

Poor credit disbursal and visible green shoots: Paradoxical mismatch

The pertinent question that one needs to ask is: Is credit growth declining due to a lagged effect of a weakened demand being faced by corporates?

JAGADISH SHETTIGAR (HTTPS://WWW.MONEYCONTROL.COM/AUTHOR/JAGADISH-SHETTIGAR-10591/) & POOJA MISRA (HTTPS://WWW.MONEYCONTROL.COM/AUTHOR/POOJA-MISRA-10601/) OCTOBER 14, 2020 / 05:44 PM IST

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The coronavirus pandemic has sent financial markets worldwide into a tailspin. In order to provide a relief from its adverse impact, an amalgamation of monetary, fiscal and regulatory interventions were announced by the government along with the Reserve Bank of India (RBI).

The corrective measures were initiated to mitigate the negative impact of the novel coronavirus on the demand as well as supply side of the economy and to ensure close to normal functioning of the financial markets.

The RBI in no way failed to respond to the unprecedented economic crisis due to pandemic. Series of monetary measures were announced to strike a balance between financial stability, preserving the economic value of businesses and protecting depositors. It was done to shield the macroeconomic and financial environment from the negative influence of the virus and mitigate its bearing on credit demand and asset quality of scheduled commercial banks. The easing of financial

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conditions was done to boost system level liquidity and sector specific funding. However, it needs to be investigated if the deployment of conventional and unconventional tools that the RBI resorted to for restoring financial stability has yielded the desired results?

Analysis of credit and deposit growth numbers showed that deposit growth has been on a rise and clearly outweighs credit growth numbers in the Indian economy. Rather, credit growth numbers in March stood at 5.9 percent as against deposit growth numbers at 8.6 percent. This brings to light that against the backdrop of a weak macroeconomic environment there could be a risk aversion by banks and a growing preference for them to park the excess money in safer and less risky instruments or alternately demand for credit by businesses and corporates as planned by RBI has really not taken off.

As per data under the reverse repo window there has been a dramatic increase in deposits by banks with RBI from Rs 41,214 crore as on January 1 to over Rs. 6.3 lakh crore on May 28. Is this a reflective of the fact that businesses which have been facing the onslaught of liquidity stress and tightening of financial conditions amidst disruptions of cash flows and working cycles are still not borrowing?

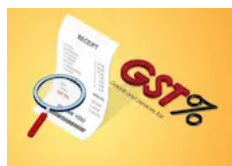
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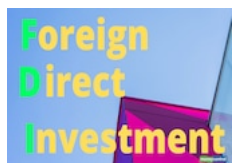
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On further investigating the credit and deposit growth numbers it can be seen that deposit growth (8.6 percent in March) clearly outweighs credit growth (5.9 percent in March) in the Indian banking system. The inability to lend has become so dominant that banks have huge amounts of cash lying unutilised. This clearly outlines a lack of credit-offtake in the Indian financial system.




