Indian Economy since 1980

Virtuous Growth or Polarisation?

It is widely believed that India’s economic growth in the 1990s accelerated – in response to the orthodox economic reforms initiated in 1991 – mainly on account of a faster growth in the tertiary sector. There is also a growing consensus that (i) the improved growth since 1980-81 reduced poverty, and (ii) the reforms in the 1990s increased the growth rate further, without dampening the process of poverty reduction. This study seeks to verify these propositions. Further, it examines some dimensions of income distribution – a neglected issue in the recent times – to assess if the developments during the last two decades led to a diffusion of growth – or a polarisation in the economy.

RNAGARAJ

1 Introduction

Picture the economic discourse in the early 1980s. There was widespread gloom about India’s macroeconomic performance – perhaps, best captured in the words of Raj Krishna:

A review of the economic development of India in the last three decades reveals an astonishing fact: a large number of the indicators of development have remained stuck at very unsatisfactory levels...The stability of numerous parameters would not be a matter of concern but for the fact that their stable values epitomise a large and a growing mass of unrelieved suffering...For 32 years the rate of growth of national income has been stagnating around a miserable mean of about 3.5 per cent. This rate keeps India as low as 71st in the list of 104 countries ordered according to the rate of growth of income per capita [Raj Krishna 1984:62-63].

Now, consider the discourse, one and a half decades later. Intervening in a popular debate on the development policy, T N Srinivasan illustrated his arguments with an assessment of India’s recent economic performance:

During 1980-90, the rate of growth increased to 5.8 per cent and was exceeded by only eight out of 113 countries. During 1990-98, the growth rate further increased to 6.1 per cent and was exceeded by only 9 out of 131 countries...Only after the growth accelerated in the 1980s, was there a significant declining trend in poverty, a trend that appears to have continued after the recovery from the 1991 crisis and reform [T N Srinivasan, The Financial Times, September 27, 1999].

That the (orthodox) economic reforms initiated in 1991 have improved economic growth with a continued positive effect in reducing poverty has made scholars optimistic that accelerating the growth further will banish poverty very quickly. Participating in the same debate, Deepak Lal argued:

...dispute about the poverty numbers in India merely reflects the fact that rapid growth has not occurred or has not been sustained to make a marked dent on poverty. The stalled reforms have failed to raise growth rate appreciably. Some estimate that...I have made...show that if the growth rate rises to 9-10 per cent that China has seen, by 2006 the poverty ratio can fall from its current rate of over 30 per cent to just over 5 per cent [Deepak Lal, The Financial Times, October 8, 1999].

These views reflect the dramatic change in the professional perception about the Indian economic performance and prospects – especially in the international circles – over the last two decades.1 Vijay Kelkar also echoed a similar view recently: “There is, in fact, some evidence that during the nineties the growth rate in India has shown some acceleration”. He further contended, “As we enter the new century, the economy stands at the crossroads. It can take either the ‘business as usual’ road which means continued poverty and the low-growth trap or the high road to prosperity through accelerated reforms” [Kelkar 1999:2326, 2329].

Thus, the emerging consensus is:

(1) Improved economic growth since in 1980-81 has reduced poverty significantly.
(2) The growth rate improved as a result of the economic reforms initiated since 1991, without affecting the trend decline in poverty.
(3) Therefore, more reforms – popularly called the ‘second generation reforms’, or ‘completing the reform agenda’ – will further improve the growth rate, and reduce poverty.2

More recently, there is a growing view in popular writings that Indian economy is increasingly driven by services, as the tertiary sector now accounts for close to one-half of GDP. Therefore, India is perceived as a post-industrial society – a ‘knowledge’ based economy. Such optimism is perhaps largely based on the recent spurt in software exports and the perceived potential of trade in services such as information technology, communications and entertainment.

The foregoing views and perceptions have considerable significance, both for the current policy initiatives in India, as well as for the development discourse in general. Therefore, there is a need for a careful examination of these propositions, both for their analytical soundness and empirical validity.

Whether the reforms – as defined by stabilisation and structural adjustment programme, or as popularly called the
The 'Washington Consensus' – result in a superior economic performance has been seriously questioned in the literature. Dornbusch had warned a decade ago: “Stabilisation may be inevitable but is not a ticket to prosperity... One should not presume that the market automatically solves the coordination problems...” [Dornbusch 1990:42-43].

More recently, there has been considerable rethinking on the neo-liberal orthodoxy (Washington consensus) within the mainstream economics. 2 This is perhaps best illustrated in the writings of Joseph Stiglitz. According to him, the goal of the Washington Consensus was to provide a formula for creating a vibrant private sector and stimulate economic growth. In retrospect, the policy recommendations were highly risk-averse – they were based on the desire to avoid worst disasters. Although the Washington Consensus provided some of the foundations for well functioning markets, it was incomplete and sometimes even misleading [Stiglitz 1998:30].

