

Escaping the middle income trap: India

A presentation made at *Warwick Emerging Markets Forum*

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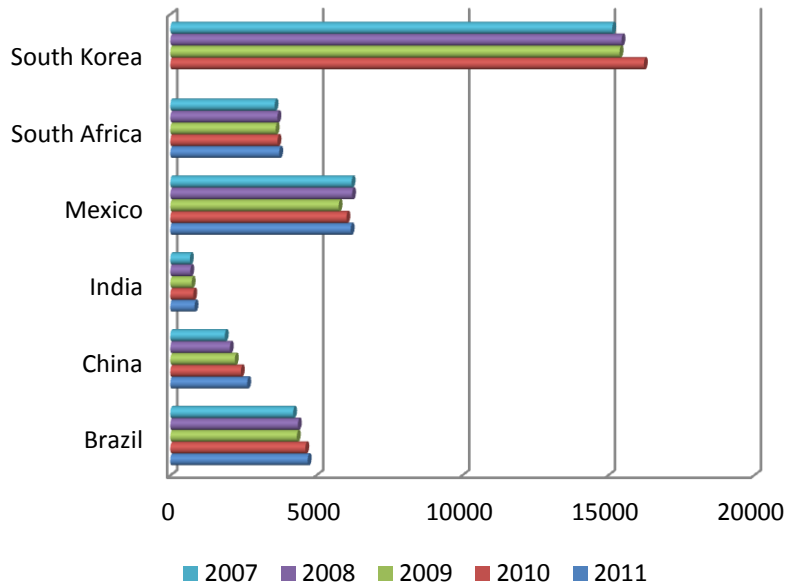
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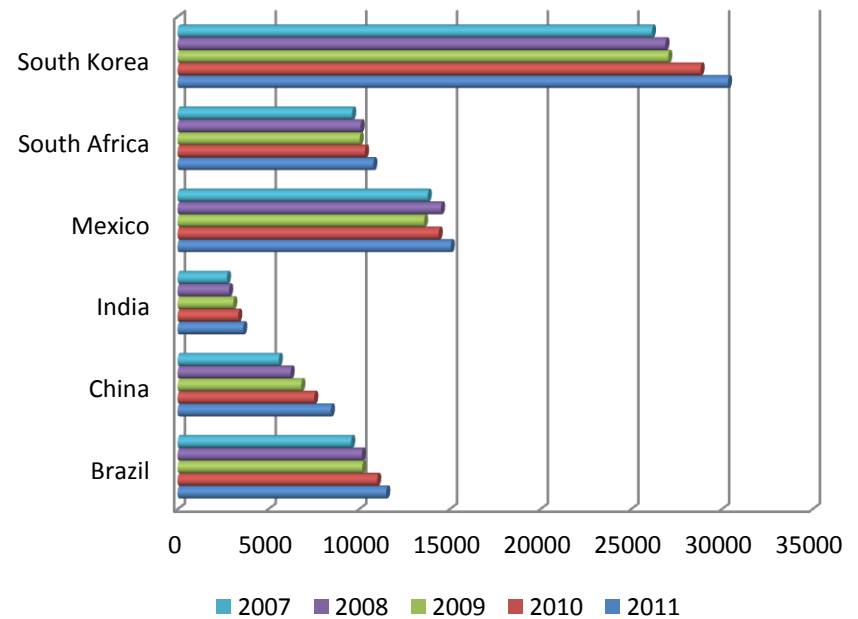
Let us start with some data

The gap in per capita GDP

GNI per capita (constant 2000 US\$)



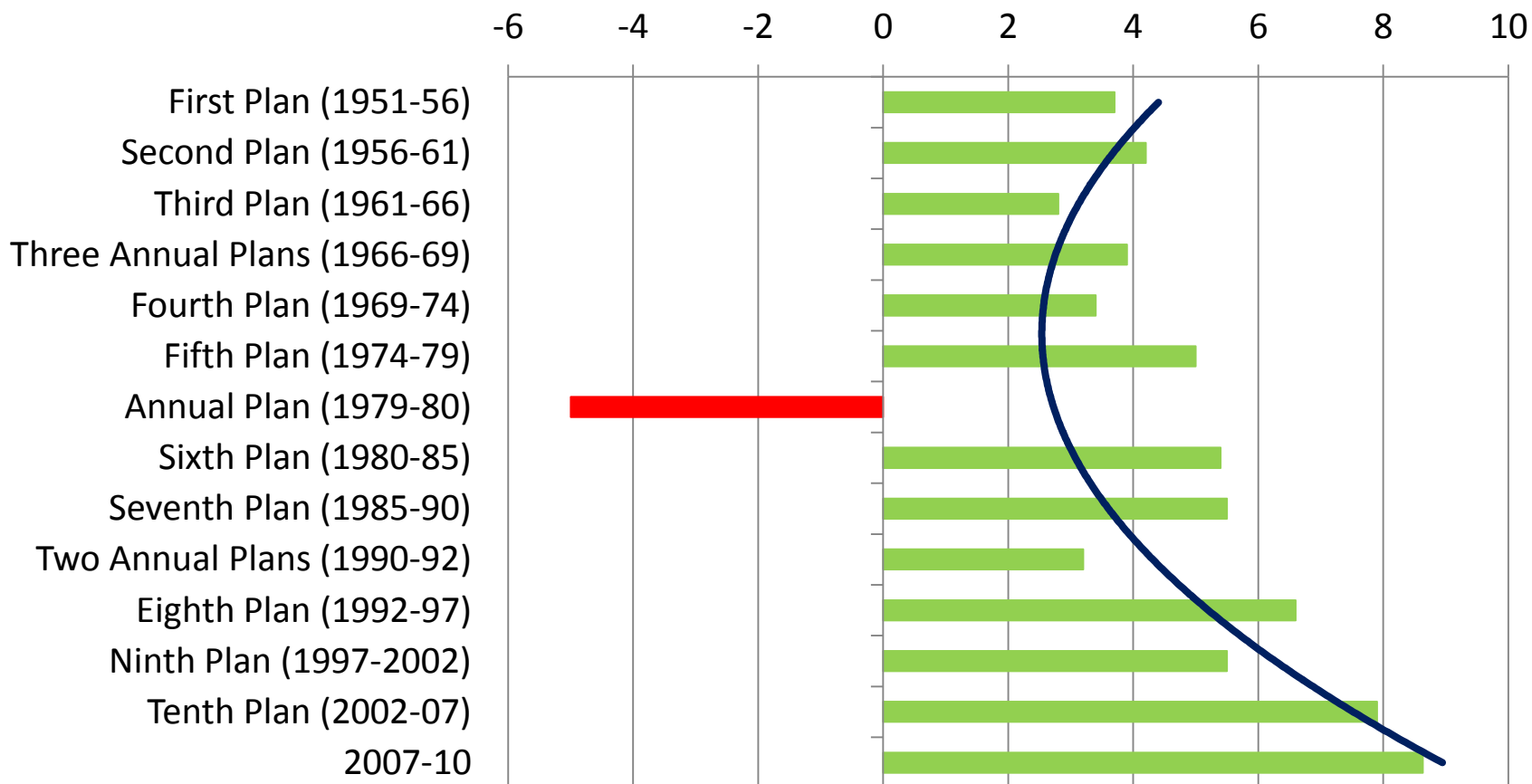
GNI per capita, PPP (current international \$)



