***Apart from the fact that automobile demand is not just driven by tax rates, consumers need to rebuild their savings***

When faced with poor demand conditions, the natural response of most producers is to lower prices. So, it is not entirely clear why India's automobile industry should be different, and instead of cutting prices, clamour for cuts in GST rates; a final decision on this will be taken by the GST Council on Friday. There is, of course, no harm in petitioning for a tax cut, especially when the average rates are as high as 28-30% on even low-end cars and two-wheelers, but if the situation is as dire as is being made out, and tens of thousands of people are being laid off, surely the industry should lead with sharp price cuts? After all, at 12.8% for Maruti, 23.5% for Bajaj Auto, and 15.3% for Hero MotoCorp, the industry had healthy pre-tax margins in FY19.

Nor is it going to be that easy for the government to convince the GST Council to agree to this demand. For one, since a GST cess can only be levied on goods whose tax rate is 28%, lowering the GST rate to the 18% level that the industry wants will mean that whatever cess is collected from the sector will have to be given up; considering that cess collections—a fourth of this comes from the automobile sector—are used to pay the states for any shortfall in tax collections, few states would be willing to reduce the rate. Two, if the rate-reduction is not accompanied by a sharp increase in sales volumes, states will lose out on valuable revenues.

It is certainly true that, in response to the global financial crisis in FY09, the government made a sharp cut in excise duties; and while sales did increase—26%, in the case of passenger vehicles and two-wheelers—it is not clear how much of this was due to the tax cut, and how much due to the economy bouncing back. While FY08 growth was 9.3%, this had slipped to 6.7% in FY09, and then bounced back to 8.6% in FY10.

Apart from the fact that there is no certainty that manufacturers/dealers won't roll back their discounts once the government cuts GST rates—this will allow them to protect their margins even while prices fall for the retail consumer—there is another big difference between FY09 and now. Savings rates had fallen even then, though nowhere as sharply as now. From 37.5% of GDP in FY08, savings fell to 32.7% in FY09. But, much of this was either due to a fall in corporate savings (9.4% of GDP to 7.6%) or due to a collapse in public sector savings (5.1% of

GDP to 1%); household rates actually rose, from 22.8% to 24.1%. In sharp contrast, while savings rates fell from 34.6% in FY12 to 30.5% in FY18, it is household savings that have collapsed (from 23.6% to 17.2%) this time around while public and private corporate savings rose. Presumably, if private consumption expenditure stayed buoyant all these years, even when the economy was slowing and jobs/increments were in short supply, this is because the household sector was drawing down on its savings. So, it is entirely possible that consumers will now focus on rebuilding their savings portfolios—the collapse in the Sensex also hit this—instead of increased consumption in response to tax-rate cuts.