A Reflection on Indian Economy and Other Concerns

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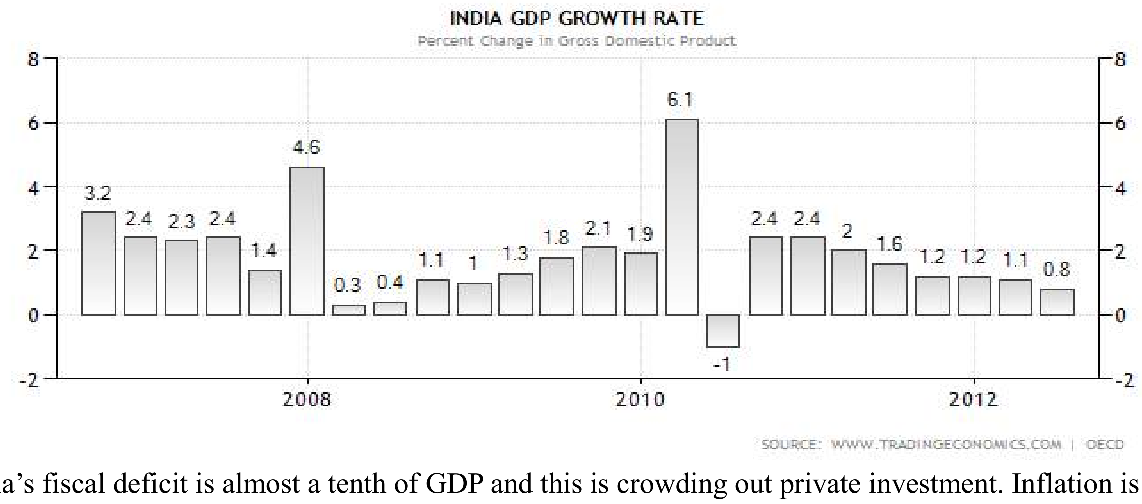
Emerging economies are slowing down, so is India. It has been a practice that the development and growth economists often compare these rapidly developing economies on several perspectives. In this article, I offer a cogent view on the recent 'halt' in Indian growth accelerations with minor reflections on China, so as to adduce reasons in support of my argument. This is because rise of both the nations has caused shift in world economic and political landscape giving birth to the neologism 'Chindia.'

Remarkable economic growth in last several years following economic reform programs in 1990s has established India as one of the Southern Engines, ranking 11th in the world in 2011 in nominal dollar terms. Adjusted for purchasing power parity, being the 4th largest economy after the US, China, and Japan it was poised for an enormous possibility of double-digit growth in coming years. However, the recent performance tarnishes 'Incredible India' (Figure below). The near double-digit growth approaching almost 10-11% from an average 6-7% in late 1980s-1990s has come to a halt now as it has fallen to 6.5%, lowest in last 9 years, from 8.4% during preceding two years. This has been called 'rickshaw rate of growth' as opposed to Hindu rate. The figure below shows the movement of GDP in percentages, indicating a limping growth scenario, with 5.3% growth in 1st quarter of 2012. Although World Bank's flagship publication 'Global Economic Prospects' paints a complacent picture of 6.9% in 2012-13, 7.2% in 2013-14, and 7.4% in 2014-15, many cast doubt about its bouncing back prospect. This might affect social and financial stability because this might make people jobless, drive more people into poverty, and scare away foreign capital needed for growth. I enlist some of the major syndromes that could signify the gravity of situation.



India's fiscal deficit is almost a tenth of GDP and this is crowding out private investment. Inflation is high. For reducing vulnerability to external shocks, Indian economy needs to contain the fiscal deficit, short-term debts, and inflation. Inflation hurts everyone, esp. the poor and it ignites protests. In July 2012, the wholesale inflation rate is about 7%. India's CPI inflation, highest among the BRIC nations, is about 10%. Core inflation—excluding foods and necessities—is about 6%. With summer monsoon being well below average the uncertainty about agricultural output in drought-like condition makes her more insecure regarding food perils, hunger and malnourishment. These have caused "agflation" (inflation esp. in agricultural products) and the decrepit public distribution system has caused massive food distribution problems when overproduced things are just rotten in the cellars. The industrialists and politicians are clamoring for lowering interest rate as they argue that high interest has slumped growth via demand squeeze. Often, this growth versus inflation trade-off is mired with the ruling party's populist policy for votes rather than impartial solid macroeconomic analysis. With bad monsoon and slack infrastructure (e.g., grave power failure in July), the prospects of growth seem bleak and tight monetary policy is needed to contain inflation for controlling severity of food insecurity. As over 600 million of 1.2 billion Indians rely on farming, the drought and lack of rural infrastructure is a drag on crop production, often resulting in upward crop prices. Apart from that, Indian rupee weakened by about 18% during last 1 year causing import costs to soar and hence, rise in imported material cost might further lead to inflationary spiral. However, it remains to be seen whether the cheaper currency could boost manufacturing and its exports. Also, a matter of concern is the soaring budget deficit due to government spending, subsidies for fuel, fertilizers. If subsidies are taken out to manage deficits, this might push prices up. Thus, the Government faces dilemma. The real concern is: how to regain growth without inflicting harms on Indian middle class and the poor. The problem, however, lies elsewhere—bureaucratic red-tape, lack of proper reforms, bad governance—for resurrection of growth with human face.

