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Analysing the Parameters of the Effects and Causes of Indian Economy

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Abstract – This paper presents the wide large scale parameters of the development of the Indian economy since the country's freedom and a cross country assessment of where India stands, drawing out the examples noticeable in these aggregative statistics. The paper gives a review of the on-going debate on the components of the Indian development and the overall significance of the diverse approaches. It adds to this debate by distinguishing the milestone years, and examining the governmental issues behind a portion of the financial matters. The paper additionally investigations the variables behind the adjustments in India's funds rate and the connection among development and advancement, from one viewpoint, and the idea of work showcase guideline, on the other.

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I. INTRODUCTION

The heart of an economy's growth and take-off keeps on baffling economists. Despite the fact that, on account of long periods of supported research, a large number of the bits of the jigsaw astound are set up, it stays exceptionally hard to anticipate when an economy that has fumbled for quite a long time may all of a sudden take off. The economy, installed all things considered in governmental issues, culture, and institutions, is an adequately unpredictable creature for this not to astound. In any case, growth tends to conceive growth; however, obviously, slips can convey it to an end. Consequently, our comprehension of an economy's fast growth needs to concentrate to a great extent on what causes the primary stirrings.

What this paper endeavours is to dissect and comprehend the star grouping of powers that has decided the growth execution of the Indian economy, including its extensive stretch of hibernation and abrupt, late show of dynamism. The principal task in such an endeavour is to get the certainties right. In the course of the last 4 or 5 years India has been showing signs of improvement press than any time in recent memory, since its autonomy in 1947. Is this great press truly defended? On the off chance that the economy is developing quicker, when did the take-off happen? This is critical to research to fulfill inert interest as well as to comprehend the different powers that may have set off the dynamism; and that thusly is significant for the creating of approaches to continue the growth and spread its crown jewels all the more equally over the populace.

II. GROWTH: TRENDS AND PATTERNS

(a) Backdrop

Thanks to a long history of data collection, the basic numbers of the Indian economy are, for a poor country, well documented. At the time of its independence in 1947, India had: a literacy rate of 18 per cent; an investment rate of around 9 per cent of its GDP; life expectancy at birth of 32 years; an annual population growth rate of 1.25 per cent; and an average annual growth rate of GDP of around 3 per cent. In 2005/6, India had: a literacy rate of around 60 per cent; an investment rate of around 30 per cent of its GDP; life expectancy at birth of 63 years; an annual population growth rate of 1.5 per cent; and an annual growth rate of GDP of around 8.4 per cent.

To get a basic idea of the absolute numbers involved, Table 1 gives the size of the Indian population, the real GDP (at market prices), and the real GDP per capita (at market prices). The key difference between the GDP at factor costs and the GDP at market prices is that the latter includes indirect taxes net of subsidies. As the latter is considered a better measure of the standard of living, we have opted to report the absolute figures of the GDP and GDP per capita at market prices.

From Table 1 it is clear that while the Indian population has more than doubled since the 1985s, GDP has increased more than eightfold since then. As the population figures for India are based on projections from Census of India data, we have opted not to show the entire time series for population or GDP per capita.

Table 1 GDP Growth in different years

Year	Population in Millions	GDP (in millions constant 2000 US$)	GDP per capita (constant 2000 US$)
1985	435	76983	175
1990	487	91054	187
1995	548	113606	207
2000	687	152621	213
2005	765	268023	222
2015	932	345394	259

(b) Growth patterns and hypotheses

Owing to the huge amount of noise, the trends are not too evident to the naked eye. But once we smooth out these annual fluctuations and look, instead, at averages of several years of growth, a pattern emerges. The average growth holds steady till about the mid-1970s and then, somewhere after that, it begins to move up, and that upward incline has persisted till current times. This is corroborated by the average, annual growth-rate figures for each of the 5-year plan periods. Average annual growth nearly touched the 5 per cent mark during the Fifth Plan period, and has never dropped below that since. The sharp spike occurred during the Eighth Plan period, when annual growth averaged 6.7 per cent. All the portents are that, during the Tenth Plan period, the economy will grow at close to 8 per cent per annum. Given that India's population growth rate is much slower than it used to be three or four decades ago (1.5 per cent in 2014-15 as against 2.22 per cent in this means that the rise in per-capita income growth rate from the 1960s and 1970s to current times has been even more marked

To understand this debate and the components of the post-1980s growth further, let us take a look at the results of the growth accounting exercise. The objective of growth accounting is to decompose the economic growth rate of a country into contributions of different factors. Assuming a certain aggregate production function and competitive markets, the method identifies the contribution of the different factors (such as labour and physical capital) and a residual, called total factor productivity (TFP).

