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`Economics' of prosperity: Why the dominant perspectives may be unhelpful to make sense of underdevelopment

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`Economics' of prosperity: Why the dominant perspectives may be unhelpful to make sense of underdevelopment

Introduction

"India is still recovering from a bad case of old-fashioned socialism¹ ..."

When I was asked to write a book -review on Professor Vijay Joshi's recent work (India's Long Road: The Search for Prosperity), I had never written one before. How could one comment in less than 1000 words (specified limit for most publications) a comprehensive scholarly work that runs into over four hundred pages (and lists nearly 500 works in its bibliography)? But I was assured I could learn. This meant my supervisors were flexible with time (and perhaps with the 'quality' of output). To begin with the learning exercise, I read a few reviews of the book. In searching for reviews, I came across a lecture which the author had delivered at a prominent university department². The above quote comes from the lecture. Paradoxically, the author himself suggests that only three countries – South Korea, Taiwan and more recently China – have had rapid and sustained economic growth for three decades (Chapter. 1). I say paradoxically because in all the three cases, including in recent cases of rapid economic growth such as Vietnam, there have been elements of so -called socialism as the states have played roles far greater than that of the oft-prescribed gatekeeper and night-watchman. In fact, they continue to play an active part in enabling structural transformation. Other late-developers such as Germany and Japan have had (and continue to have) similar orders. The kind of role the respective states have played in the three countries (e.g. the active and broad-based industrial policy) is too well-documented to overlook³. At the risk of oversimplification, it appears meaningful to contend that policies around growth and development have usually been about a mix of both 'socialist' and 'non-socialist' ideals. The two models of governance, if you will, have barely functioned as silos.

This article is mostly a book-review but I take a slightly revisionist approach across several generally accepted conventions, for example, the length (the article goes well-beyond the 1000-word convention). The 'deviation' from rules, however, has specific objectives. I have critically analyzed Joshi's work and in so doing include relevant evidence, debates and questions not just from economics but also from other disciplines such as history and political science.

¹ The author delivering The Corden Lecture at the University of Melbourne, 2017 (Goerge, 2017)

² See (Goerge, 2017)

³ See (Amsden, 1989; Amsden & Chu, 2003; Evans, 1995; Wade, 2004, Weiss, 2005)

Reviewing India's Long Road

What policies and reforms can put India on the path of rapid and sustained economic growth (or prosperity⁴)? The book sheds light on, not just the required policy initiatives and reforms (several critically impending⁵), but also the probable explanations underlying the suboptimal growth performance and development outcomes. The book is written for a wide audience – economists, policymakers and students - among others.

Compared to sub 1 per cent economic growth between 1900 and 1950, India, a manifestly 'free market' economy then (an era where countries like the US, Japan and Germany used active Hamiltonian policies to build production transformation capabilities), achieved a rather commendable 3.5 per cent growth between 1950 and 1980. The economic growth in the three decades between 1950 and 1980 appears reasonable because India was constrained owing to factors like severe droughts, multiple wars and the most critical of all, the political challenge to keep a diverse society together. Maintaining political unity within the framework of a democracy has been an accomplishment⁶ and in fact serves as a model for other diverse nations. Joshi notes that the 'Hindu growth' (1950 - 1980) is suboptimal when compared to other developing countries (primarily Korea). India indeed could not achieve the same economic growth as Korea did but nor did countries like Pakistan or Philippines, then relatively advanced compared to Korea. For Joshi, explanations for the divergent path lie in factors like Korea's initial conditions (greater literacy compared to countries like India for example, Chapter. 2), India's statist command and control policies and regulations that produced inefficiencies as well as a general contempt for the price mechanism (Chapter. 2). While there were indeed differences in the initial conditions, such conditions did not come from nowhere and in fact the institutional processes that led to such conditions impact development outcomes. In fact, understanding the evolutionary process of institutions – societal and political – offers a credible window as to why similar policies (such as active industrial policies in both India and Pakistan) yielded such varying outcomes⁷. As a society, Korea has had a different path of evolution owing to, among other things, a deep and highly repressive Japanese colonialism⁸. The society and its institutions got so structured that subsidy-receivers (the firms) could be