Empirically, there is little unambiguous positive association between the reforms and economic growth. The 1999 annual report of the World Bank Operation Evaluation Department has reported some startling facts. In its assessment of the World Bank lending for 28 countries between 1981 and 1997, the annual report came to the following conclusions. To quote the report, the facts of growth and poverty in the 28 countries between 1981 and 1997 are sobering:

- In 40 per cent of the countries, per capita income either failed to grow or shrank.
- In 25 per cent, the share of population in absolute poverty increased.
- In 23 per cent, life expectancy declined.
- In 54 per cent, the people experienced stagnating per capita income, rising poverty and declining life expectancy, or a combination of these events.
- In 85 per cent, per capita income grew 1 per cent a year or less in the 1990s.
- In 59 per cent, gross savings as a percentage of GDP were low (less than 10 per cent) or declining.
- In 67 per cent, investment efficiency was less than 10 per cent or declining. These findings confirm the view... that the battle against poverty is being lost and that business as usual will not accomplish the objectives of the development community [World Bank 2000:17].

In a careful assessment of the structural adjustment in Latin America since 1980, Agarwal and Sen Gupta (1999), conclude that there is no evidence of a positive association between reforms and growth. In addition to growth and poverty, there is a considerable evidence of growing inequality among countries that have systematically followed the reforms. Growing inter-regional disparities in China after market-oriented reforms were initiated in 1978 is, by now, a well-accepted proposition [Tsui 1996]. In the context of similar reforms in the 1980s in Thailand, John Lewis and Devesh Kapur (1990) had warned of a growing rural-urban divide.

Quite apart from the question of how the reforms affect income distribution, recent economic literature has witnessed a renewed interest on the effects of growth on inequality, from a variety of analytical perspectives.

Bringing Income Distribution Back In

In the Keynesian literature, income distribution is central to the pace and pattern of economic growth in terms of its implications for aggregate demand. Within the mainstream economic discourse, micro-economic arguments are increasingly brought in to understand how greater equality is conducive to faster economic growth. 4 Yet another strand in the recent years, following the public choice theoretic literature, has shown how income distribution influences economic growth as it affects voting behaviour in a democracy [Tanzi and Chu 1998]. In this genre of literature, there are several chains of causation, in which initial level of inequality affects economic outcomes. These are perhaps best described in Alberto Alesina's words:

Several channels imply an inverse relationship running from initial income inequality to growth. A fiscal channel suggests that income inequality creates a demand for redistributive fiscal policy. In a median voter model, the key measure of inequality is the level of income or wealth of the median voter relative to the average. The poorer the median voter, relative to the average, the larger the amount of redistribution that a majority of voters will favour. More generally, a large, impoverished fraction of the population creates political pressure for redistributive policies. The pressure may take different forms in different institutional contexts but it is generally felt in both democracies and dictatorships. In fact, in order to survive, even dictators cannot totally ignore popular demands. Redistributive fiscal policies lead to high levels of taxation, which negatively affects growth. Thus, the chain of causation goes from high initial income inequality to high taxes and from large redistributions to low growth. An alternative argument is that the rich in very unequal societies have the political and economic resources to escape taxation by exiting the economy with capital flight or by tax evasion. Thus, demand for redistribution policies with a vanishing tax base may lead to large budget deficits. A second channel linking inequality and macroeconomic performance goes through political instability. Income inequality fosters social discontent and unrest. The associated threats to property rights, policy volatility and government fragility depress productive investment, promote capital flight and ultimately reduce growth [Alesina 1998:301].

Empirically, it has been found that in the OECD countries, in the post-war period, economies with less unequal income distribution have performed better. 5 Similarly, comparing the performance of the east Asian economies with those of Latin America, Jeffery Sachs contended, “... high income inequality... [in Latin America] contributes to intense political pressure for macroeconomic policies to raise income of lower income groups, which in turn contributes to bad policy choices and weak economic performance” [Sachs 1989:9].

Seen in this background, a near total lack of interest in how the gains of the improved growth in India since the 1980s are distributed is surprising. 6 Perhaps, it is implicitly believed that the problem of absolute poverty is more acute in India, and that a decline in it implies an improvement in income distribution. Since there is a widespread consensus on the positive effects of growth on poverty reduction over the last quarter century or so, concerns of income distribution seem to have taken a back seat.

