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THE OUTLOOK

On Close Inspection, India's Sharp Growth Picture Gets Fuzzy

World-beating GDP figure is based on infrequent surveys, rough estimates of tiny, cash-based enterprises



Lal Bazar Street in central Kolkata, India, is home to hundreds of addresses used for tax-avoiding financial maneuvers, tax authorities say. PHOTO: RAYMOND ZHONG/THE WALL STREET JOURNAL

By Raymond Zhong

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KOLKATA—India's economy expanded by 7.3% last year, outpacing every other major nation, including China, for the first time in nearly two decades.

But as with most developing countries, where official statistics can be dicey even when they aren't showing world-beating growth, India's economy defies easy measurement. Most enterprises are tiny and unregistered, and most workers are employed off the books. The government's infrequent surveys represent only a best guess of the value being added in back-alley workshops, outdoor markets and other cash-based corners of the economy.

So even if India's measurement of gross domestic product, a broad indicator of activity, isn't thought to be politically manipulated like China's, it should come with a warning label: Handle with care.

GDP in India, "much more than in other economies, is more an estimate than a measurement," said Neelkanth Mishra, a Credit Suisse economist in Mumbai.

The fog surrounding India's GDP places challenges before analysts and policy makers—and just plain baffles some of them. The country's central bank, sensing an economy running at less-than-full blast despite strong headline growth, has cut its main interest rate five times since the start of 2015.

One reason for the data murkiness can be found on Lal Bazar Street, a busy thoroughfare of tea merchants, typists-for-hire and a sitar shop in the heart of Kolkata, the country's onetime colonial capital.

Within the dingy commercial buildings that line the roads in all directions are hundreds of addresses used to register shell companies, or ones used for tax-avoiding financial maneuvers and little else, tax authorities say.

Yet because these firms regularly file balance sheets to the

government, they appear in a new official database of corporations—and get counted when statisticians tot up India Inc.'s contribution to national output.

India's numbers have been under a microscope since it revised methods for estimating GDP last year, causing performance in earlier years to shoot up. Growth stayed brisk throughout 2015 even as exports, cargo traffic and other indicators disappointed.

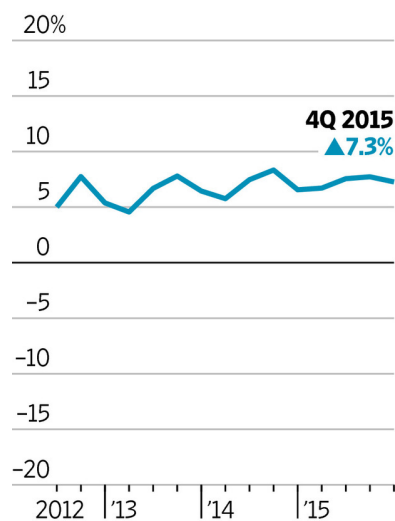
A report from India's Ministry of Finance said data-related uncertainty was causing economic signals to be "mixed, sometimes puzzling."

Crossed Signals

By the official measure, India's economic growth remains strong. But other indicators point down, stirring debate about the soundness of the country's GDP numbers.

Gross domestic product

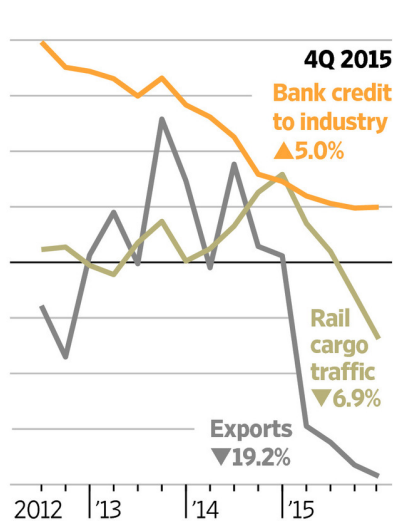
Change from a year earlier



Sources: CEIC; Indian government agencies

Selected indicators

Change from a year earlier



THE WALL STREET JOURNAL.

The GDP revision included updates large and small. Based on an academic study of “dung evacuation rates,” goats and sheep were found to be contributing more to the economy, as producers of natural fertilizer, than previously thought. A much wider array of financial services is now being counted. But there are still areas where some observers, including the International Monetary Fund, see India’s data falling short.

To strip price changes out of a wide swath of GDP, for instance, India uses its wholesale price index—which, thanks to lower oil prices, has been decreasing for 17 straight months. But many businesses, particularly services like finance and information technology, haven’t benefited much: Retail prices are still climbing at around 5% a year overall. If India’s statisticians were factoring in more of these price rises, then their inflation-adjusted GDP figures would be lower.

In a March report on India, the IMF criticized the use of wholesale prices in GDP. In a written response to questions, the country’s Central Statistical Office acknowledged the issue, but said that until India updates its inflation measures, the wholesale price index “remains the best available alternative.”

“There’s no rhyme or reason why the service sector would be deflated by WPI,” said Kunal Kumar Kundu, Société Générale SA’s India economist. “It’s basically a data availability issue. That will always continue to be a challenge.”

Data availability is also a problem when it comes to small-time services like mom-and-pop stores, hairdressers and repair shops, which account for more than 5% of India’s GDP. The government comprehensively measures their activity only every few years, so sales-tax revenue is used to approximate growth in between—another practice the IMF criticized in its report. The statistics office said tax revenue is an accurate proxy.

India relies on another workaround to gauge corporations’ contribution to the economy. The new database includes hundreds of thousands of companies’ balance sheets. But because not all of them file on time each year, the statistics office has to extrapolate to produce an initial estimate of GDP.

This is where Kolkata’s shell entities may be entering the growth calculation. Income-tax authorities say they’ve logged 14,000 shell firms and counting in a new enforcement database.

T.C.A. Anant, India’s chief statistician, said shell companies are small by nature and unlikely to throw measurements off by much. “When you work with such large numbers, these things balance out.”

Whatever the data’s specific kinks, India’s GDP haze is sending some grasping for other tools.

Ambit Capital, a Mumbai-based brokerage, has created an index named after Li Keqiang, China’s premier, who once famously said his country’s GDP figures were “man-made.” Using

vehicle sales, airport cargo, electricity demand and imports of machines and equipment, Ambit's index indicates that momentum in India has been flagging since 2014.

Ila Patnaik, a former adviser in the finance ministry, said that in more than 20 years of studying India's economy, the official GDP numbers have never appeared more out of step with other metrics.

"I don't even know how to make sense of it," she said. "Everything has gone out the window."

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