India's per capita GDP therefore has to rise 6-7 fold to reach the threshold of escaping the middle income trap, requiring sustained GDP growth of about 10% per annum

GDP growth rate

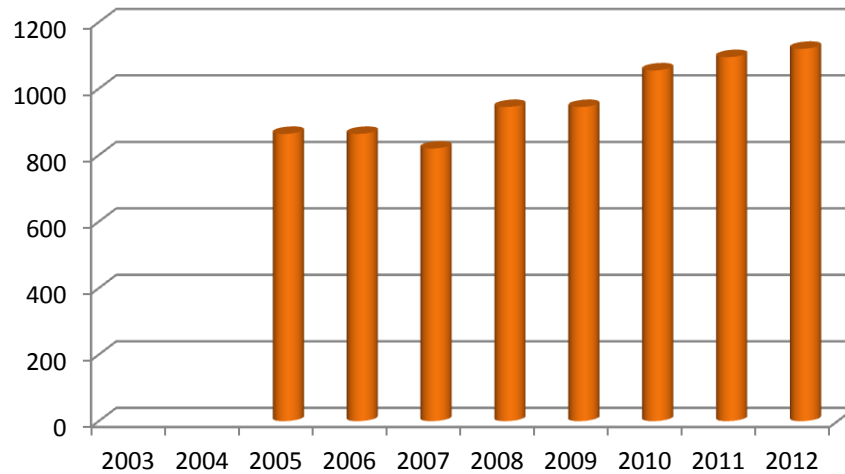
Growth of GDP at factor cost (in 1990-91 prices)



*And thus began the India story, which is now at
a cross-road*

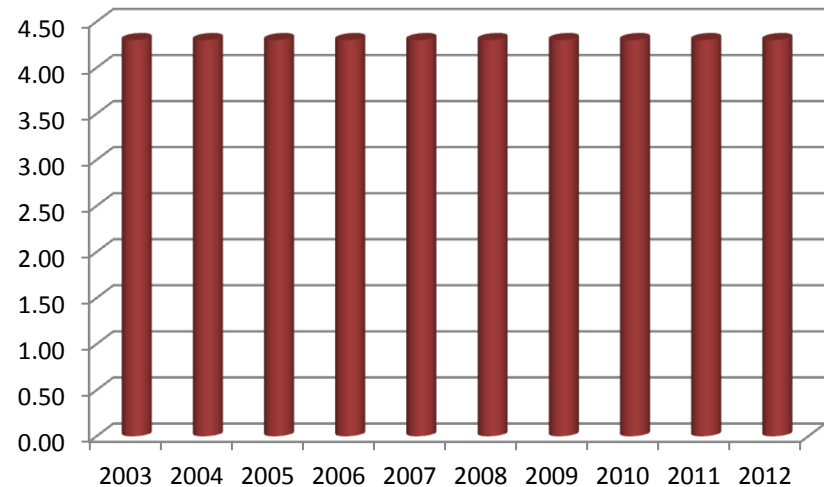
Physical and institutional infrastructure

Cost to export (US\$ per container)



Ease of doing business rank
(2012) = 132

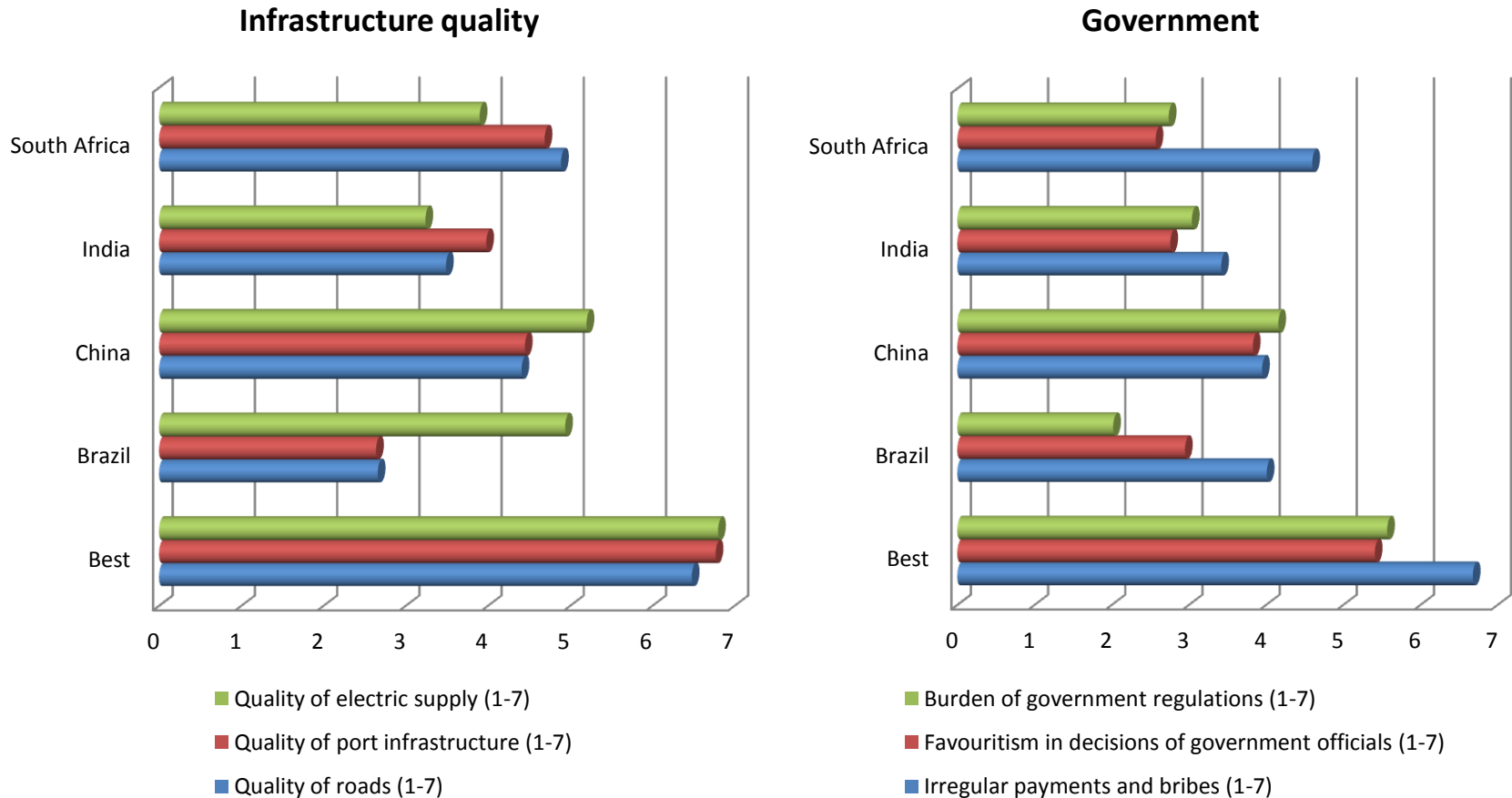
Time to resolve insolvency (years)