⁴ Per capita income like a country like Portugal where the author posits that the national income is widely shared even the poorest have reasonable standards of living)

⁵ Reforming public health for example (Chapter. 9)

⁶ Historian Ramachandra Guha argues that while countries like Pakistan could not accommodate credible demands from powerful factions (such as on linguistic autonomy) and saw major conflicts, the shifting political equilibrium allowed numerous often warring factions to co-exist in India (not from the book, The New Indian Express, 2017)

⁷ See (M. H. Khan & Blankenburg, 2009; Kohli, 1997)

⁸ See Kohli (1997)

credibly disciplined to perform (or meet export targets set by planners⁹). Indeed, the dominant strand of economic analysis, often with which economics is considered synonymous with, considers itself a physical science and has been extremely apolitical and ahistorical and even if it dwells into history, much of it is rather superficial often bordering around sensationalism. India's development outcomes (in metrics like the number of people below poverty line, Chapter 2) in the three decades of so-called 'Hindu' growth, were not very encouraging. In explaining the suboptimal economic growth and the rather modest outcomes, Joshi contends that the state -driven command and control policies - planning driven dominance of public undertakings (PSUs) in economic activities, licensing on entry, exit and investment and protectionist trade among others created inefficiencies and distortions. It appears that the several exogenous shocks - droughts and war in mid 1960s and droughts and war and quadrupling of oil prices in the 1970s among others – constrained sizably the capabilities of the state (captured well by Joshi's previous work of which he is co-author¹⁰). The rise in oil prices resulted in rapid deterioration in terms of trade in 1979, also the point at which the structural break occurred.

Professor Joshi attributes the structural break and the subsequent increase in economic growth to "marketization, hesitatingly first, explicitly then (Chapter. 2)". The work, however, almost flatly ignores critical micro-meso-developments between 1950 and 1980 that have been instrumental in the emergence of many competitive sectors of today such as the automobiles, IT and pharmaceuticals (among the top export items). These are among the flagship sectors responsible significantly for India's growth and development story as well as for India's reputation as a sophisticated manufacturing hub. Public Sector Undertakings (or PSUs) like Bharat Electronics Limited, founded in 1954, functioned as a training ground for thousands of engineers¹¹. The PSU churned out thousands of trained engineers and this essentially was the groundwork for turning Bangalore into the Technopolis of today (Evans, 1995). Others have stressed on how the prestigious Indian Institute of Technology (the IITs) and the Indian Institute of Management (the IIMs) graduates form the core human resource base in sectors like IT and manufacturing¹². Both the IIT and the IIM are part of the Nehruvian legacy. The extremely competitive

⁹ See (Khan & Blankenburg, 2009)

¹⁰ See (Joshi et al, 1998)

¹¹ See Evans (1995)

¹² See Rajan et al (2006)

automobile sector (India in FY16 has exported more cars than China¹³), its foundation was laid when in the 1980s, Suzuki was roped in for a joint-venture (JV). The JV became possible because the highest political leadership was committed for it while capable Indian bureaucrats were scouting for the potential partners (Khan, 2015). Maruti-Suzuki started off amid heavy protection (85% tariff) or a guaranteed domestic market though this was conditional upon time-bound local content requirements. Since then, the expansion in the automobile sector has led to development of credible linkages such as emergence of large number of world-class auto-component manufacturers (ibid.). Joshi's work, much like the dominant 'development and prosperity research', fails to acknowledge that states, the most credible organized institution in a typical resource and capability starved society, are instrumental to societal learning, capability building and promotion of sectors with greater growth potential.