The brief discussion above on growth, reform and inequality – both from analytical and comparative economic perspectives – provides a meaningful background to formulate working hypotheses to examine the recent Indian experience. In light of the foregoing, we will examine the following propositions:

- Has GDP, or any of its major components, shown a statistically valid change in its growth rate since 1991?
- How valid is the postulated association between economic growth, poverty and the policy reform. Does the inverse relationship between growth and poverty reduction hold at the disaggregated level?
- How has the improved growth rate since
the 1980s been distributed across rural and urban areas, between the organised and unorganised sectors, across the major Indian states, and between the factors of production in the private corporate sector?

II

Data Sources and Their Limitations

This study mostly uses the National Accounts Statistics (NAS). Recently a new series of NAS has been introduced with the base year 1993-94, replacing the earlier one with the base year 1980-81. As the new series are available only from 1993-94, and the old series stopped with 1996-97, we had to use a chain index to convert the data for the recent years to the old base year. To this extent, the findings here are tentative. As the data for 1998-99 and 1999-2000 are based on quick and revised estimates respectively, they are subject to revision. Hence our growth estimates are tentative on this count also.

State domestic product (SDP) data, though available in time series, have many limitations for comparability across states (Nagaraj 1998). Planning Commission computes ‘comparable estimates’ of SDP that are used for the finance commission awards.7 Apparently, these estimates, though comparable across states, are not comparable over time. Therefore, in principle, it is difficult to be sure, which series is superior. Thus, it would be useful to check if the two series give similar results. However, such a question will remain hypothetical, as the ‘comparable estimates’ are not made public.

Data on poverty and employment are based on the widely used five-yearly surveys conducted by the NSS. We avoided using the results based on the yearly ‘thin sample’ surveys, which are found to have a large variance, and hence unreliable. We have followed the official definition of poverty and used the head count ratio.

Since the unorganised sector accounts for over 60 per cent of NDP and over 90 per cent of workforce, ‘mixed income’ forms a large share of India’s national income. As mixed income is a composite of wage income and property income, it is difficult to study factor incomes systematically. Therefore, we examine the distribution of income across broad structural categories like rural and urban, organised and unorganised and across regions. However, we study factor incomes in the private corporate sector since the mid-1980s, as systematic accounts for this sector are available.

In analysing growth rates, we use semi-log trend analysis, and employ a dummy variable to test for statistically significant breaks in the trends. We use as long a time series as possible to minimise problems caused by the omitted years. Where data are available for discrete time points, we have computed implicit growth rates using compound growth rate principle.

III

Findings

Trends in GDP

Table 1 (i) provides estimated growth rates for GDP, and its main sectors, between 1980-81 and 1999-2000; and tests of significance of the dummy variable. Evidently, there is no statistically valid break in the series at 1991, implying that, so far, on a trend basis, GDP has continued to grow since 1991-92 at the same rate as it did during the previous decade – at 5.7 per cent per year.8 This result holds, even when the year 1991-92 is excluded. There is no change in the trend growth rate between the 1980s and the 1990s for the primary sector as well, at 3.2 per cent per year.

Though modest, there is a statistically significant slow down in the growth rate of the secondary sector, after 1991-92. Thus, the widely held view that there has been acceleration in the GDP growth rate since the introduction of the reforms is not statistically correct. The same holds true for the tertiary sector as well. However, since the secondary sector growth rate has modestly slowed, the tertiary sector has become the fastest growing sector in the 1990s – but not because its growth rate has improved in that decade, statistically significantly.

A further disaggregation of GDP suggests that none of the industry group (at one digit level) show a statistically significant improvement its growth rate after the reforms. However, (i) total manufacturing and (ii) public, social and personal services – constituting around 30 per cent of GDP in the 1990s – have witnessed a statistically significant slow down since 1991-92.

Growth and Poverty Reduction

Figure 1, describes the official estimates of poverty levels (right-hand scale) and the absolute number of persons below the

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<tbody>
<tr>
<td>Primary</td>
<td>3.4</td>
<td>3.2</td>
<td>-</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>Secondary</td>
<td>7.0</td>
<td>6.8</td>
<td>-</td>
<td>Significant**</td>
<td></td>
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<tr>
<td>Tertiary</td>
<td>6.7</td>
<td>7.1</td>
<td>-</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>GDP</td>
<td>5.6</td>
<td>5.7</td>
<td>-</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>GDP#</td>
<td>5.6</td>
<td>6.2</td>
<td>+</td>
<td>Not significant</td>
<td></td>
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</table>

Notes: Data for 1999-2000 represents the revised estimates, released in June 2000. # Excluding 1991-92. ** Statistically significant at 99 per cent confidence interval.

Source: NAS, various issues, and the official press releases.