Transparency International
Corruption perception index
rank (2011) = 95

*There are significant physical and institutional
bottlenecks 27 years after start of reforms*

Comparison with BCS – cost of doing business



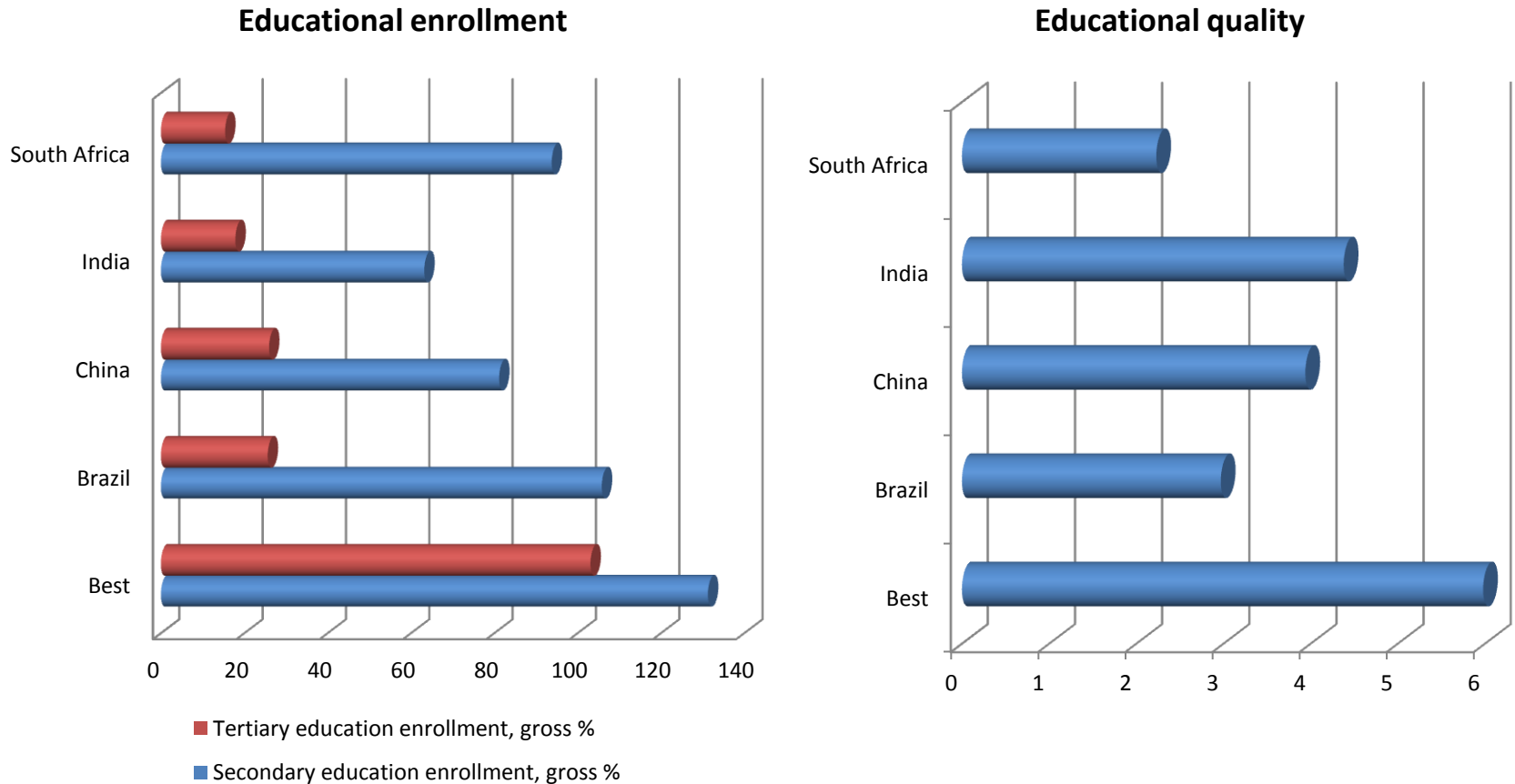
Moving on

Educational transition

	Male		Female	
	Rural	Urban	Rural	Urban
Below Primary to primary education or higher	0.59	0.76	0.32	0.58
Primary to middle education or higher	0.70	0.80	0.53	0.71
Middle school to secondary education or higher	0.53	0.65	0.38	0.56
Secondary to higher secondary education or higher	0.49	0.58	0.34	0.50
Higher secondary to tertiary education	0.47	0.57	0.37	0.51
Sample size	58,027	31,709	58,834	31,127

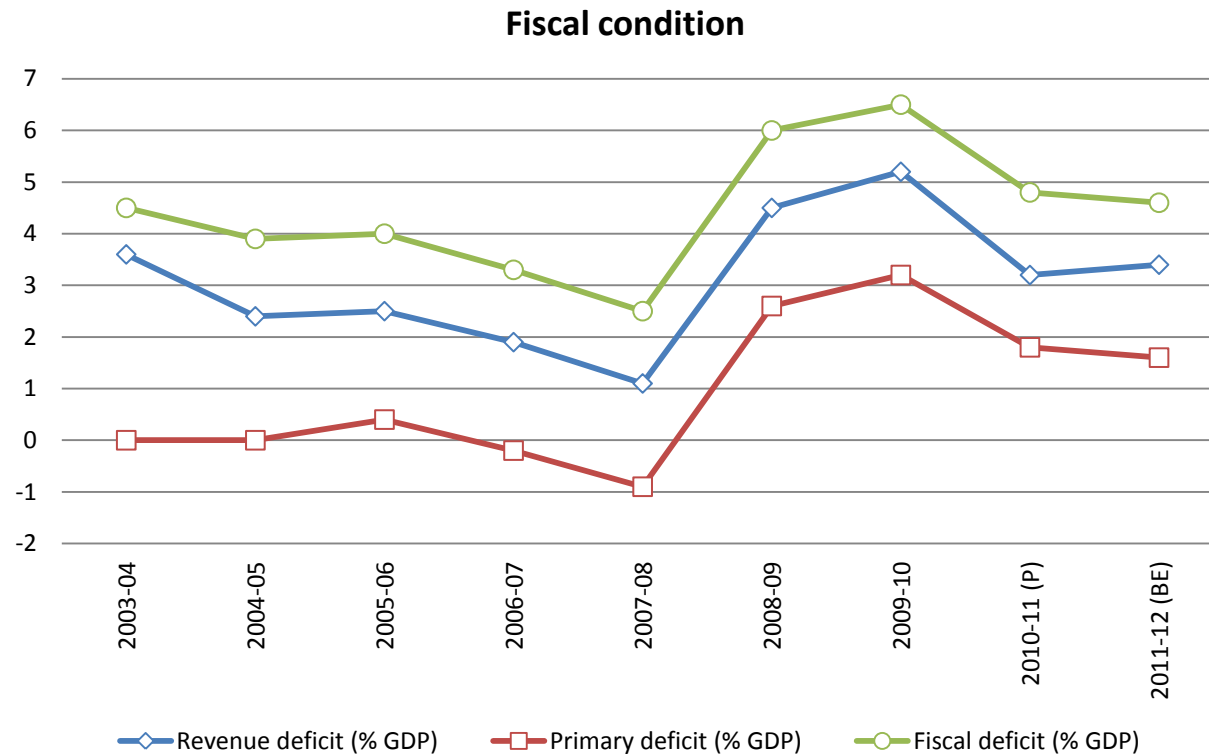
And skilled labour is not plentiful either