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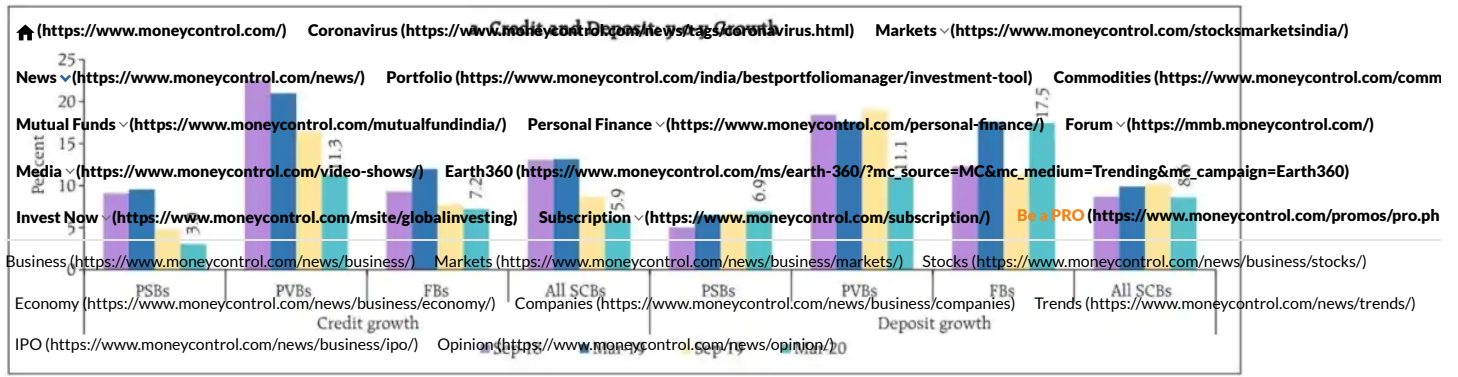
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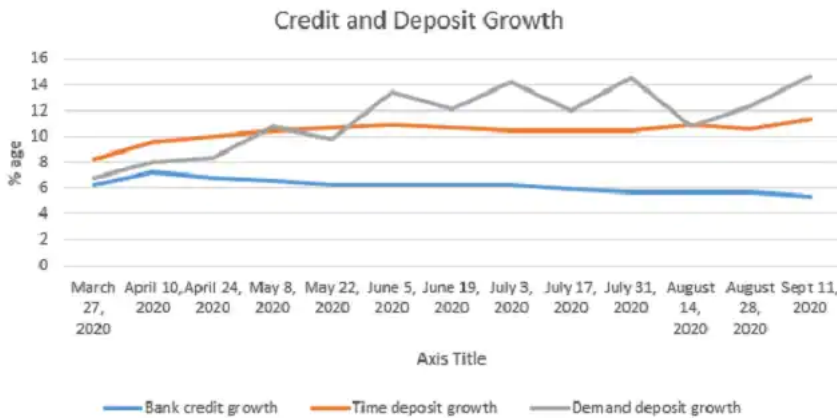
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(Source: RBI's Financial Stability Report, 2020)

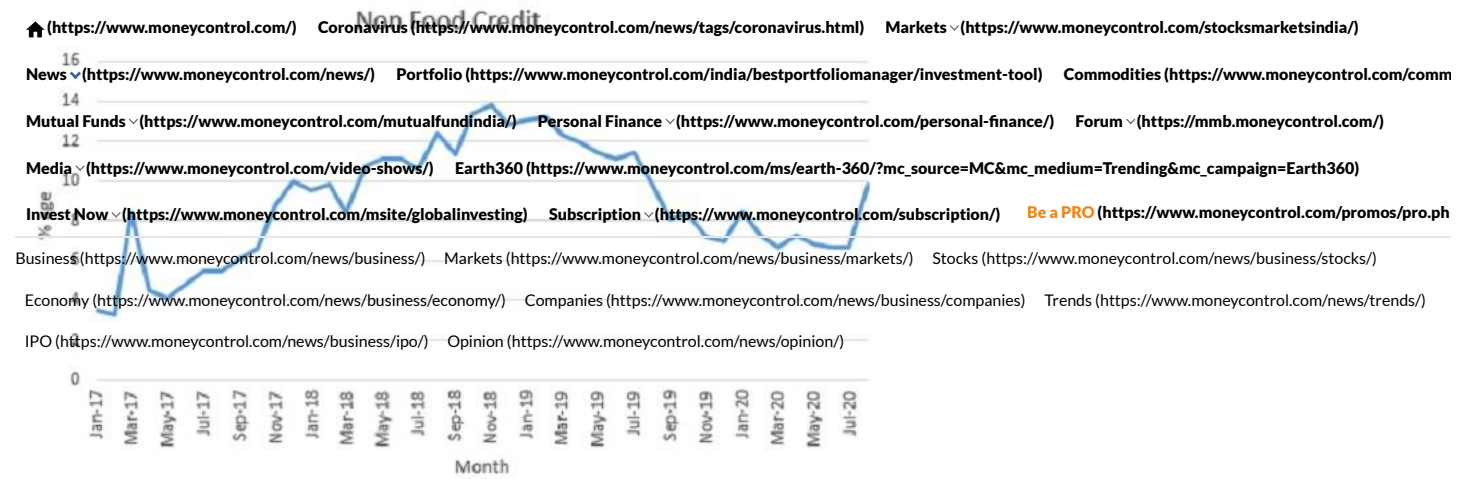
A micro level analysis of bank credit growth, time deposit growth and demand deposit growth numbers shows that bank credit, which was already on a decline in Q3 and Q4 of 2019-20 witnessed a further downswing. Rather, the difference between deposit and credit growth numbers for India has widened even more during the pandemic. Contrary to RBI infusing liquidity in the financial system, bank credit growth which in March 27 was at 6.3 percent saw a fall to 5.4 percent as on September 11. It only witnessed a temporary increase to approximately 7 percent in April. So, the pertinent question is: Are corporates not engaging in borrowing from banks?