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<tbody>
<tr>
<td>1 Agriculture and allied</td>
<td>3.1</td>
<td>3.1</td>
<td>-</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>2 Mining</td>
<td>7.7</td>
<td>5.8</td>
<td>-</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>3 Manufacturing</td>
<td>7.4</td>
<td>7.0</td>
<td>-</td>
<td>Significant**</td>
<td></td>
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<tr>
<td>3.1 Reg Mfg</td>
<td>8.3</td>
<td>7.7**</td>
<td>-</td>
<td>Significant</td>
<td></td>
</tr>
<tr>
<td>3.2 Unreg Mfg</td>
<td>6.1</td>
<td>5.8</td>
<td>-</td>
<td>Significant</td>
<td></td>
</tr>
<tr>
<td>4 Electricity, gas and water</td>
<td>8.9</td>
<td>8.3</td>
<td>+</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>5 Construction</td>
<td>4.6</td>
<td>5.1</td>
<td>+</td>
<td>Not significant</td>
<td></td>
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<tr>
<td>6 Trade, hotel and restaurant</td>
<td>6.1</td>
<td>7.3</td>
<td>-</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>7 Transport, communication</td>
<td>7.3</td>
<td>8.2</td>
<td>+</td>
<td>Not significant</td>
<td></td>
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<tr>
<td>7.1 Railways</td>
<td>4.1</td>
<td>3.4**</td>
<td>-</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>8 Finance and real estate</td>
<td>7.4</td>
<td>8.1</td>
<td>+</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>8.1 Banking and Insurance</td>
<td>13.0</td>
<td>13.1</td>
<td>+</td>
<td>Not significant</td>
<td></td>
</tr>
<tr>
<td>9 Services</td>
<td>6.5</td>
<td>6.2</td>
<td>-</td>
<td>Significant</td>
<td></td>
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<tr>
<td>9.1 Public admin and defense</td>
<td>7.7</td>
<td>6.2</td>
<td>-</td>
<td>Significant</td>
<td></td>
</tr>
<tr>
<td>GDP</td>
<td>5.6</td>
<td>5.7</td>
<td>-</td>
<td>Not significant</td>
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</table>

* These estimates are for the period, 1980-81 to 1997-98, based on the NAS.

poverty line (left-hand scale) since 1973-74, for all-India combined for rural and urban areas (Economic Survey, 1998-99). It shows that the proportion of population living in poverty has steadily come down – from 55 per cent in 1973-74, to 36 per cent in 1993-94. Evidently, the widely believed poverty reduction started in the 1970s, quite a few years before the economy got on to the higher growth path after 1980-81. Thus, Srinivasan’s propositions that poverty began to decline only after the growth rate improved and, that the growth accelerated in response to the reforms in 1991 – as we have seen above – are not sustainable.

Admittedly, the official estimates for all-India do suggest an inverse relationship between growth and poverty, at least since the 1980s. But does it hold across the states? To find it out, we estimated two kind of correlation: one, between the levels, and two, between the growth rates. This we did for the years since 1973-74 across 13 major states for which data are available – 5 for the levels, and 4 for the growth rates. There is an unambiguous, statistically significant, inverse relationship between per capita SDP and levels of poverty across the states, for all the years (Table 2 (ii)). But, no such relationship was found between growth in per capita SDP and change in poverty for all the four periods (Table 2 (ii)). This is true, both with simple correlation coefficient, as well as with the rank correlation coefficient. Thus, our finding provides a basis to question the widely believed virtuous association between output growth and poverty reduction at a disaggregated level.

However, since the bulk of poverty is in rural areas, with agriculture as the main source of livelihood, we estimated the association between growth in SDP per capita in the primary sector and poverty reduction in rural India across the major Indian states (Table 2 (iii)). The association is negative and statistically significant in only one out of two cases. Thus, it seems reasonable to infer that the suggested inverse relationship between primary sector growth and poverty reduction in rural India is at best a weak one.

As officially reported, if poverty has indeed declined by about 20 per cent in the two-decades after 1973-74, it would be reasonable to expect a steady improvement in average per capita consumption, especially of the bottom half of the population. Expectedly, as Suryanarayana (2000) has shown, the monthly per capita consumption expenditure in rural India has increased by 32 per cent during the two decades, from the levels of Rs 18.40 in 1973-74.

However, on a closer examination, the whole process largely appears a statistical mirage. If one takes a longer period since 1960, as Suryanarayana has documented, there was a drop of about 20 per cent in the average per capita during 1960-65. And, it took over a decade (ending in 1977-78) to recover this consumption loss.

Nevertheless, during the subsequent 16 year period, between 1977-78 and 1993-94, the average consumption grew annually at 0.9 per cent. More significant, the average for the bottom half of rural population increased annually at 1.5 percent. Though modest, these trends indeed suggest a process of growth with redistribution in rural India.

