pharmacies were already nearly empty

India — half way t

India

By N Ravi

The dominant view at the Stanford conference was that many of the lessons from elsewhere and current economic wisdom were still to be fully assimilated into the Indian policy chain

FOR long Indian exceptionalism has been an abiding faith with establishment economists and planners. India's problems, especially because of its size and diversity, were unique in character and solutions imported from outside would not work. Thus, as the Yale economist TN Srinivasan put it at a recent conference on the Challenges of Economic Policy Reform in Asia at Stanford University, on the reasoning that countries such as Korea that achieved rapid growth were too small and that India was sui generis, planners were unwilling to learn lessons from elsewhere. That indeed was the experience of another key participant, Anne Krueger, the first deputy managing director of the International Monetary Fund, in her dealings with policy makers in India for over two decades: she was told repeatedly in the 1980s that India could not export because it was too large. China's success, however, changed the learning environment, for the small versus big argument could no longer be pulled out to question the relevance of other countries' experiences.

Yet, have the lessons from the growth experience of other countries been learnt, is current economic wisdom reflected in Indian policy making? The message from the Stanford conference was that there are many lessons and findings still to be assimilated into the policy chain. While the change and the progress made so far, particularly the most recent shift of the economy to a higher growth trajectory of 7 to 8 percent, were indeed striking, much more needed to be done if the growth rate was to be sustained and even pushed up. The unfinished business is not confined to market-friendly policies, though they form an important core, but extend to health and to education as well.

While one size fits all solutions may not work, India-specific research pointed to broad areas of opportunity as well as challenge. Offering a substantial opportunity is the favourable demographic transition, with a large working age population entering the labour market and offering the prospects of pushing up production as well as savings. This transition is similar to what China experienced during its high growth phase, as David Bloom and his colleagues at the Harvard School of Public Health along with Linlin Hu of Tsinghua University pointed out in a paper titled "Why has China's economy taken off faster than India's?" Both the countries started with the same ratio of working age (15 to 64 years) to non-working age (0 to 14 and 65 and over) population in 1975, but China's population policy led to a decline in fertility and triggered a sharp rise in the ratio of working age people which is expected to peak at 2.5 in 2010. India's demographics are changing, but much more slowly, with the peak of 2.1 (the level reached by China in 1995) expected in 2035. Over the medium term, while China anticipates a rising population of the elderly, for India, "the greater portion of this potential demographic dividend lies ahead."

Bloom and his colleagues stress that this demographic change only creates the supply side potential for growth but whether the potential is exploited in a substantial measure depends on the right mix of policies: the quality of government institutions, labour laws, macroeconomic stability, openness to trade, and education policies. Latin America, which experienced a demographic transition similar to that in East Asia, faltered and could do little better than Sub-Saharan Africa. India and China have been able to absorb an increase in the labour force better than parts of Africa or Latin America but their performance is not as good as Ireland's demographically induced economic boom.

Has India finally got its policy mix right? The dominant view was that in trade and regional integration as well as in domestic market reform it had progressed significantly and come half way, but was not fully there yet. First, in the area of trade, Arvind Panagariya of Columbia University who presented a paper on "India and China: Trade and foreign investment" pointed out that there was both good news and bad. The good news was that the economy has turned the corner and the export pessimism of old had given way to a new confidence. The bad news came from a comparison with China, which was "a humbling experience" as the two countries were in different leagues in terms of performance. In 1982, China's per capita GDP was lower than India's but growth rates ranging from 9.1 percent to 10 percent during the period since

> As much as getting the policy mi
> political system as a whole is to
> political officials act in the best int
> and to make sound policies and goo

...and control levels don't func- COURTESY THE GUARDIAN

to getting it right

1980 pushed it to 2.4 times that of India in 2004. China's share of world trade is over 6 percent in contrast to India's less than 1 percent share. China's remains more open, with an average tariff of 9 percent in contrast to India's 13 to 14 percent, and it has been much more successful in its exports of both semi-skilled labour intensive goods such as apparel and high technology merchandise including office machines. His prescription included encouraging the export of semi-skilled labour intensive goods such as clothing where India held a great advantage, removing distortions such as small scale industry reservations, reforming the labour market, strengthening the infrastructure, and encouraging more foreign direct investment.

mix right, the challenge before the o devise incentives to ensure that nterests of the economy as a whole ood governance politically rewarding

Addressing a second area of domestic policy reform, Chang-Tai Hsieh of UC Berkeley and Peter Klenov of Stanford University argue that in both India and China output distortions and unequal access to capital lead to firms of widely varying efficiencies functioning side by side, and if capital and labour were allocated more efffciently among all the firms within an industry, output could double. Typically, this would involve transferring resources to the larger firms whose output would grow while the medium and smaller firms would shrink. Thus, even without increasing the stock of capital or labour, reallocation among firms can work magic and provide a generation's worth of growth. Roger Noll, the Director of the Stanford Centre for International Development, was persuaded to term it "cost-free gain" to both India and China as output would double at zero cost.

Wholesale reforms: Chang and Klenov's paper also provided a key insight that policy makers need to keep in mind when crafting the extent and timing of reforms. Their analysis showed that partial domestic liberalisation in India where only output distortions or only capital distortions are removed would provide significantly lower gains than wholesale reforms. While the gains from domestic liberalisation would be huge, the task has hardly been addressed in any systematic way.

The third critical area of policy reform is in education. It is true that no country has graduated to the developed stage without near universal literacy. One long held view, reiterated among others by the World Bank, is that a developing country must focus on primary education as the gains from investing in primary education would be larger than in higher education. That does not, however, seem to be the entire story, for the returns on primary education fall and those on higher education rise as an economy advances. The message that emerged from the conference was that higher education could play a very important role and that its contribution to economic growth would grow in both India and China. India has followed a sub-optimal path in higher education and needs to step up investments and pay much greater attention to quality in both professional and arts and science courses.

If then the way ahead is all that clear, why does public policy lag so far behind current economic wisdom? Why is it that India is just half way to getting it right? Resistance from sectional interests both among labour and in industry is one part of the story. A more important reason, as former Planning Commission member NK Singh pointed out, is the persistent belief that economic reforms are somehow detrimental to political power. The political change not just at the Centre but in the States as well in 2004 reinforced this belief.

One explanation for this disconnect between reforms and political power is that reforms have not been packaged properly, that the obvious benefits to all sections have not been sold convincingly. Opponents of reforms, on the other hand, attribute it to a problem intrinsic to reforms, that they are non-inclusive of large sections of the population. The continual decline in the poverty ratio during the era of reforms and high growth calls into question the assertion of non-inclusive growth. The proportion below the poverty line declined from 36 percent in 1993-94 to 22 percent in 2004-05, according to the latest National Sample Survey data. While proportion declined by 0.74 percent a year during the period as a whole, the last five years saw an improvement to 0.79 percent. Yet, the continuing resort at election time to populist appeals that go against the grain of reforms shows that political parties at the ground level sense that a significant constituency feels bypassed by the growth process and needs to be addressed directly through immediate benefits. As much as getting the policy mix right, the challenge before the political system as a whole is to devise incentives to ensure that political officials act in the best interests of the economy as a whole and to make sound policies and good governance politically rewarding. COURTESY THE HINDU