On the flip side, deposit growth numbers YoY on account of private commercial banks have shown a steady upswing during the pandemic. Growth in time deposits has increased from 8.2 percent YoY as on March 27 to 11.4 percent YoY as on September 11. Additionally, demand deposits have also shown a growth from 6.8 percent YoY as on March 27 to 14.7 percent YoY as on September 11. One must be cognizant that this growth in time and demand deposits has happened despite lowering of interest rates by the lenders on term deposits and savings bank accounts. In the backdrop of the pandemic is this reflective of the fact that the precautionary savings motive is being highly dominant as against the transaction and speculative motives of money?

On further investigating deployment of gross bank credit by major sectors, it is being witnessed that non-food bank credit growth is on a downswing. In July, non-food bank credit growth stood at 6.7 percent in July (same as in June) but lower than the growth of 11.4 percent in July 2019. August data shows no different results. On a YoY basis, in August, non-food bank credit growth decelerated to 6 percent from 9.8 percent in August 2019. Credit growth to industry decelerated to 0.5 percent in August from 3.9 percent in August 2019 and to 0.8 percent in July as against 6.1 percent growth in July 2019.





Decline in demand for non-food bank credit growth reflects a declining demand by industry and coincides with declining demand in the economy and falling capacity utilisations. On the flip side, thrusting in money into banks and financial institutions without boosting demand could result in increasing of bad loans and non-performing assets. The excess liquidity in the financial system could result in a huge social cost. This could lead the country into a liquidity trap with a large increase in money supply and not much use of it by corporates and households.

Thus, the pertinent question that one needs to ask is: Is credit growth declining due to a lagged effect of a weakened demand being faced by corporates? Have supply side interventions been able to clear supply-side bottlenecks in the Indian economy and generate demand? Signs of green-shoots observed in the month of September do indicate revival of the economy. Purchasing Managers' Index (PMI) at 56.8 was the highest in eight and half years; GST collections at Rs 95,480 crore was the post-pandemic record collections and also 4 percent higher than the corresponding month of the last year; E-way bills at 57.4 million set a record; power demand at 169,000MU showed 4.8 percent increase. Importantly, the number of persons seeking support from MGNREGS at 29 million was the lowest since May which is a definite sign of improvement in employment opportunities. The FPIs would not have become net buyers of Indian debt instruments after 11 months without seeing positive signal in Indian economy.

Pick up in consumer demand is likely to get further intensified during Q3 and Q4 of FY21. In this highly uncertain economic environment retailers are pinning their hopes on Q3 festive demand i.e. from Diwali to the onset of the New Year 2021 to revive flagging sales. Festive season typically accounts for 20-30 percent of the annual sales and businesses are waiting with bated breath for the season to yield positive results for them. Attractive offers are being lined up to influence consumer demand and the pedal has been pressed on aggressive promotions and advertising campaigns. To be able to bring cheer and respite from the pandemic linked slumber it is time for companies to woo back customers through behavioural nudges.

However, baffling question here is the mismatch between RBI's noble intentions in facilitating availability of liquidity vis-a-vis the corporate sector's unenthusiastic response in availing the offer. Does it mean that the corporate sector is flush with cash and hence need not rely too much on the banking system? In a way it is a good sign now that the government borrowings is to expand horizontally as well as vertically.