But the growth in per capita consumption did not result in any improvement in the nutritional status of the poor, mainly for the following reasons.

- Since the 1970s, to acquire the same level of nutrition, the poor had to substitute expensive cereal like rice and wheat for jowar, bajra and other millets whose production has fallen sharply in per capita terms.
- The decline in the institution of permanent farm servants and an increase in casualization of rural workforce resulted in monetisation of the rural economy. This required (i) a ‘diversification’ of consumption of the poor to include fuel and other complementary items, and (ii) an increase in ‘overhead’ cost of acquiring the same level of nutrition. In other words, changes in the cropping pattern and the institutional setting in rural India seem to have wiped out the potential benefits of improved – albeit modest – average consumption growth in value terms. Thus, when measured in terms of nutritional status there is, in fact, a definite evidence of an increase in poverty in India (Figure 2). The proportion of the rural population not getting adequate nutrition

<table>
<thead>
<tr>
<th>Year</th>
<th>Simple Correlation Coefficient</th>
<th>Rank Correlation Coefficient</th>
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<tbody>
<tr>
<td>1973-74</td>
<td>–0.683*</td>
<td>–0.535*</td>
</tr>
<tr>
<td>1977-78</td>
<td>–0.525*</td>
<td>–0.341</td>
</tr>
<tr>
<td>1983</td>
<td>–0.722*</td>
<td>–0.605*</td>
</tr>
<tr>
<td>1987-88</td>
<td>–0.702*</td>
<td>–0.627*</td>
</tr>
<tr>
<td>1993-94</td>
<td>–0.596*</td>
<td>–0.682*</td>
</tr>
</tbody>
</table>

* Statistically significant at 95 per cent confidence level.

Table 2 (iii): Correlation between Growth in Per Capita SDP in Primary Sector and Change in Rural Poverty Level across Major Indian States (No of observations = 14)

<table>
<thead>
<tr>
<th>Change Over the Years</th>
<th>Simple Correlation Coefficient</th>
<th>Rank Correlation Coefficient</th>
</tr>
</thead>
<tbody>
<tr>
<td>1977-78 over 1973-74</td>
<td>–0.043</td>
<td>–0.007</td>
</tr>
<tr>
<td>1983 over 1977-78</td>
<td>–0.254</td>
<td>–0.118</td>
</tr>
<tr>
<td>1987-88 over 1983</td>
<td>–0.493</td>
<td>–0.350</td>
</tr>
<tr>
<td>1993-94 over 1987-88</td>
<td>–0.493</td>
<td>–0.484</td>
</tr>
</tbody>
</table>

a sustained growth in per capita income for nearly two decades since 1980-81, there has been no real improvement in the nutritional status of the poor. Intuitively, one could argue that a large-scale subsidised food distribution could have, in principle, improved the nutritional status. In the absence of such a programme, perhaps one should look at how the labour market has performed, since it is only through gainful employment on a large scale that demand for food could go up, and thus improve the nutritional status of the poor. As Amit Bhaduri rightly reminded us,

It is through the labour market that both the stimulus to economic growth and the process of social justice could largely operate. And, the extent of increase in gainful employment opportunities provides the crucial bridge between economic growth and efficiency on the one hand and social justice on the other...Economic reforms, no matter labelled 'capitalist or socialist' are bound to falter without enough popular support, unless they meet this latter test" [Bhaduri 1996:15].

**Trends in Employment**

Since the incidence of poverty and unemployment as highly correlated, one would expect that if poverty has really declined, then it would have reduced unemployment and underemployment. But we find that since 1973-74, there has been an economywide decline in employment elasticity of output (Table 3).11 For instance, the elasticity for the economy as a whole has declined from 0.61 between 1972-73 and 1977-78, to 0.47 between 1987-88 and 1993-94. The fall is more pronounced in the secondary and tertiary sectors. Although there has been a modest decline in the proportion of population in agriculture since the 1970s, and there has been some diversification of rural workforce into non-farm activities especially in the 1980s, there is no evidence of a sustained reduction in unemployment levels, however measured [Ghose 1999].12

On the contrary, there is a distinct deterioration in the quality of employment. Between 1977-78 and 1993-94, the share of – the organised sector in total workforce declined from 8.7 per cent to 8.1 per cent; wage employment in the unorganised sector went up from 6.6 percent to 7 percent; self-employed in total workforce declined from 56.5 per cent to 51.7 per cent; and, casual wage employment went up from 28.2 per cent to 33.2 per cent.