Professor Joshi associates the late 1970s and early 1980s with the 'unleashing of animal spirits' or a period that saw relatively high economic growth compared to the past. This is in line with how most other economics research looks at the structural break issue in India¹⁴. The fundamental assumption (partially tenable indeed) is that relatively rapid economic growth will result into greater societal progress or development. As one of the repercussions of such premise, it would not be wrong to assume that the period since the late 1970s is assumed as one with relatively rapid growth and development. However, such broad-brush analysis cannot be trusted to capture wellbeing. Between late 1970s and mid 1980s, the phase, the so-called 'animal spirits' phase (Chapter. 4), saw almost 50,000 textile-sector workers lose their jobs in the textile city of Ahmedabad (Shani, 2007, Pp 37-41). Joblessness meant widespread deprivation became a norm as the other sectors (mostly informal services or odd-jobs) fetched the workers a quarter of what they earned in textiles (ibid.). Recently, the demonetization in India has wreaked havoc on the informal sector workers. Bear in mind that over 80% of the workers in India are in the informal sector. Despite the misery among workers in sectors like construction that employs millions, the recent economic survey neither has aggregate data nor cases-studies on the hardships faced by the largely voiceless workers (Economic Survey, 2018). If the issues concerning majority workers remain invisible, can solely the current order of 'economics and economists' guided policy processes be relied upon to solve societal challenges? Indeed the 'omission' could be driven by factors such as political considerations (as perhaps is the case with India and its current regime's demonetization shock). Imminent is a major rejig in the way development policy is guided and researched upon. Reading economic growth rates and considering it a proxy for wellbeing is problematic. Hence, more initiatives like the reassessing the measurement dynamics of societal progress (See Stiglitz, Sen, & Fitoussi, 2009) are critically impending.

¹³ See Kulkarni (2016)

¹⁴ See Rajan et al (2006) and Rodrik & Subramanian (2004)

The 1990s liberalization occurred amid a major fiscal crisis where IMF credit support was conditional on reforms – *inter alia*, devaluation, tariff reduction and elimination of quantitative restrictions on essential imports such as machinery, and delicensing (Chapter 4). The 1990s saw over 5.5% growth fueled by rising, more stable investments and greater production efficiency driven by smooth imports of required inputs. The 2000s, specifically the 2003-2010 phase has registered the fastest growth so far, over 8%, in line with global buoyancy and largely via heavy firm level borrowing and increased corporate savings and investments. Beginning in 2011 and exacerbated by the global financial meltdown, the growth has slowed down at 5% on average amid declining corporate investment. The book argues that this occurred because of deleveraging among corporates and governance failures such as scandals (Chapter 4).

Dr. Joshi argues that despite the ingredients – macroeconomic stability, no serious conflicts and non-extractive governance - among others, India grapples with suboptimal growth and development (jobless growth and severe underemployment). Creating good-quality jobs is certainly a complex yet urgent challenge for every society (Andreoni et al, 2016). Most economic research contends that India has missed the labour-intensive industrialisation bus and in explaining this, economists including Professor Joshi have attributed factors like, *inter alia*, India's restrictive labour laws. The 'restrictive labour law line' of research while widely cited has also been recently contested¹⁵. On the other hand, much of those employed are in the informal sector. Despite churning out half the industrial output (Chapter. 5), the informal sector workers (over 80% of those employed are in the informal sector), other than being miserably paid, are vulnerable and voiceless in an order where a disproportionate extremely unfair value share is captured by capital. The current exploitative order that has persisted rather dangerously in India, perhaps solely benefits capital albeit only in the short-termist narrow sense. The adverse rent seeking dynamics perhaps explain the burgeoning inequality¹⁶ and the fact the major capitalist houses in 1947 continue to be so.

Dr. Joshi rightly contends that India continues to experience largely jobless growth because of its inability to expand labour-intensive manufacturing and in this, the principal constraints are, – *inter alia*, poor quality physical infrastructure, lack of credible skills among workers, poor SME finance access, minimally conducive business environment (corrupt tax officials) and the employment protection laws (that require firms above a certain size to obtain permission for, *inter alia*, laying off workers, Chapter 6). On whether credible industrial policy interventions are a potential policy measure, the author suggests that such interventions – 'requires a smart, dispassionate and benevolent state which can 'pick winners' - (See Chapter. 6). Professor Joshi goes on to argue that countries like India should avoid the primrose path of such policies because such policies have a thin 'empirical case' (Chapter 6). Joshi's brief insight on industrial policy is extremely narrow and in fact reflects a superficial understanding of dynamics like industrial policy driven learning. For example, India's real exchange rate has appreciated by nearly over 20 per cent since 2014 and this has sizably hurt exports. While Joshi does highlight this issue around the appreciation (Chapter 8), he perhaps is not aware that, in fact, preventing real exchange rate appreciation (among other exchange rate management strategies) is itself a major industrial policy tool