Comparison with BCS – education



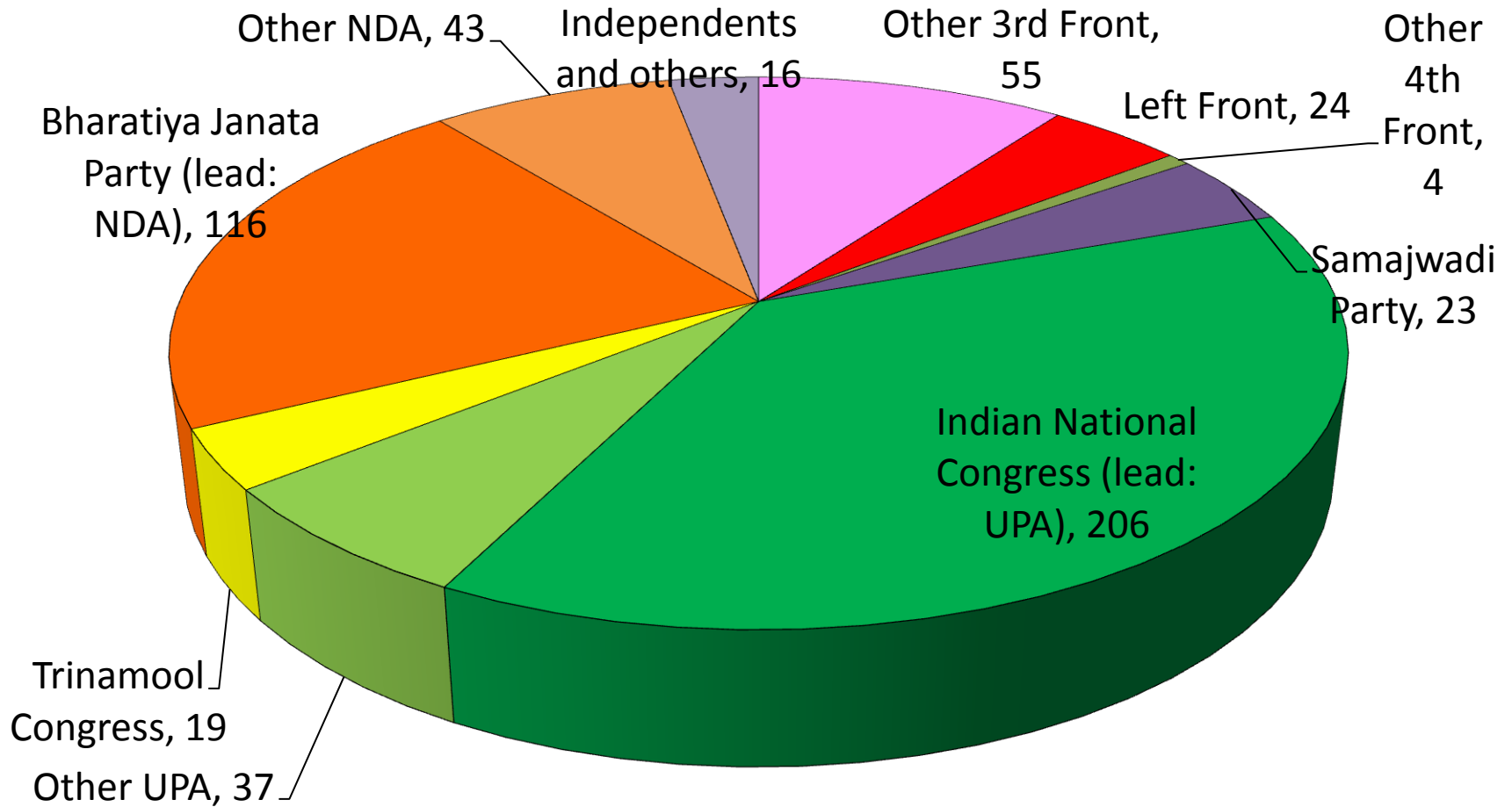
Moving on

Government deficit

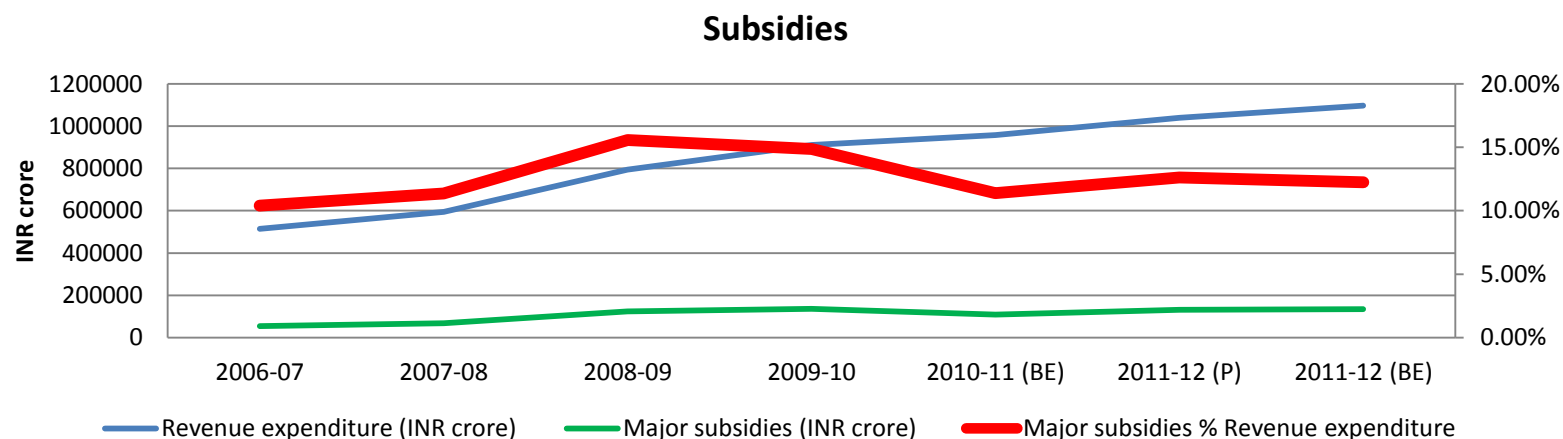


*The government has little manoeuvring room
with respect to investment in physical
infrastructure and education*