Some of these changes, in principle, could have improved labour market flexibility.13 However, they could have been equally responsible for the changes in the level and composition of aggregate demand that could have adversely affected the consumption growth of the unemployed.14 If the suggested implications for the labour market have any value, then the observed growth process is likely to have been inequalising. In other words, since the improved growth since the 1980s did not result in a proportionate increase in employment (and poverty reduction), it is very likely that the growth has helped only those persons, regions, or segments of the economy that are already employed or better off. To test this proposition, we now look at some dimensions of income distribution.

**Trends in Income Distribution**

As in most developing economies, there is no information on personal income distribution since over 9/10th of the workforce is in the unorganised sector where the majority of the population is self-employed. As a proxy, the consumption distribution is widely used. As noted earlier, there has been a modest improvement in the per capita consumption of the bottom half in rural India in value terms, since 1977-78. But it has not improved their nutritional status mainly as they have been compelled to consume costlier cereal like wheat and rice, since the output of inferior cereals has fallen sharply.

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<tbody>
<tr>
<td>1 Agriculture</td>
<td>0.54</td>
<td>0.49</td>
<td>0.26</td>
<td>0.54</td>
</tr>
<tr>
<td>2 Mining</td>
<td>0.95</td>
<td>0.67</td>
<td>0.81</td>
<td>0.36</td>
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<td>3 Manufacturing</td>
<td>1.05</td>
<td>0.68</td>
<td>0.35</td>
<td>0.39</td>
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<tr>
<td>4 Electricity</td>
<td>1.67</td>
<td>0.74</td>
<td>0.74</td>
<td>0.53</td>
</tr>
<tr>
<td>5 Construction</td>
<td>0.35</td>
<td>1.00</td>
<td>3.43</td>
<td>0.01</td>
</tr>
<tr>
<td>6 Transport, storage and comm.</td>
<td>0.76</td>
<td>0.92</td>
<td>0.39</td>
<td>0.62</td>
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<tr>
<td>7 Trade, hotel and restaurants</td>
<td>0.80</td>
<td>0.90</td>
<td>0.52</td>
<td>0.68</td>
</tr>
<tr>
<td>8 Services</td>
<td>0.80</td>
<td>0.90</td>
<td>0.52</td>
<td>0.68</td>
</tr>
<tr>
<td>8.1 Services including trade</td>
<td>0.80</td>
<td>0.90</td>
<td>0.52</td>
<td>0.68</td>
</tr>
<tr>
<td>9 Total</td>
<td>0.61</td>
<td>0.55</td>
<td>0.32</td>
<td>0.47</td>
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</table>

However, there is evidence to suggest that the distribution of income measured in other structural and institutional categories has deteriorated over the last two decades. Figure 3 shows the rural (nominal) per capita income as a proportion of urban per capita income. Evidently, the ratio, which improved in favour of rural India between 1970-71 and 1980-81, deteriorated during the subsequent 14-year period. The per capita rural income has declined relative to urban per capita income, from 42 per cent in 1980-81 to 38 per cent in 1993-94.15

A similar comparison of (nominal) per capita income in the organised and unorganised sectors is even more revealing (Figure 4). Over the decade since 1983, the per capita NDP in the unorganised sector as a proportion of that in the organised sector has steadily gone down by 3 per cent. This decline is not just because of a faster growth in employment in that sector, but its output growth has also been slower.

Another aspect of income distribution in a heterogeneous country like India is inter-regional inequality. This inequality, measured by the coefficient of variation in per capita SDP across the major states, has nearly doubled in 25 years since 1970-71, from about 0.2 to 0.4 (Figure 5). However, more significantly, the divergence in per capita income between the top three and the bottom three states has widened sharply since 1986-87 (Figure 6). In 1980-81, the average per capita SDP of the bottom three states (Bihar, Orissa and Assam) was 43 per cent of that of the top three states (Punjab, Haryana and Maharashtra). This ratio fell to 27 per cent in 1995-96. Moreover, in absolute terms, the per capita SDP of the bottom three states was lower in 1995-96, compared to 1986-87.16

Finally, we look at the distribution of value added between wages and profits in the private corporate sector.17 Although this sector accounts for roughly about a tenth of GDP in the 1990s, it uses a much greater share of domestic savings and attracts a disproportionately large attention of policy-makers. As Figure 7 shows, the share of wages in value added, in current prices, has fallen from about 35 per cent in 1985-86 to about 20 per cent in 1996-97. During the same period, the profit share (measured by profit before tax, after depreciation and interest) has gone up by about 15 percentage points – roughly equal to the fall in the wage share. Although such a simplistic comparison may have analytical limitations, perhaps the sharp changes in factor incomes, in just over a decade does indicate, however crudely, a distinct change in income distribution in favour of owners of capital, and against workers.18

In a highly diverse and heterogeneous economy like ours, perhaps one can document many more dimensions of economic inequality. But perhaps our limited inquiry does suggest an unambiguous increase in inequality in Indian economy over the last two decades or so.