III. THE POLITICAL ECONOMY OF GROWTH

The previous section gave an overview of India's growth performance over the last 50 years and briefly outlined the elements of the current debate in the literature on India's growth. This section tells the story behind the numbers. The first real big growth year for India, 1975/6, was also one that stood out politically as one of the most salient, if not notorious, years for the nation. That year the country's GDP grew by 9 per cent, a figure that has been surpassed only twice since then.19 It was also the year in which the then Prime Minister, Indira Gandhi, declared a state of emergency and established dictatorial control over the nation. This would last for 2 years. In 1977 Indira Gandhi called an election. There is no way of knowing if this was prompted by an exaggerated sense of popularity on her part or because of a genuine fatigue she felt with totalitarian control. But the fact of the matter is that she was routed at the polls, and she would return to power (re-elected) only in 1980. Some of the growth spurt of the early Emergency period would be undone in 1979-80, the worst-performing year in the history of independent India, but 1974–9, as already noted, was nevertheless to be the cross-over plan period when average annual growth rate closed in on the 5 per cent mark.

The opening of branches and making savings and borrowing outlets available to poorer citizens were explicit objectives of the nationalization. And while its impact on savings awaits formal investigation, there are other kinds of related studies that do suggest the nationalization of banks had a large impact on ordinary citizens. Burgess and Pande (2005), for instance, test whether this large state-led bank-branch expansion programme was associated with poverty reduction in India, given that an integral element of the programme was branch expansion into rural locations without banks. The paper's main finding is that branch expansion into such rural locations in India significantly reduced rural poverty.

There are two factors to which it is worth drawing attention. First, there was one unintended positive spill over of the last US presidential election. During the election campaign, outsourcing back-office work to developing countries came under heavy criticism, with some television shows, such as that of Lou Dobbs, attacking US entrepreneurs for profiteering by outsourcing work. This had a huge advertisement effect for the advantages of outsourcing. Most poor countries would not be able to afford such advertising on American television; they suddenly got it for free. Small US entrepreneurs, who were unaware of this profit opportunity, learned about it and began outsourcing, and India's already large outsourcing business received another boost.

Second, having an alignment of interest with the world's most powerful nation, the USA, can have large benefits for an economy. We have seen this happen in the case of South Korea since the 1950s. Shifts in the global geo-political balance of power have suddenly brought India into the ambit of US interest. As long as the USA's main foreign policy concern was Communism and the USSR, it had little use for India. But now, with terrorism being the main global concern of the USA, it has shared interests with India, which are deeper than the current tactical ties with Pakistan. Also, with the rise of China, the USA has apprehensions of a new unipolar world with China at the centre or, what is only marginally better, a direct face-off with China in a bipolar world. In the event of a showdown between these two countries, the risks for the USA are huge. If China were to cut off or monitor trade flows through the Strait of Malacca, the biggest sea route for trade in today's world, this could have very large consequences for the US economy. China also has a disproportionate leverage on the value of the dollar, thanks to its large foreign-exchange holdings. India is viewed by the United States as a counterpoise for all these risks, and India's economy has benefited from this emerging geo-political advantage.

But we want to turn now from these macroeconomic aggregates and broad global issues to the microeconomic foundations of what is happening in India. The advantages of global politics can easily be dissipated, as we saw in the case of the former Soviet Union, if a country's economic 'nuts and bolts' do not function well. There are now increasing data on the microeconomic institutions that permit businesses to thrive and grow and play a crucial role in an economy's long-run trajectory. The next section examines some of these issues.

IV. MICROECONOMIC FOUNDATIONS

India's initial focus on the international sector has paid off handsomely. But to sustain this growth, microeconomic issues—better distribution of income, improved labour-market functioning, the control of corruption, and more efficient institutions for business and enterprise—need greater attention. These are often referred to as second-generation reforms. There is no effort here to cover all these micro foundational issues, each of which could be the subject of a full-length paper, but we comment on one, namely, labour-market regulation, where we have some insights to offer which are not common knowledge. While the Indian economy is booming, there is evidence that workers are not partaking in the boom adequately. Employment is not growing as fast as working-age population, nor are wages rising as rapidly as per-capita income. There are many reasons for this—some to do with forces of globalization that are beyond the Indian government's policy reach. But much of it has to do with the 'culture' that pervades India's labour markets, which in turn is a consequence of the complicated and ill-conceived laws that govern the labour market. In India there are 45 laws at the national level and close to four times as many at the level of state governments that monitor the functioning of labour markets. This complexity is reflected in the World Bank's ease-of-business indicators, where India ranked 112 out of 175 countries in the category 'employing workers' in 2006 (with 1 being the best). Even though recent changes in the regulation of several Indian states have resulted in a lower 'difficulty of hiring index', 'rigidity of hours index', 'rigidity of employment index', and 'firing costs', India still scores high on the 'difficulty of firing' index (70/100), which is considerably higher than the average of the low-income countries