Electoral compulsions



Expenditure on subsidies



Source: Economic Survey 2011-12, Government of India

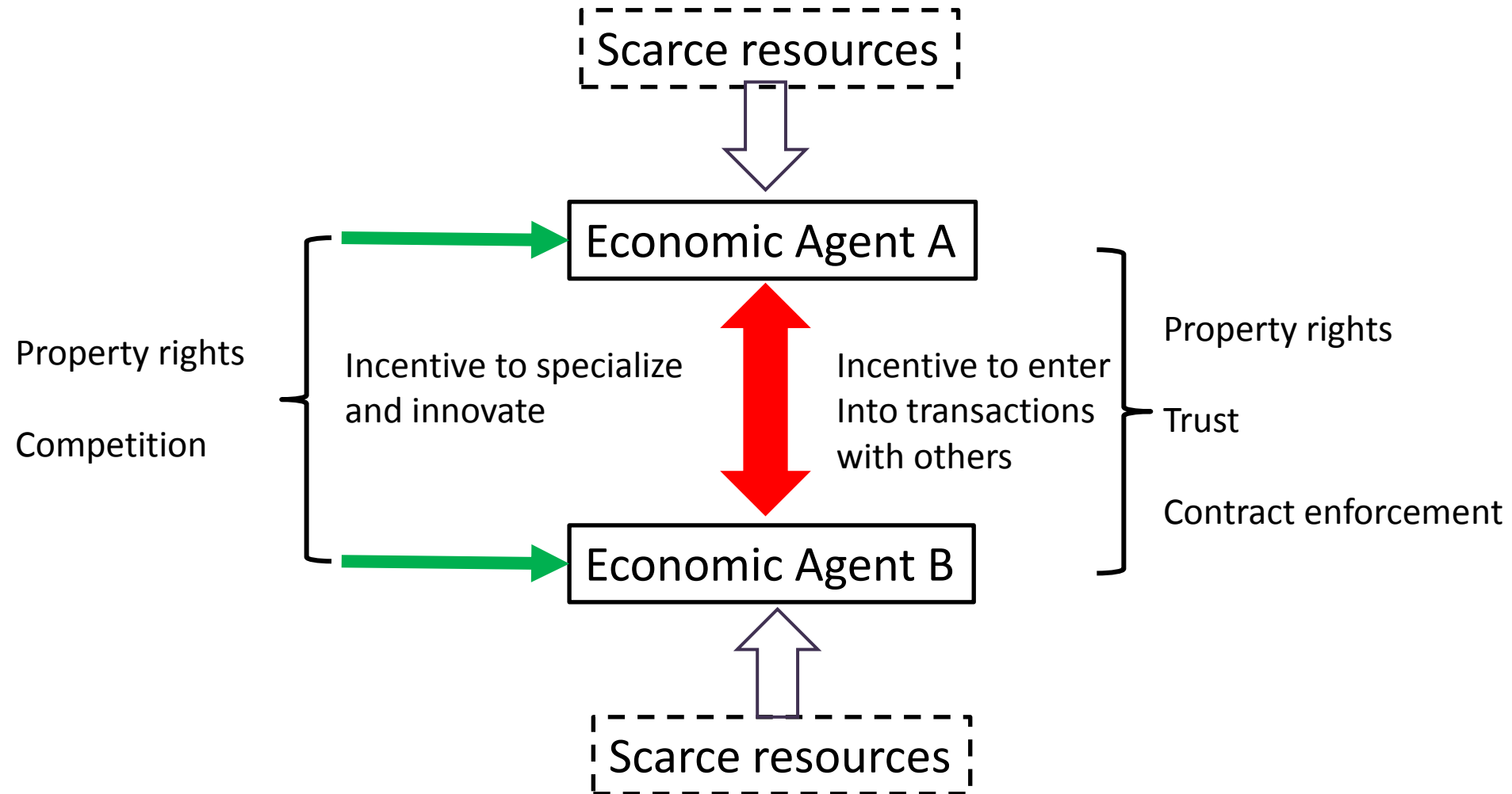
	Andhra Pradesh		Maharashtra	
	INR million	% Total	INR million	% Total
Cost of inefficiency	2058	26.5	295	16.0
Income transfer	4537	58.5	1036	56.0
Cost of leakage	1161	15.0	529	28.0
Total cost of subsidy	7778	100.0	1883	100.0

Source: Dutta, B., Ramaswami, B. (2001). Targeting and efficiency in the public distribution System: Case studies of Andhra Pradesh and Maharashtra, *Economic and Political Weekly*, May 5, pp.1525-1532; Table 9.

Electoral politics offers little scope to rapidly reduce revenue expenditure and thereby increase capital expenditure