**IV Conclusions**

What does all this add up to? Between 1980-81 and 1999-2000, on a trend basis, the domestic economy has grown annually, at about 5.7 per cent. The growth is likely to have been faster in per capita terms in the 1990s, when the population growth rate is said to have declined noticeably. The growth is laudable in a comparative perspective as well, as Srinivasan noted. While debt and inflation ravaged large parts of the developing world in the 1980s, India improved its growth rate, with a greater stability. Moreover, India withstood the 1991 external payment crisis as well as the recent east Asian contagion, without any slow down in the growth momentum.

It is widely believed – especially among the policy-makers and in the development profession – that India’s economic performance during the last quarter century or so has been a virtuous one: growth with poverty reduction. Moreover, the economic reforms initiated since 1991 are believed to have improved the growth rate further, without adversely affecting the trend reduction in poverty. The findings reported in this study question these stylised views of the recent economic performance. We found: (1) There is, at least as yet, no statistically significant acceleration in India’s growth rate after 1991-92. This holds excluding 1991-92 as well, the year of external payment crisis. Thus, on a trend basis, GDP growth rate between 1991-92 and 1999-2000 is the same as it was between 1980-81 and 1990-91. (2) The secondary sector growth rate witnessed a modest, statistically significant, slow down after 1991-92. (3) Contrary to the popular view, there is no statistically significant acceleration in the growth rate of the tertiary sector in the 1990s. On a trend basis, the primary and the tertiary sectors, like GDP, have grown at the same rates as in the 1980s. (4) As the widely believed decline in poverty started before the growth rate improved in the 1980s – and the reforms in 1991 – there is no association between the widely believed poverty reduction with the improved growth rate, or with the economic reforms. (5) There is no statistically significant association between the growth in per capita income (SDP) and poverty reduction across the major India states. Further, the correlation between the growth in primary sector SDP per capita and poverty reduction is
found to be ambiguous. This evidence contests the widely held view of an inverse relationship between growth and poverty reduction in India, at a disaggregated level. Moreover, the widely believed poverty reduction is probably a statistical mirage. The nutritional status – a contentious yet robust measure of poverty – of the average (as well as that of the bottom half) in rural India has not improved at all in the entire period since the early 1970s. Recent research cited, in fact, suggests that rural poverty, measured in terms of nutritional deficiency, has gone up by 10 percentage points since 1972-73, from 65 per cent.

The absence of an association between growth and poverty reduction across the major India states – contrary to much popular and scholarly writing – is perhaps not surprising (or intuitively understandable), if one looks at the labour market performance. After all, if the growth is poverty reducing, it should then, in principle, work through a large-scale rural employment creation, especially in poorer states, as the unemployed and under-employed form the bulk of the poor.

The study shows that while the growth rate improved since 1980-81, there is no sustained reduction in unemployment rates, however measured. Although employment growth roughly kept pace with the growth in workforce – as has been widely documented – there has been an economywide decline in employment elasticity of output since the mid-1970s, suggesting that the fruits of higher growth are largely restricted to those already employed. Further, the quality of employment has deteriorated during the 16 years since 1977-78. For instance, there has been (i) a declining share of regular wage employment in the organised sector, (ii) an increase in the share of wage employment in the unorganised sector, (iii) a decline in self-employment in rural India, and (iv) an increase in casualisation of the workforce. While these changes may have reduced some of the widely perceived rigidities in the industrial labour market, they have not resulted in greater labour absorption – as anticipated in the mainstream economic theory. Considering these, the widely held inverse association between growth and poverty reduction in India, during the last two decades or so, seems suspect.

In recent years, attention has been mainly focused on the widely believed virtuous effects of growth on poverty reduction, overlooking how the improved growth since the 1980s is distributed. Such a neglect of concerns of equity is surprising, since there has been a renewed interest in this question in the recent economic discourse, both from analytical and comparative economic perspectives. There is an increasing appreciation – both in theory and experience – that greater equality is conducive for growth. Further, recent evidence suggests that the economic reforms have, more often than not, accentuated inequalities since the 1980s across the developing world. It is with this concern that we looked at some aspects of inequality in India over the last two decades. The results, though limited to a few dimensions of the problem, appear quite startling:

- The ratio of rural to urban (nominal) per capita income, which improved during the 1970s, deteriorated during 14 years after 1980-81.
- There is a secular deterioration in the ratio of the unorganised to organised (nominal) per capita income since 1982-83.
- Since 1970, there has been a steady increase in inequality across the major states, as measured by the coefficient of variation in SDP per capita.
- The ratio of per capita income of the bottom three states, as a proportion of that of the top three states, has widened significantly since 1986-87. Further, the level of per capita SDP of the bottom three states is lower in 1995-96, compared to seven years earlier.
- In the decade since the mid-1980s, in the private corporate sector, the share of (nominal) gross value added accruing to labour has steadily declined by about 15 per cent, while that of capital (profit before tax, after depreciation and interest) has gone up correspondingly. These changes in income distribution do seem to indicate that the growing inequality – as in the case of poverty – represent long-term tendencies in India. However, it may be reasonable to infer that the increasing market orientation of the economy since the early 1980s probably hastened the process of widening of disparities.