(Dr Jagadish Shettigar is Professor, Economics, Birla Institute of Management Technology, Greater Noida and Dr Pooja Misra is Associate Professor, Economics, Birla Institute of Management Technology, Greater Noida)

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Moneycontrol understands that one of the options being given to the states is continuing compensation in lieu of tax shortfall at a much lower rate than the existing 14 percent. It could be 11 percent or lower. It is also learnt that the centre is presenting to states some revenue enhancement measures which will enable them to depend less on the shortfall compensation from the centre.

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The Goods and Service Tax Council is unlikely to reach a final decision on the ways in which to extend compensation to states beyond June 2022, *Moneycontrol* has learnt.

It is understood that the centre has given a presentation to states and laid out options on how the compensation can be extended beyond its end-date next year. However, the states are likely to be given time to decide which option suits them best, said an official who is aware of the deliberations in the GST Council meeting.

"The centre believes that beyond June 2022, annual compensation of Rs 1 lakh crore should be enough. States believe that more than that is required," said an informed source.

The person added that any decision on either the mode of compensation beyond June 2022 or on inclusion on petroleum products under GST is unlikely today, though the latter topic has also been discussed in the Council meeting.

The meeting of the all-powerful federal body, being chaired by Finance Minister Nirmala Sitharaman and being attended by all but seven state Finance Ministers, **is currently taking place in Lucknow (<https://www.moneycontrol.com/news/business/economy/packed-agenda-for-first-in-person-gst-council-meeting-in-nearly-two-years-7475451.html>)**. Sitharaman will address a press conference after 6.30 PM.



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Moneycontrol understands that one of the options being given to the states is continuing compensation in lieu of tax shortfall at a much lower rate than the existing 14 percent. It could be 11 percent or lower. It is also learnt that the centre is presenting to states some revenue enhancement measures which will enable them to depend less on the shortfall compensation from the centre.

While the centre had in-principle agreed to extend the compensation cess and the shortfall due to states last year itself, the modalities and details are being the Lucknow meeting.

When the GST came into being, states had agreed to join the new tax regime provided they were compensated for any revenue loss in the first five years from July 1, 2017 to June 2022.

Section 18 of the Constitution (101 amendment) Act, 2016 and Section 7 of GST (Compensation to State) Act, 2017 permits that the loss of revenue will be compensated to states at the end of every two months for five years. The shortfall is calculated assuming a 14

percent annual growth in GST revenue over the base year of 2015-16.

As per the centre's perspective, the pandemic has hit the finances of the centre as much as the states and hence to compensate states at an assumed rate of 14 percent GST growth, something which was decided pre-COVID, may no longer be possible.

For the current 2021-22 financial year, the centre has already released Rs 75,000 crore to the states and union territories to compensate them for the shortfall in GST revenue.

This is not the first time that states have been presented **options on compensation due to GST shortfall.** (https://www.moneycontrol.com/news/business/economy/explained-why-gst-council-cant-arrive-at-a-consensus-on-compensation-issue-5962391.html)

In the GST Council meeting on August 27, 2020, in light of a massive hit to revenues due to the COVID-19 pandemic, Sitharaman had proposed two options to states - to either borrow Rs 1.1 lakh crore (on account of GST implementation) through a special window facilitated by the RBI, or to borrow the complete shortfall of Rs 2.35 lakh crore (including Rs 1.8 lakh crore due to COVID) from the market. The states were given time, and most had chosen the first option.

The states whose Finance Ministers are not attending the current meeting in Lucknow are Gujarat, Maharashtra, Tamil Nadu, Karnataka, Chhattisgarh, Meghalaya and Mizoram.