But in today's globalized world, with volatile and shifting demand, firms have responded to this by keeping their labour force as small as possible. It is little wonder that in a country as large as India fewer than 10m workers are employed in the formal private sector. Some commentators have argued that India's labour laws could not have had much of a consequence since most of them apply only to the formal sector. What they fail to realize is that one reason the formal sector has remained minuscule is because of these laws and also the culture that these laws have spawned

Several recent studies have analysed the impacts of labour regulations on firm productivity, patterns of specialization, and technological progress. According to Besley and Burgess (2004), increasing pro-worker regulation has a negative impact on investment and productivity in the registered manufacturing sectors. What is also interesting about their findings is the lack of evidence that such policies improve labor interests. Aghion and Burgess (2003) confirm these results and in addition show that the negative impact of having stricter labour regulations on productivity has increased in the post-liberalization period. Kochar et al. (2006), based on their analysis of the patterns of specialization of Indian firms, suggest that not only is the level of productivity of existing firms affected by stringent regulations, but new firms are also kept from entering as a result.

Much of the debate on labour laws has been misconstrued. What is needed is no change in labour laws and policy to elicit sacrifice from organized labour, as some economists have suggested. Indian workers, whether they be in the organized sector or the unorganized sector, are too poor for that. The need is for changes in order to create greater private-sector demand for labour, which would boost wages and employment. We believe that India's poorly construed labour laws have been so persistent because of an intellectual failure—to wit, the inability to grasp that, in some contexts, it may be in the worker's own interest to be able to waive some rights that have been granted to him/her. It should be clarified that we are not making the case for all workers to be given the right to give up their right either to call strikes or to continue to work, but simply arguing that there are contexts where it is worthwhile giving them the meta-right to give up some right. One has to weigh lots of pros and cons before making a general recommendation. We feel that the right to strike has other advantages so that, barring some very special cases, workers should always have this right. On the other hand, we believe that in India workers should be given the right to sign contracts with different kinds of firing or retrenchment rules, and that doing so is likely to cause such a rise in aggregate demand for labour that all workers will be better off. While much of the current debate in India on labour laws is conducted as though worker interests are pitted against business interests, in reality it is between thinking clearly and not thinking clearly.

V. CONCLUSION

To conclude, if India wants to sustain and raise even higher its current growth, the main bottlenecks in the Indian economy will need to be addressed. These are infrastructure (roads, expensive freight rates, power supply, ports, and airports), labour and bankruptcy regulations, and the high level of corruption in the government bureaucracy. In addition, the current erratic and low growth pattern of the agricultural sector, and the rising inequality—between states, between rural and urban areas, and within urban and within rural areas mainly since the 1990s—are a concern. Of these numerous factors, we have addressed only a few in this paper. Each of these factors deserves inquiry, research, and policy initiative, but in concluding we remark briefly on just one of them—the subject of inequality.

Comparing the ratio of the income shares of the richest 10 per cent over the poorest 10 per cent in India with other countries, one may be tempted to conclude that inequality in India is not abnormally high. According to the World Bank's World Development Indicators 2006, this ratio was 7.2 in India (in 2000), compared to 18.36 in China (in 2001), 48 in Guatemala (in 2002), and 15.9 in the USA (in 2000). As such, India's current inequality seems to be low and comparable to some of the Western European nations. But one has to remember that a poor country will have a natural tendency for greater equality, since people cannot survive below a certain level of income. To take an extreme case, a country that has a per-capita income equal to the subsistence income will, by definition, have no income inequality. Hence, despite the seemingly encouraging inequality ratio mentioned above, inequality—especially when it results in higher poverty—is a serious problem for India. This could lead to political tensions and could destabilize the otherwise optimistic growth scenario. But, even if it does not dampen the country's growth prospects, it seems to us that greater equity and the reduction of poverty are valuable ends in themselves. Indeed, it is arguable that growth is valuable precisely because it enables a country to banish poverty and achieve greater equality. India's trajectory over the last 15 years has been remarkable, but there will truly be reason to celebrate this when the overall gains filter down to the poorest and the most deprived sections of India's vast population.

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