Can India regain its lost charm, and spread the boons of growth? The answer rests on the factors on the home front as the world economy itself is faltering. Given the fact that India and China are the biggest market for the West, as the US and European crisis unfurls the contagion affects them. As world economy is poised to grow at a modest rate of 2% and domestic woes are of concern, the 7.4% for India seems to be a tall order. '*Behind the border*' factors are more important than those beyond the subcontinent. Narrow focus on GDP and its parameters offers a grossly disported picture and obfuscates the visionary perspective of how Indian economy should be developing for producing broad-based and equitable growth benefiting most of her citizens, and transforming her into a modern 21st century emerging economy rooted in rich history. That does not mean that GNP/GDP growth are not useful for fighting poverty or improving living standards, rather using it as means to achieve better quality of life instead of amassing inanimate objects of convenience. Growth is pro-poor and beneficial for all provided it is used as means to achieve the developmental objectives. While impressive growth performance catches our attention, and the recent slowdown has caused worries it is crucial to see the accompanying factors underlying it. In other words, this deceleration has been accompanied by several problems on many fronts such as: widening regional divergences, lack of infrastructure, relatively slow performance in poverty decline, worrisome performance in controlling deprivation, health-care facilities, education and literacy, suboptimal socio-economic conditions, sociopolitical instability, etc. Often the problem lies with the functioning of the state machinery, the central government and their leadership. In case of India, this has culminated into syndromes hindering the growth process and thus, might encumber the overall objective. I ascribe these feeble growth to several longstanding 'traps': infrastructure bottlenecks, political anomalies, traps from neighborhood effects, corruption trap, bureaucratic black holes, traps from communal-religion nexus, most importantly inadequate human capital parameters. For parsimony, I will just highlight major hindrances seen in recent times.

With India's service-export led growth as compared to manufacturing, a recent study has highlighted India's failure in engaging in international production networks as compared to East Asia, in general, and China, in particular. For stimulating economic growth, India, having a well-endowed skilled engineers and English-speaking professional, partaking in IPN is necessary for extracting the benefits of at least regional free trade agreements in South Asia. Although post-reform economic progress based on IT-services has generated spillover, India has not attracted FDI as China did and this process of growth raises question whether India can sustain productive employment in labor-intensive manufacturing sectors. India's manufacturing is about 15% of GDP as opposed to her services (60%). An IMF study by Rodrik and Subrmaniam (2004) showed that the pro-business attitude of the government in the 1980s set the ground for the registered manufacturing to take advantage and swing from 'Hindu' growth to productivity surge. This highlights to the necessity of having a manufacturing base for employment rather than excessive dependence on service-led growth. Although Tata Nano is an indicator of frugal innovation with a $2,000 car (cheapest in the World!), the furor over its land acquisition in West Bengal is noteworthy. Without a strong manufacturing base, it will be harder to absorb the emerging youth of 250 million in coming 10-12 years. However, some rosy pictures exist; for example, the Volkswagen factory in Pune, a plant by Mercedes-Benz, and Land Rover are doing good, and mostly, engaged in trade in parts and components with assembling. Her share in global good exports is 1.5%, way below China's 13%. India's labor cost is similar to China's (under a dollar per labor-hour). However, poor education, infrastructure, red tape and tough labor laws often work against this. On the whole, manufacturing jobs shrunk to 50million between 2004 and 2010 and basic industries are declining. It is important to create jobs and boost industrial employment.

Regarding infrastructural bottlenecks, India invests less than 10% of her GDP in infrastructure, required for sustained growth of 8% or more. Recent power crisis in cities show that the area needs further attention. The massive power failure in the Northern and Eastern India sometimes in early August this year has restrained functioning of the aspiring Indian Economy. That blackout threw every hard infrastructure—railways, hospitals, factories, even traffic lights, essential service sector, airports—to a halt. The power crisis—resulting from overloading of national network connecting regional grids—is an indicator of lack of investment in power plants, inefficient and corrupt distribution system of debt-ridden companies, often indulged by the political class, decrepit governance, fuel shortage, red tape, and lack of attention on the part of government for self-interest. The problem might worsen as demand is expected to grow due to expansion of manufacturing and household demand for items such as fridge, television, computers as the middle-class burgeons. Such a crunch in infrastructural facilities is bound to arrest growth as energy is vital for making progress.

Concerning the political landscape, the ruling coalition government, facing a general election in 2014, suffers from initiating needed reforms due to threat from its regional coalition partners with vested selfish motives, internal feuds, and degenerative bureaucracy with throttling red-tapism. Politics of caste and religion, and grievance is no longer going to pay off and the voters could care no less about job, invention, employment, and social sectors. Facing risks due to fragmented politics, the incumbent is afraid to push through needed reforms regarding foreign investment or macroeconomic imbalances. The recent Anna Hazare episode is a pointer how the nexus of corruption and political maneuverings could impede domestic and foreign investment by spoiling the investment incentives. The multi-billion dollar scam for license distribution of 2G mobile-phone networks is an example of graft and wastage of public resources. Recently, government overruled the Supreme Court—highest judicial body—to change the tax code for taxing foreign takeovers retroactively, especially for large Vodafone company. This political cronyism is surely going to give wrong signal for foreign investors.