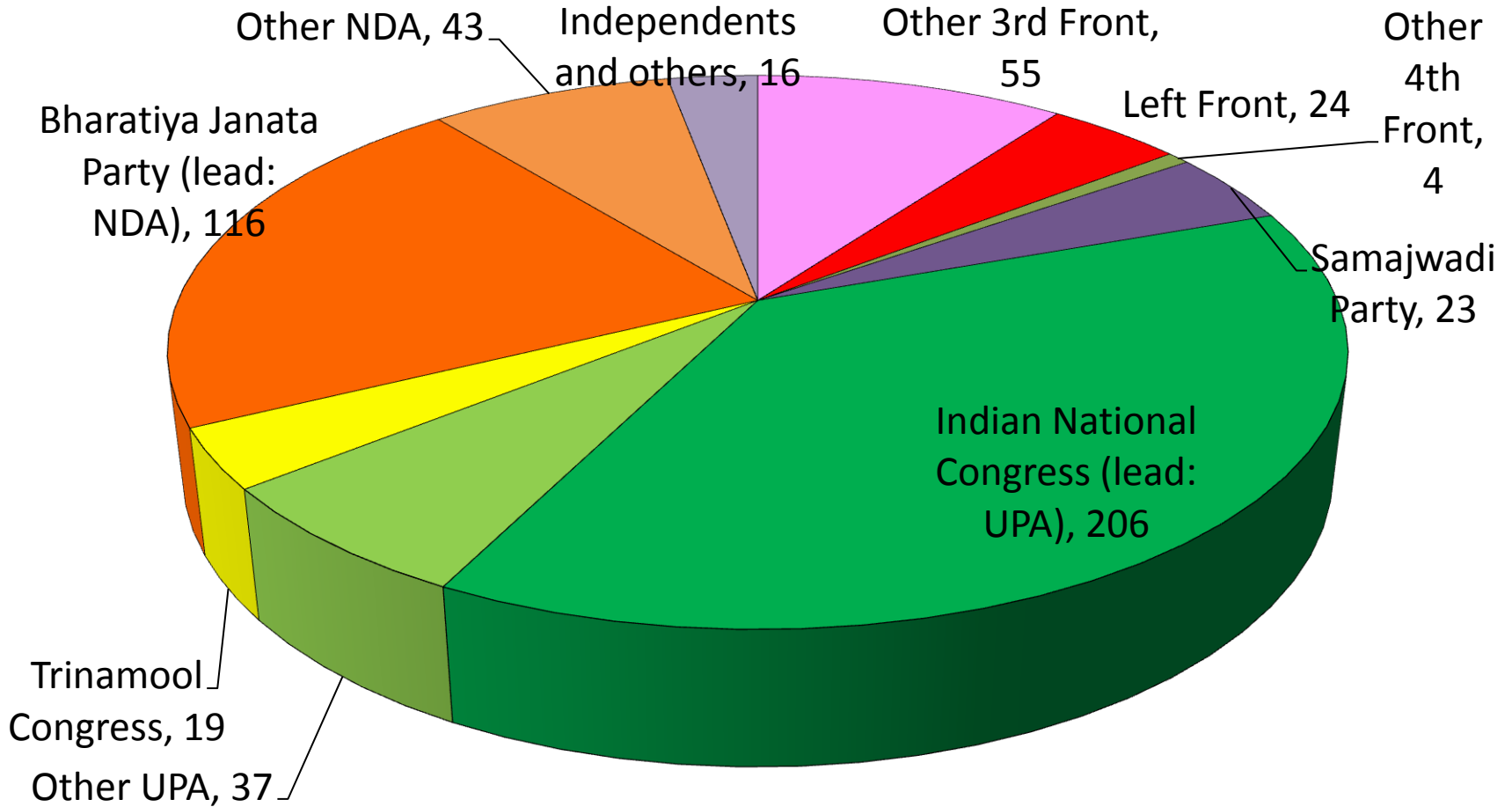
Moving on

Importance of institutions



So improving institutional infrastructure may be the way out, and that may not be a second-best option

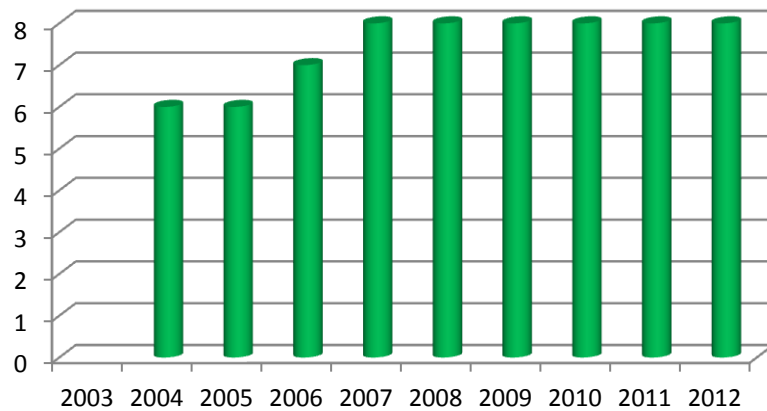
Fractured legislature



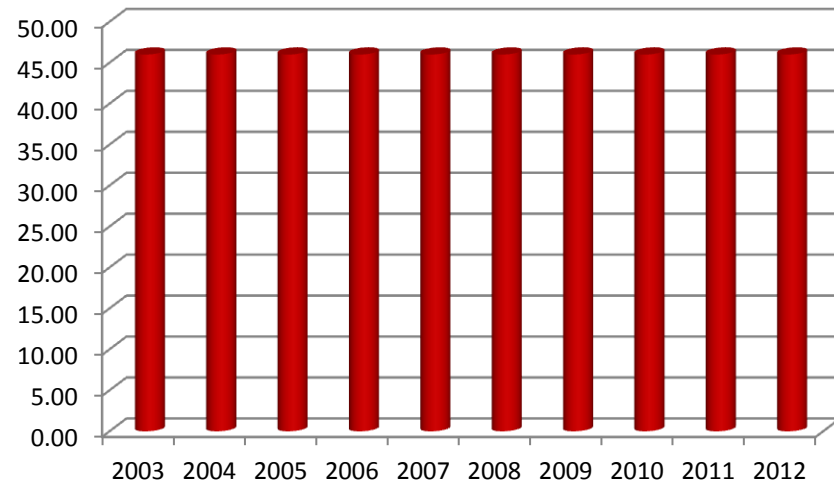
But passing new legislations (and even executive orders) are proving difficult