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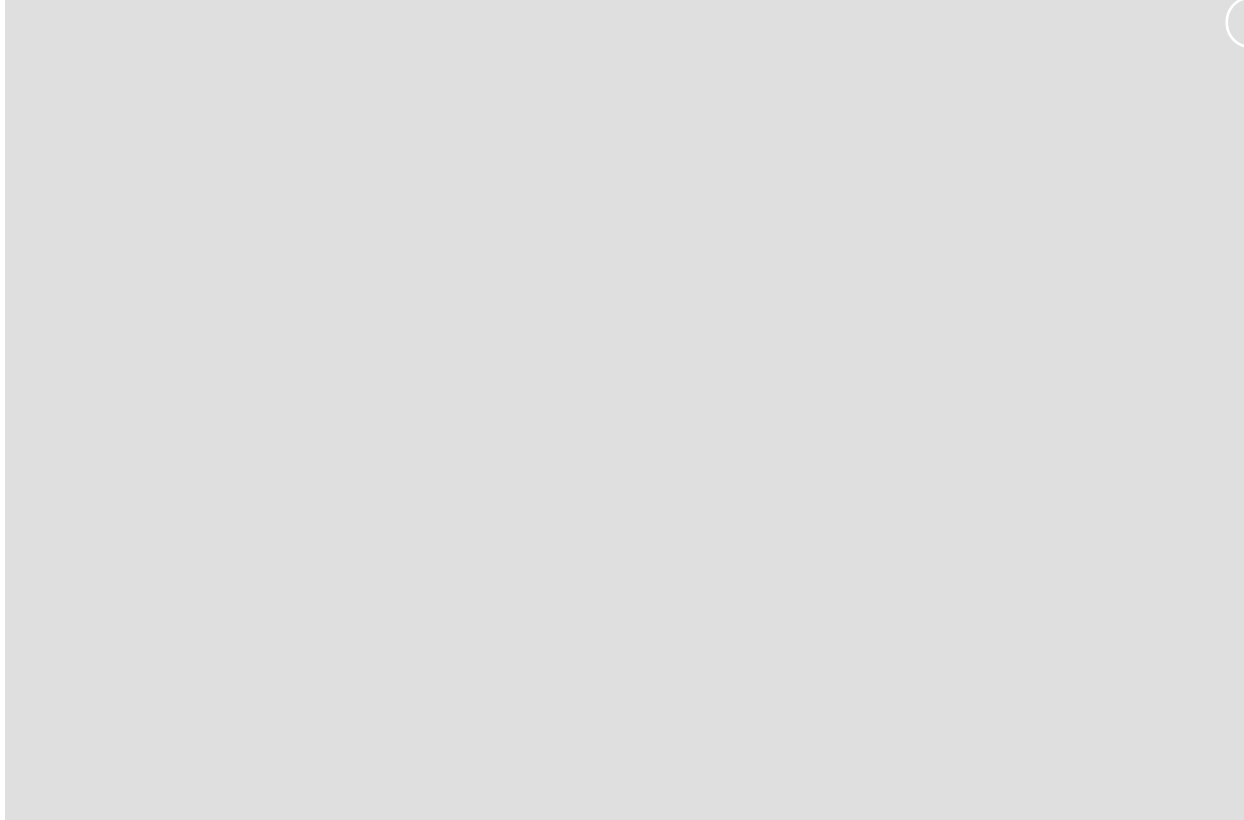
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India woos ASEAN with generics production, vaccines, wants support in IPR waiver

Apart from securing the support of ASEAN nations for the global intellectual property waiver for COVID vaccines, the move is also aimed at pulling closer the traditional partners in the bloc, who have become close to China, sources say

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Flags of ASEAN nations. Representational Image.

India has promised the Association of Southeast Asian Nations (ASEAN) full cooperation in generic drug manufacturing, for which the bloc of nations is increasingly becoming dependent on China.

This comes in exchange for ASEAN's support to New Delhi's bid for the global intellectual property rights waiver for COVID-19 vaccines at the World Trade Organization (WTO), sources say. As reported by Moneycontrol earlier, **talks on the IPR waiver have stalled**

(https://www.moneycontrol.com/news/business/trade/exclusive-deadlock-on-vaccine-waiver-issue-at-wto-continues-at-latest-meet-7150051.html) and support from the 10 ASEAN nations remain crucial.

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At the recently concluded 9th East Asia Summit Economic Ministers' Meeting, India promised East Asian partners its willingness to collaborate in the production of generic drugs, medical technologies to treat COVID-19 patients, and vaccines production.

Up to 70 percent of the global vaccines are produced in India and its large capabilities in producing standardized affordable medicines are globally recognized. Reeling under successive waves of COVID-19, and having a mixed bag of experiences with regards to Chinese vaccines, the ASEAN nations have responded favorably to India's overtures, External Affairs Ministry sources said.

