreased at an annual rate of 1.0 per cent in the first quarter of 2014 as compared with the increase of 2.6 per cent it registered in the fourth quarter of 2013. So the trend is downhill rather than upward.

There are other questionable features underlying the OECD's optimism. Thus, in the past it was the non-OECD countries that were expected to hold up global growth by continuing to cruise along high-speed lanes in the global growth highway, relatively untouched by the recession in the OECD areas. But starting now, the OECD is being seen as being the area that would begin to pull the global economy out of deceleration. Here again fourth quarter GDP estimates seem to be the basis.



There are two factors that are expected to contribute to the turnaround. One is a recovery in the Euro area (from -0.4 to 1.2 per cent) and the other is a growth pick up in the US (from 1.9 to 2.6 per cent) (Chart 2). Neither of these is likely to be true. As noted earlier, advance estimates for Q1 2014 in the US point to a deceleration in growth. In fact, the big picture seems to be that the post crisis recovery (facilitated by huge stimulus packages and easy money policies) in parts of the OECD has been followed by a deceleration in growth across the world, with the picture till 2013 being one of stagnation at most. Even China is in slowdown mode, even if still at a high growth level.

The fact that OECD growth is the basis for optimism is also surprising because most OECD countries are now focused on fiscal consolidation. The OECD Secretariat projects that the fiscal deficit to GDP ratio will fall from 6.4 to 4.6 per cent of GDP in the US between 2013 and 2015, and from 4.6 per cent to 3.2 per cent in the OECD as a whole. Yet, the projection is one of recovery. The case for this optimism is by no means clear. To boot, the global imbalances that were partly seen as the cause of the 2008 crisis still remain after years of adjustment. In fact, the current account deficit in the US is expected to increase from \$379 billion to \$544 billion between 2013 and 2015.

Overall, therefore, it is more than likely that global growth would remain low and sluggish over the next two years or even more. The impact of that on the trade in goods and services is bound to be adverse. Between 2011 and 2013, for example, world trade growth more than halved from around 6.5 per to 3 per cent. That is not good news for an India looking to become a low-wage, labour intensive manufacturing hub along the global value chain. In the circumstances, it does appear that the external economic environment confronting the new government is by no means favourable.

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