Law and its enforcement

**Strength of legal rights index
(0=weak to 10=strong)**

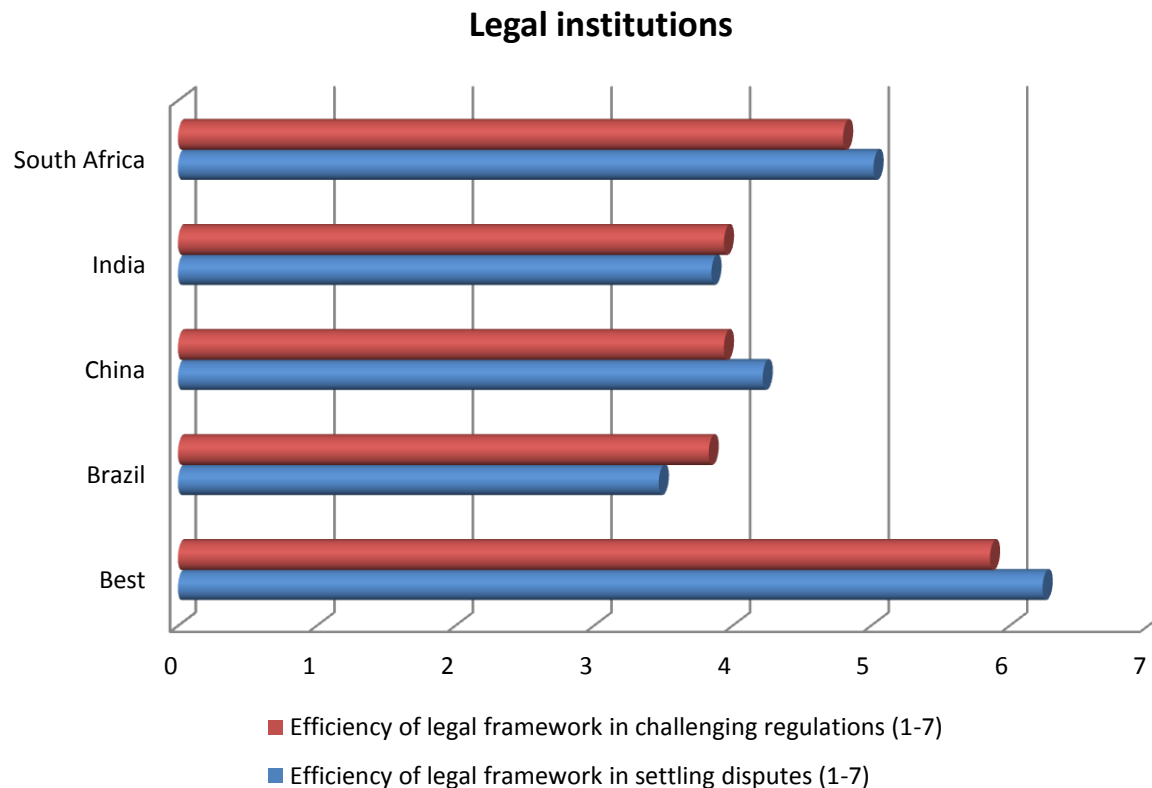


Procedures to enforce a contract (number)



And good intentions and legislations come to nought at the time of implementation