Generic generosity

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Search 'covid vaccine near me' on Google to book a slot, says Health Minister Mansukh Mandaviya

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According to the Department of Pharmaceuticals, India exports one-fifth of global generic drugs by volume. As domestic companies ramp up production, India has held firmly to its long-established moniker of 'the pharmacy of the world'. India's pharmaceuticals industry is the third-largest in the world, with the majority of it focused on generics.

On the other hand, China is a major producer and exporter of low-cost, high-volume active pharmaceutical ingredients (APIs), which go into the making of drugs. China accounts for around 40 percent of all APIs used worldwide while India's dependency on China is an estimated 65-70 percent.

To reduce this, the government had announced a production-linked incentive scheme of Rs.6,940 crores, which seeks to provide financial incentives to eligible manufacturers of 41 products covering 53 APIs.

"To make the scheme even more attractive, the government has later allowed exports under the scheme as well. We have informed the Asean Bloc that exports to their region would not be restricted," a senior official said.

WTO hurdle

Even after talks gained pace in June, nations failed to meet the early August deadline given the differences

on the subject.



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The powerful TRIPS Council had on June 9 cleared India's proposal <https://www.moneycontrol.com/news/business/economy/wto-decides-to-hold-text-based-negotiations-on-indias-global-vaccine-waiver-proposal-7010561.html> for a further debate by all members. All WTO actions are passed only by the full consensus of all members.

It seeks to suspend certain provisions of the TRIPS agreement, which came into effect on January 1, 1995, and is to date the most comprehensive multilateral agreement on intellectual property.

However, it has been hailed as a model law for protecting the commercial rights of countries and corporations, given that it extends the protection for new varieties of plants, the layout designs of integrated circuits, and undisclosed information, including trade secrets and test data.

Suspending parts of this agreement will allow countries to overcome the legal challenges posed by patents to timely provisioning of affordable medical products. Some WTO nations have had to carry out urgent legal amendments to their national patent laws to expedite the process of issuing compulsory/government use licences.

If the proposal becomes global law, **a massive ramp-up in the manufacturing of vaccines is expected** <https://www.moneycontrol.com/news/business/economy/explained-how-the-us-decision-to-back-indias-proposal-at-the-wto-may-end-the-global-pandemic-sooner-than-expected-6859861.html>, especially in poorer nations, which will now get access to the technology and resources to manufacture vaccines.



SUBHAYAN CHAKRABORTY has been regularly reporting on international trade, diplomacy and foreign policy, for the past 6 years. He has also extensively covered evolving industry and government issues. He was earlier with Business Standard newspaper.

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Packed agenda for first in-person GST Council meeting in nearly two years

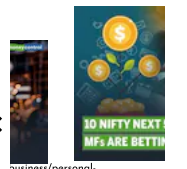
The Council is expected to discuss the extension of compensation to states beyond 2022, rationalizing the inverted duty structure on supply chain of certain items, bringing petrol and diesel under GST, extending the GST exemption on Covid-essential items, and deciding the future of profiteering cases, since the tenure of the National Anti-Profitteering Authority ends in November.

ARUP ROYCHOUDHURY |

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Poor credit disbursal and visible green shoots: Exclusive! GST Council: Decision on mode of India woos ASEAN



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File image of Finance Minister Nirmala Sitharaman (Image: Twitter/@FinMinIndia)

Finance Minister Nirmala Sitharaman will chair the 45th meeting of the Goods and Service Tax Council in Lucknow on September 17. It will be the first in-person meeting of the all-powerful federal body in nearly two years. And given the loaded agenda, it is likely to be an action-packed one.

The Finance Minister and her counterparts from States and Union Territories are expected to discuss the extension of compensation to states beyond 2022.

They are also likely to deliberate on rationalizing an inverted duty structure on the supply chain of certain items, bringing petrol and diesel under GST, extending the GST exemption on Covid-essential items, and deciding the future of profiteering cases since the tenure of the National Anti-Profitteering Authority ends in November.

