From Export-led to Consumption-led Growth?

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A CHORUS of “establishment” voices, from consultancy firms to the financial press, has been demanding a boost to domestic consumption as a means of reviving the flagging growth rate of the Indian economy. The latest to join this chorus is the Reserve Bank of India which in its latest Bulletin has asked for a boost to consumption to “rekindle the animal spirits” of the “entrepreneurs” in the economy.

Two points are to be noted about the concern underlying this chorus: first, if India’s growth rate, originally predicted to be 7 per cent in 2024-25 is now expected to be only 0.5 per cent lower, then that cannot possibly explain such agitation. After all 6.5 per cent is a high enough rate of GDP growth by any standards, and cannot be considered a sign of flagging “animal spirits” that should worry the “establishment” economists. Such concern suggests that this entire growth rate calculation, even within the ambit of the normal GDP concept that itself is deeply flawed, represents a gross overestimate. Second, as the RBI makes clear, the concern it has is with urban middle class consumption and not the consumption of the working people.The boost to consumption it is talking about is urban middle class consumption. This emerges from the following.

If the idea was to boost aggregate demand through the consumption of the labouring poor, then an obvious way of doing so would be to raise the wage rate across the board and that could be effected by raising the statutory minimum wage rate. But no one is talking along these lines; on the contrary, the chairman of Larsen and Toubro has demanded, and no other “captain of industry” has explicitly differed from him, that working hours should be raised to 90 per week! This would make factories in India resemble the Nazi concentration camps where the inmates were worked to death; in fact his argument that workers would be better off working than staring at their wives at home, that more work rather than leisure enriches life, is eerily similar to the notorious words in wrought iron over the entrance gate to the concentration-cum-death camp at Auschwitz: “Arbeit Macht Frei” or “Work Makes One Free”. So, the Indian “establishment” is not talking about boosting the consumption of the labouring poor.

Even as far as the urban middle class is concerned, the means of boosting its consumption are seen to lie in a moderation of food price inflation. Now, food price inflation obviously must be curbed, but the question here is: what is its impact on aggregate demand? After all the beneficiaries from food price inflation are also consumers; so, is the consumption demand lost among the urban middle class owing to food price inflation greater than the consumption demand gained among the beneficiaries of food price inflation? Since the latter, namely the gainers from food price inflation do not necessarily have a higher savings ratio than the urban middle class losers from it, food price inflation does not necessarily shrink demand for consumption goods the way the Reserve Bank and others think it does; it shrinks consumption demand through squeezing the incomes of working people (who save very little of their incomes) but not necessarily through squeezing the urban middle class. But the urban middle class consumes more goods produced by monopoly capital than the beneficiaries from food price inflation; this is the real reason for the solicitous attention to the consumption of the urban middle class. But let us move on.

In a neoliberal economy that is kept trade-open, the stimulus for growth normally comes from exports; there may be occasional local asset-price bubbles that give rise to unusually larger consumption and hence some spurt to growth, but in the normal course of things it is the growth in export demand that drives the economy forward. What is being asked for therefore is a shift from export-led growth to consumption-led growth, which essentially means growth led by the home market. The question is: is this possible within the boundaries of a neoliberal economy?

Simply making more credit available or easier credit available would not necessarily make even the urban middle class consume more; its consumption may get a boost for a while because of easier credit availability, but soon this boost will peter out as consumers get more indebted and seek to avoid any further increase in their debt-burden. Likewise even if food price inflation is halted, this will only give a temporary boost to consumption but cannot keep raising consumption as a spur to growth.

It may be thought that if consumption is increasing and income is also increasing as a result, then there is nothing to stop this process from going on and on; but if consumption for some reason falls in any period then a downward movement will begin with nothing to stop it. Consumption-led growth in other words needs to be continuously fed from outside by some autonomous force to keep it going. Typically, government expenditure that puts purchasing power in the hands of the consumers provides such an autonomous force.

For this to happen requires a jump in government expenditure, even if that expenditure takes the form merely of making transfers to consumers that put more purchasing power in their hands. But such a jump in government expenditure can happen only if either the fiscal deficit expands, or if taxes are raised at the expense of classes that save a good deal of their incomes, because only in that case would there be a net increase in consumption. If taxes are raised at the expense of classes that more or less consume their entire income, then say Rs100 raised in taxes from them reduces their consumption by Rs100; and when this is given as a transfer to consumers and therefore consumption rises by Rs100, there is no net addition to consumption and no question of any consumption-led growth.

Consumption-led growth therefore requires a fiscal policy that must raise larger resources either by taxing the rich (who save a significant amount of their income) or by resorting to a larger fiscal deficit. Both these however are ruled out in a neoliberal regime. Fiscal deficit cannot be raised as a conscious fiscal measure in violation of the Fiscal Responsibility and Budgetary Management Act that puts a ceiling on the magnitude of fiscal deficit as percentage of GDP. And taxing the rich, whether through wealth taxation or profit taxation, will drive capital away from the country to the detriment of its growth prospects within a neoliberal setting; in fact even before any driving away of productive capital, finance would have left the country in large magnitudes bringing it to grief.

There is of course the possibility of stimulating agricultural growth that would enlarge incomes of the farmers and thereby stimulate consumption. In fact the true rationale of consumption-led growth, and hence home market-led growth, lies in agriculture-led growth. But this requires a pro-peasant policy on the part of the government rather than a policy of promoting corporate and agribusiness interests at the expense of the peasantry, as the government is currently doing in accordance with the demands of the neoliberal regime.

Promoting corporate agriculture that does not enhance farmers' income, and on the contrary contracts it, does not give any boost to consumption.

It follows therefore that a transition from export-led growth to consumption-led growth cannot occur within the confines of a neoliberal regime. China is one country that has managed to make a shift from reliance on exports as the mainspring of growth to reliance on domestic consumption; but China is not constrained by a neoliberal regime. It is not a country where the autonomy of government policy is constrained by the whims and caprices of globalised finance, as it is not open to free cross-border flows of finance; and it is not forced to open itself to such flows since it always enjoys a trade and current account surplus.

But India and other third world countries belong to an altogether different category. They are not only open to global financial flows, but they have to be, since most of them will not be able to manage their balance of payments without financial inflows as long as they do not resort to trade controls and allow relatively unrestricted cross-border trade flows.

The Reserve Bank of India and all the other "establishment" commentators on economics talk as if the government has complete autonomy in matters of economic policy; but that shows an extreme lack of awareness of the modus operandi of a neoliberal economy.

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