¹⁵ See Bardhan (2015)

¹⁶ See Rangarajan et al (2018)

(as argued by equally if not more illustrious economists, See Guzman, Ocampo, & Stiglitz, 2017). Perhaps Joshi's 'aversion' to industrial policy stems from an ideological (so-called free markets guided by the invisible hand) and normative epistemological standing which contradict his own philosophical premise that dispassionate and objective (read rational) approaches are almost always desirable (as Dr. Joshi argues that states should not intervene for example via an industrial policy because they may not be dispassionate, smart and objective).

While there have been modest improvements, India continues to fare poorly in critical development outcomes such as nutrition and infant and maternal mortality. India's performance compares poorly to several of its regional peers who have significantly lower per capita incomes. This contention, though debated by a few citing technical grounds¹⁷ is widely agreed upon including in this work (Chapter 9). Professor Joshi insightfully dwells into how public health interventions such as immunization, basic sanitation, nutrition and other preventive and promotional healthcare measures – which impact overall health outcomes significantly, are largely neglected and underfunded (less than 10% of state health expenditure, Chapter 9). Indeed the Dr. Joshi links the appalling outcomes to the weak preventive and promotional public health services. In explaining this, the author delves into history as well as political economy contending that it was the powerful medical lobby that got public health merged into medical services (Pp. 189). In what is a display of his erudition, Dr. Joshi evidences that Tamilnadu, which has much better health and overall development outcomes, bucked the broader trend by retaining a dedicated public health service. For a host of reasons including an inappropriate incentive structure, medical services, associated largely with curative health, addresses only partially the overall health-related challenges.

¹⁶See (Rangarajan & Dev, 2018)

¹⁷Economists like Bhagwati suggest limitations in the way infant mortality rates in countries like Bangladesh are computed (Bhagwati & Panagariya, 2013). Despite 'technical arguments', there is consensus that social underdevelopment and multidimensional deprivations are widespread in India.

Widespread multidimensional deprivation has been common in India despite dozens of targeted subsidies and welfare programs. While welfare entitlements like income guarantees have indeed played a role in tackling extreme deprivation and hunger, chronic poverty is rampant. Nearly half the labor force is into low productivity agriculture and over 200 million people are below the poverty line (Chapter 10). The author proposes a universal basic income (UBI), which raises average incomes to the poverty line. This is indeed a commendable prescription (Chapter 10). UBI, the author estimates, will require funding at around 4 per cent of the GDP and that the fiscal space can be created by freeing up resources from existing subsidy programs, whose effectiveness, as has been documented widely, has been widely questioned¹⁸. In building the case for UBI, Professor Joshi evidences that targeted subsidies such as the Public Distribution System (PDS, subsidized food grains) have been utter failures in terms of providing reprieve to the poorest. In fact, the targeted subsidies, a significant chunk, is exploited by unintended beneficiaries (though this lot perhaps is not necessarily well-off) often by diverting grains to the black market (Chapter 10). The author documents cases like Chhatisgarh where over 90% households are enlisted as Below Poverty Line (BPL) while the number of BPL cards issued exceeds the overall population. The section on UBI indeed documents the failures of targeted subsidies but (perhaps the mark of a credible academician) it does not shy away from highlighting intricacies in devising public policy and how policy outcomes can be non-linear and unpredictable. In Tamilnadu, unlike Chattisgarh, the leakages in targeted PDS are less than 10 per cent. The author evidences complexities in other welfare programs like National Rural Employment Guarantee (NREGA) where there are inefficiencies such as delayed payments but it has benefitted the poorest due to the program's attributes' such as selfselection where only the poorest turn-up asking for work.