Comparison with BCS – legal institutions



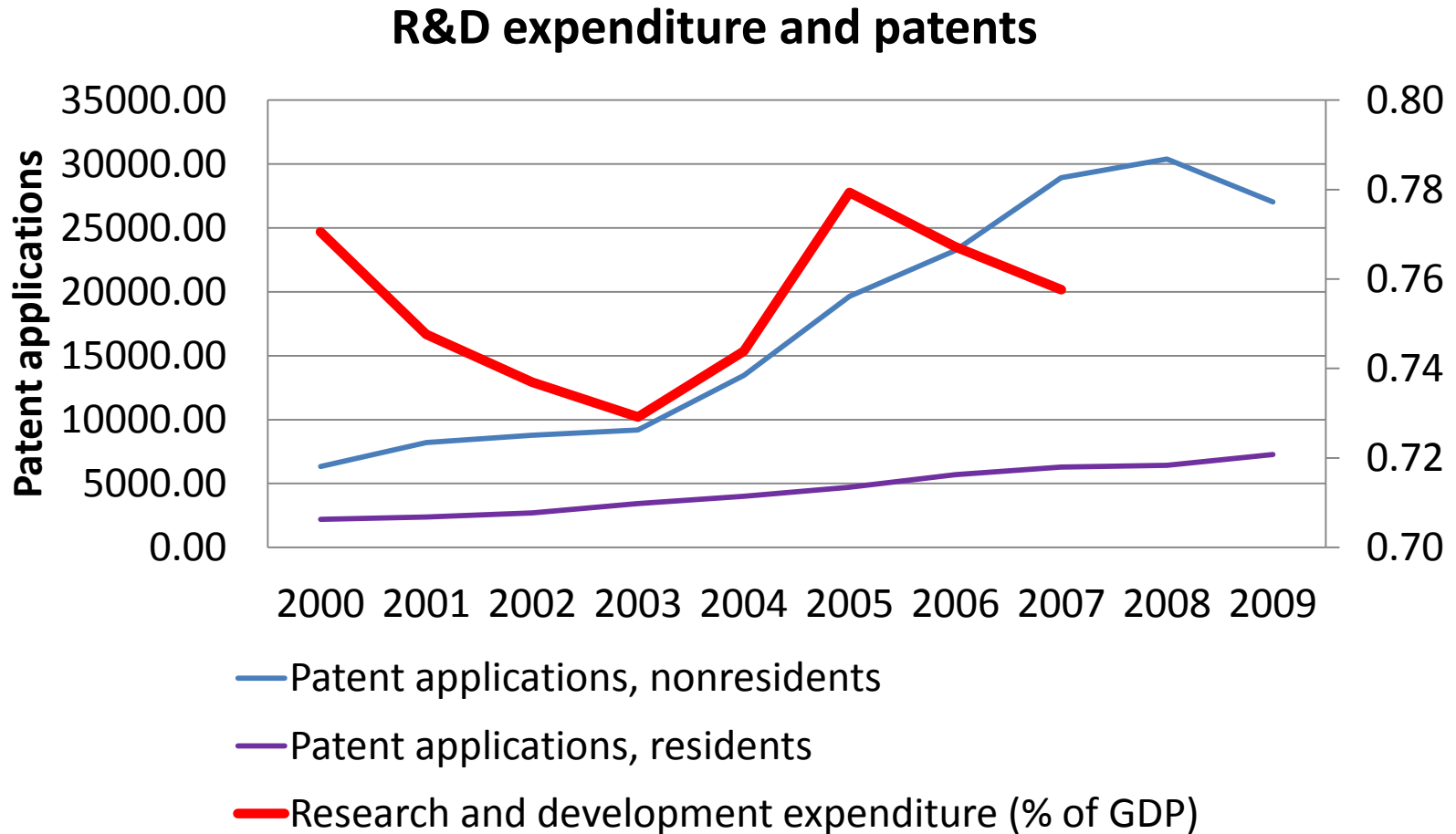
Moving on

Implications for the private sector

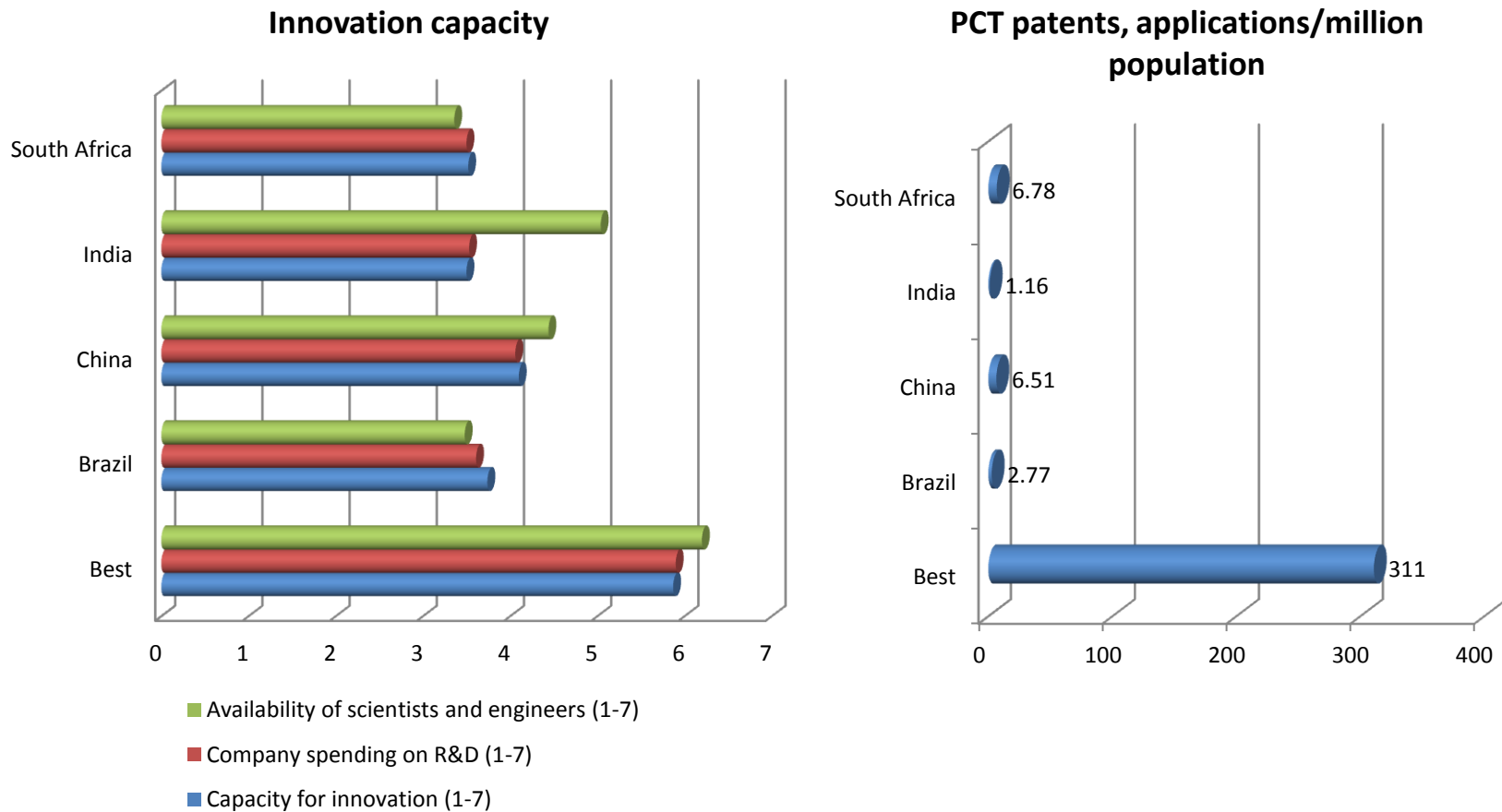
- **Uncertainty**
- **Transactions cost**
- Agency cost

Is the private sector (which is not all about the likes of the Tata Group) ready to shoulder the responsibility?

Innovation



Comparison with BCS – R&D and innovation



Agency cost

- Family firms (and business group affiliated firms) are less likely to invest overseas
- Business group affiliated firms have lost the advantage vis-a-vis unaffiliated firms with respect to technological progress
- Business group affiliated firms retain an advantage vis-a-vis unaffiliated firms with respect to risk management but they are not as efficient at using financial resources

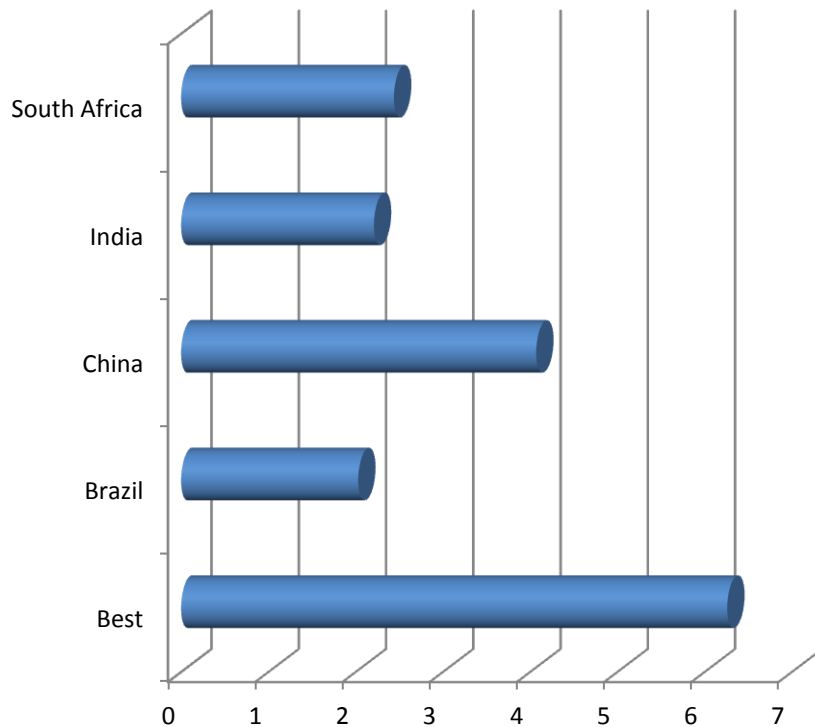
Where does it leave us

Questions begging answers

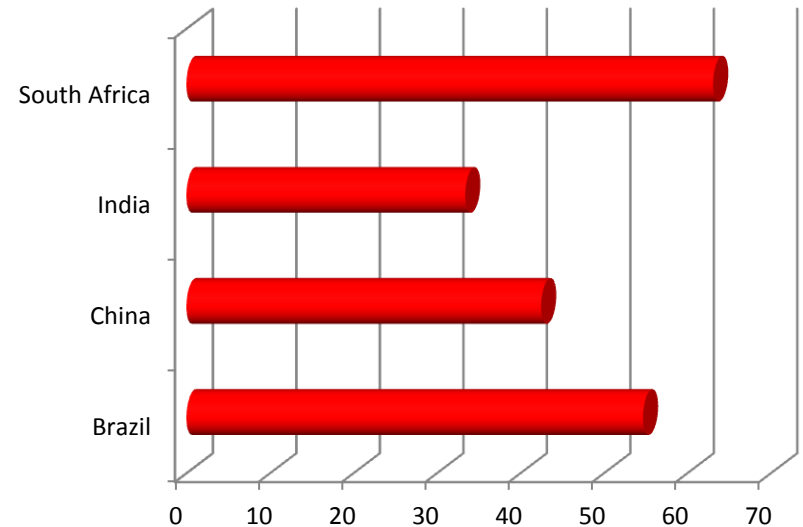
- Is it a text book example why Solow-vian convergence with developed countries does not eventually take place?
- Is it a text book example of how weak institutions can inhibit growth in the longer run?
- Is it a text book example of how a break down in social contract reduces the ability of the government to bring about changes that are essential for sustainability of growth?

The more things change

Public trust in politicians



Gini index



The Gini indices for Brazil and South Africa are for 2009, and those for China and India are for 2005.

Source: Global Competitiveness Index 2012-2013, World Economic Forum

Source: World Development Indicators, The World Bank

A return to 6.5-7.5% growth rate is not infeasible, but sustained growth rate of about 10% will require structural changes that, in turn, require trust (or faith) in government, a pre-requisite for which is good governance