If the above findings and inferences are valid, then the gains of faster economic growth since 1980-81 have been unequally shared by different sections of the Indian society. Growth has favoured urban India, organised sector, richer states and property owners – against rural India, unorganised sector, poorer states and wage earners. To answer the question posed in the title of this study: India’s growth process during the last two decades does not seem to have been a virtuous one – it has polarised the economy. It has been a period of growth with inequality.19

Interestingly, such an inequalising process of economic growth has occurred at a time when there is a distinct diffusion of political power towards the erstwhile disenfranchised classes and castes, which broadly represent those left behind in economic development.20 To quote Pranab Bardhan’s recent assessment of the political changes in India:

Along with political power drifting from the centre to the regions, there is an associated drift towards the backward and lower castes. This is clearly a sign of democratic progression in an unequal society. The numerical strength and increased assertiveness of some of the historically subordinated groups have compelled the upper classes and castes to form downward alliances and brought to the fore political actors from backward communities and regions. These players may not be initiated in the etiquette of parliamentary democracy and social grace of modernity, but are quite astute in pursuing the interests of their constituencies (and, of course, their own self interest) [Bardhan 1988:132].

If such an iniquitous growth process is not corrected – and corrected quickly – Indian society may have to pay a huge political price for it. [FN]

Notes

[Following the usual disclaimers, I thank Errol D’Souza, Veena Mishra, K V Ramaswamy, C Rammanohar Reddy, S L Shetty and M H Suryanarayana for their comments and suggestions on earlier drafts of this study. Jyann Jose Thomas’s computational assistance is gratefully acknowledged.]

1 Reviewing books on India in the Times Literary Supplement, Jagdish Bhagwati wrote, “India’s liberal and outward-oriented economic reforms, began in earnest after the external-payment crisis of 1991, have been accomplished by a sustained increase in a growth rate that had remained stuck at a dramatically low level of around 3.5 per cent over nearly three decades of illiberal and autarkic policies. The 1980s, treated to only a small dose of such reforms, were already registering higher growth rates...” (March 31, p 28).

2 The meaning of the term, “second generation reforms” is far from clear, except to broadly mean a continuation of the market-oriented changes in policies initiated earlier. Reportedly, Sebastian Edwards coined the term in an unpublished note in 1996 to mean (i) central bank independence, (ii) budgetary constraint on all levels of government, (iii) creation of an efficient civil service, (iv) improvement in citizens’ security, and (v) judicial reforms to strengthen the rule of law.

3 This is best illustrated by the deliberations of a group constituted by the United Nations “to review some of the key questions that arise in formulating strategies for development in the contemporary world”, in the forward by Edmond Malinvaud and Amartya Sen.
One of the reasons for it could be the sharp fall in public investment – much of which is in infrastructure – that we know has a dampening effect on increase in equality (Nagaraj et al 2000). Significance of public infrastructure investment in absolute decline of states like Bihar is being increasingly appreciated by policy-makers.

Recently, Raja Chelliah (1999) advocated a special development programme for Bihar.

This is based on CMIE data.

Roughly during the same period, a similar pattern is evident in Europe as well. Olivier Blanchard (1997) found a steady rise in profit share in Europe in the 1980s. I am grateful to Kaushik Basu for this reference.

One may reasonably take comfort from the fact that the observed growth process is following the Kuznetsian inverted U. Alternatively, one may defend the process as being Pareto superior. These arguments are of questionable validity. Evidence during the last half a century of development experience does not support the Kuznets hypothesis unequivocally. Invoking Pareto could be misleading, as it ignores initial income distribution. As Frances Stewart had warned, “If a given income distribution is considered to be wrong, then maximising on that may lead to a worse outcome than the income distribution that leads to a better income distribution.”

Welfare conclusions...cannot occur independently of an assessment of income distribution in two situations.

We are aware, in turn, raises many questions. For instance, if political power has really shifted in favour of the erstwhile disenfranchised classes and castes, why have they not been able to grab a larger share of the domestic output? We have no answer to this moment, as the question lies outside the scope of the present study.

References