At the state level, the problems are also vivid. For example, in West Bengal the land acquisition bid by the Tata for industrialization drive, aided by the political hegemony of the then ruling government, created a huge uproar and turmoil leading to the overthrow of the government in 2010. The mismanagement cost the state to lose Tata out to Gujarat and the resultant prospect of industrial youth employment. However, without properly addressing the compensation scheme or some mechanism for setting prices and property rights issues on land, the entire land deal was mismanaged and created a bad omen for the state—displacement of the farmers as well as unfriendly investment climate—giving wrong signal for future investment potential for youth job creation. Similarly, in Bihar the wrong constellation of actors inhibit Posco to start its project. In case of Gujarat, although the Tata Nano project moved due to welcoming business environment, however, the ruling party's religious inclination creates problems for development. Viewing economic policy through lens of petty politics obfuscates growth and development. Although 'licence raj' was dismantled with reforms in 1990s, the intertwining of politics, business and economy hinders growth and welfare.

Another concern in India's political arena is the unholy meddle with her spiritual landscape. It is to be remembered that India, with multi-ethnic pluralistic structure, is home to Christians, Muslims, and others apart from large number of Hindus and often, the political reality mess up with the religion in a bad way to deter development process. This immense ethnically, culturally, and linguistically diverse country is united via the dominant religious bindings of Hinduism although other religions exist in this secular nation-state. But, sometimes blind religiosity provokes people to be involved in war against each other causing immense human loss. Often, the political parties use it as a platform to meet selfish ends, causing riots and human movements. Recent conflict in the North-East Indian state of Assam caused unprecedented crisis causing involuntary movement of people across states. This is, whether true or not, due to being landlocked by neighbours with whom India has had sour relations on the basis of religion and politicians use this as platform for selfish ends. Prudence is warranted in this regard. If under SAARC or SAFTA, India-Bangladesh-Pakistan could cooperate and set aside this religious bigotry, then socio-economic stability is achieved. A greater economic and technical cooperation between these three South Asian neighbors is a good way to ward off religious animosity and form a secular agenda in true sense.

All these signify that growth and development policy should focus on something ‘core or basic.’ Economic growth might be benefiting the already privileged or well-off Indians, just widening their choice set, and getting media attention. That is fine as long as they are sizably large. The picture is murky, however, if the fruits of economic progress is misused in India due to inappropriate focus. Economic growth creates resources for the government for allocating over its priorities. Most of these ‘traps’ and syndromes could be cured if this core elements are given high priority. Too much obsession with GNP or GDP measure as estimates of national income, as emphasized by United Nations’ Human Development Report, does not cover other aspects like education, health, human capital, infant mortality, or life expectancy in which some countries like China (even Bangladesh) score over India. According to WHO study, in case of Physicians per 10,000 people, India is way below at 6/7 compared to China (15/16) and Korea (20). Life expectancy at birth in China is 73 years, whereas India’s is 64 years; adult literacy rate is 65% in India as compared to 94% in China; mean years of schooling is 7.5 years in China whereas India’s is 4.4 years; infant mortality rate in India is 50 per thousand while China’s is 17; India’s adult female literacy is 80%, way below 99% in China. Although India made some progress especially due to its comparative advantage in software sector or IT sector, thanks to engineering skills of graduates from IITs and mushrooming private engineering colleges, the ‘Universal education’ goal under Millennium Development Goals (MDG) of the UN is a far cry. In terms of social capital index encompassing trust, norms, networks, social structure, conflict, India ranks below Japan and South Korea with a score of 3.4. Social capital is necessary for human capital.

Recently, Sir Partha Dasgupta of Cambridge University has authored a report titled ‘Inclusive Wealth Report 2012’ published by the United Nations, where he measured the ‘real’ wealth—natural, human and physical assets as opposed to measuring flow of goods and services in traditional accounting framework—of 20 countries. Despite growth, India faltered in many fronts than China and others. According to this measure, China has $20 trillion wealth as compared to $6.2 trillion in India where growth rate (1990-2008) is 2.1% for China as compared to 0.9% for India. Inclusive wealth concept is important for economic policy-making. India’s one of the biggest asset is her population and hence, if human capital (based on schooling and skills) and natural assets can be fostered, the demographic dividend can be reaped. This comparison sheds light on what India needs to shift her focus on.

The policy imperatives should focus on these aspects for sustained growth and development for making this newfound economic prosperity to reach most of the Indians, lifting millions out of poverty in keeping with the MDG, job-creation for the youth, and to increase sociopolitical stability. Otherwise, the constellation of all these factors would hobble the Elephant to face the Dragon. It is necessary to remove the weedlike gridlocks—by denouncing cronyism, making system transparent, developing complementary inputs, and investing in human development— for the benefit of India’s largest democracy.