To tackle the leakages in targeted PDS, Professor Joshi suggests replacing the multitude of subsidies with Aadhar (National Biometric Identity Card) linked cash transfers. Indeed, and as Joshi notes, India has the technology to implement cash transfers. On resources, the author rightly argues that subsidies - on fertilizer, coal, electricity and railway fares – largely benefit the thriving and often promote, for instance, unsustainable overuse. The author estimates that non-merit subsidies are roughly 12% of the GDP and that resources can be freed up to finance the UBI (Chapter 10). However, the proposition that non-merit subsidies can be reduced to fund a UBI, indeed a reasonable proposal which has been proposed repeatedly¹⁹, raises a host of fundamental questions. Subsidies such as in fertilizer or agriculture being

¹⁸ See (Sen, A. 2014)

¹⁹ See Economic Survey (2018)

tax-free, are essentially rents and redistribution mechanisms to powerful factions and classes which can destabilize the regime²⁰. The rents, distributed through legal as well as non-legal means, fuel the patronage network and ensure their loyalty²¹. The rents are a necessary element to ensure the political equilibrium, in absence of which there may not be political stability²². If we go by the dynamics comprehensively outlined by the World Development Report 2017, the subsidies are here to stay till major structural transformation takes place where there are several competitive sectors that enable arms-length based functioning. After all, several governments have come and gone by but the competitive clientelist order, certain variants of which do produce growth enhancing stability, remains intact²³.

It was felt, perhaps rightly, that the current BJP government has the mandate to tread difficult paths and implement difficult decisions unlike a typical coalition government with, *inter alia* ideological differences. However, the actual policy paths taken (such as hasty adoption of demonetization) as well as the outcomes (often owing to poor designs such as in the GST) have been somewhat divergent often disappointing than anticipated. The difficulties in disbanding several unwanted subsidies on welfare programs have multiple dimensions and complexities when it comes to design or actual implementation. A particularly relevant paradigm that enables a greater understanding of how societal, economic and political distribution of power affects policy design and outcomes is the political settlements (PS) theory. The PS theory²⁴ argues that its stability in developing societies is largely a function of allocation of rents to the most powerful factions (with mobilization and hence destabilizing capabilities) and that the political equilibrium eventually is set at the actual distribution of power rather than what formal mechanisms (such as being a state) confers. Indeed, that policy designs and outcomes are significantly determined on distribution of power and the political settlements has been widely accepted²⁵. In this sense, technocratic physical science like estimations based on hyperbolic assumptions serve no purpose when it comes to application. To the readers dismay, Joshi's work is largely of the physical sciences type where economists with a specific 'orientation' if you will do not find political and sociological explanations objective enough (and 'quantifiable' enough).

²⁰ See Khan (2017)

²¹ See KELSALL (2018)

²² World Bank (2017)

²³ See (P. Bardhan, 2015; Pranab Bardhan, 2010; Pranab Bardhan & Mookherjee, 2000)

²⁴ See (KELSALL, 2018; M. H. Khan, 2010, 2012)

²⁵ See (UNIDO, 2016; World Bank, 2017)

This is not to suggest that the author does not delve into the more realistic side of affairs. Welcome as it is, the author, in the concluding chapter (Chapter 13) contends that the BJP should not toe the line of the RSS (BJP's parent organization) as doing so runs the risk of not just curtailment of individual freedoms but also the imposition of majoritarian tyranny. Indeed (and with the benefit of hindsight), if one goes by statements²⁶ (perhaps aspirations) made by most BJP legislators (including the PM and ones with Ivy-league training in economics), one gets a sense that not everything is alright when it comes to stability and progress in India.

To sum up...

For India's continental size and numerous heterogeneities across, for example, among the states and their levels of economic and institutional development, it is indeed a challenge for any scholar to provide an aggregate macro policy perspective and at the same time, cater to numerous non-uniformities. In this sense, the book, with nearly 500 works in the bibliography, does well to address several questions it outlines. However, and as can be established from Hume's law, no normative prescription is derived from a positive analysis unless there is a normative idea as an assumption. It is for the readers to infer for themselves the normative assumptions in this extremely useful scholarly work.

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²⁶ See Ghosal (2015)

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