"The GST Council is physically meeting after a long time, and the industry is keenly looking forward to this meeting. Issues such as bringing petroleum products, natural gas under GST ambit, capacity-based taxation for tobacco products, future of compensation levy, GST rate rationalizations are expected to be discussed in the meeting," said Rajat Bose, Partner, Shardul Amarchand Mangaldas & Co.

"It will also be interesting to see if the GST council extends the GST exemptions for essential COVID supplies for a further period," Bose said. The last in-person GST Council meeting was held in December 2019 in New Delhi. Since then five more meetings have been convened through video conferences.



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<https://www.moneycontrol.com/news/business/pan-aadhaar-linkage-deadline-extended-till-march-2022-7479181.html>

Compensation Extension

While the centre has in principle agreed to extend the compensation cess and the shortfall due to states, the modalities and details will be discussed at the Lucknow meeting. It is understood that the centre will present various options for a compensation formula

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GST Council: GST on supply of bricks increased from 5% to 12%

<https://www.moneycontrol.com/news/business/real-estate/gst-council-gst-on-supply-of-bricks-increased-from-5-to-12-7479071.html>

When the GST came into being, states had agreed to join the new tax regime provided they were compensated for any revenue loss in the first five years from July 1, 2017, to June 2022. It was in October 2020 that the Council had decided, in principle, to extend the compensation beyond the original five years.

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GST Council | Centre says no compensation beyond June 2022; states take a different view

<https://www.moneycontrol.com/news/business/economy/gst-council-centre-says-no-compensation-beyond-june-2022-states-take-a-different-view-7478861.html>

Section 18 of the Constitution (101 amendment) Act, 2016 and Section 7 of GST (Compensation to State) Act, 2017 permits the loss of revenue will be compensated to states at the end of every two months for five years.

The shortfall is calculated assuming a 14 percent annual growth in GST revenue over the base year of 2015-16. One of the points of discussion is whether to stick to this assumed rate beyond 2022.

“The pandemic has hit the finances of the centre as much as the states. To compensate states at an

assumed rate of 14 percent GST growth, something which was decided pre-Covid, that is something we will discuss with states,” a senior official told Moneycontrol.

For the current 2021-22 financial year, the centre has already released Rs 75,000 crore to the states and union territories to compensate them for the shortfall in GST revenue.

Petroleum Products under GST

More than four years after the implementation of the nationwide GST, the Council seems finally ready to discuss bringing petrol and diesel under GST. However, this issue is understood to be a complex one, and it will take many meetings before a decision is made on the issue.

This comes at a time when petrol and diesel prices are reaching record highs across the country due to incessant hikes in rates since May. Central and state-level taxes contribute about 55 percent of the retail price of petrol and 51 percent for diesel.

The Centre’s excise duty collection in 2020-21 was Rs 3.9 lakh crore, about 62 percent higher than the Rs 2.4 lakh crore in 2019-20. Out of the Rs 3.9 lakh crore, Rs 3.45 lakh crore was collected only in excise duties on petroleum products. In just the April-June quarter of the current financial year, the Centre collected about Rs 94,181 crore in revenue through excise duties on petrol and diesel.



States have also used their taxation power on fuel to raise resources. The price of fuel differs from state to state, depending on the rate of local taxes like VAT and also freight charges in that state, as the attached charts show.

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It is essential to overcome the challenges arising from the inverted duty structure on certain products, in addition to extending relief for pharma products required for treatment of Covid patients," said MS Mani, Senior Director, Deloitte India.

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The Council will take up the matter of inverted duty structure on the advice of the Supreme Court.

A recent judgement by the apex court had clarified that a refund of unutilized input tax credit will not be available in case of a refund due to an inverted duty structure. The Court in its judgement has accepted that there is an anomaly in the formula for computing the quantum of eligible refund and has urged the GST Council to reconsider and take a policy decision regarding the same.

The Council will also take up the matter of how to deal with profiteering cases. It may also take a call on extending the concessional rates for Covid-19-related drugs, including remdesivir, by another three months.

The Council will decide whether the term of the National Anti-Profiteering Authority will get over after November 30, and instead, the Competition Commission of India (CCI) or any other authority could be given its mandate.

ARUP ROYCHOUDHURY

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