

Preface

Simply not Debatable!

On December 02, 2010 Professor Jagdish Bhagwati delivered a Lecture to a joint session of the Lok Sabha and the Rajya Sabha (the Lower House and the Upper House of the Indian Parliament) with the Prime Minister of India Manmohan Singh, the Lok Sabha Speaker Meira Kumar, the Vice President of India and Chairman of the Rajya Sabha Mohammad Hamid Ansari on the dais and dignitaries including Sonia Gandhi (Chairperson of the United Progressive Alliance – the ruling coalition in India), L K Advani (former Deputy Prime Minister of India and a senior leader of the main opposition: Bhartiya Janata Party), and many other Members of the Parliament such as Karan Singh, Shashi Tharoor and N K Singh in attendance. The Lecture, that is available now in a revised augmented version on the Lok Sabha web site (www.loksabha.in) alongside the shorter oral version, was entitled “Indian Reforms: Yesterday and Today” (the 3rd Professor Hiren Mukherjee Memorial Annual Parliamentary Lecture).

It is a Myth that Reforms are Not Helping the Poor

The core point of his Lecture was that it is a myth that reforms are not helping the poor. He said that several analyses reveal that “the enhanced growth rates have been good for reducing poverty, while it has not increased inequality measured meaningfully”.

Stating that high economic growth has led to greater revenues, and that India was finally able to spend more on health and education for the poor and underprivileged, Professor Bhagwati described conventional growth-enhancing reforms as stage one, and the spending on health and education of the poor as stage two reforms.

Both were 'inclusive', he said, adding that Stage 1 reforms have benefited, not immiserised, the poor and the underprivileged, while Stage 2 reforms, rendered possible by Stage 1 reforms, reinforced "the beneficial pro-poor effects of stage one reforms".

As an advocacy group committed to raising the living standards of people, and seeing that the issues raised by Professor Bhagwati are intrinsic to the policy discourse, CUTS International posted a news item of the Lecture on its web site and circulated it widely through its Internet-based Fora. The response was huge and unprecedented. The e-groups reach out to a large number of social scientists, intellectuals and policy-makers in India and indeed worldwide. Nearly all the contemporary important Indian economists joined the debate, which ran into thousands of pages, including some which were argumentative. Quite naturally the posting commentators did not respect the boundaries and some were quite garrulous.

This led Martin Wolf, Chief Economics Commentator of *Financial Times* to write: "Obviously higher incomes are a necessary condition for better state-funded welfare, better jobs and so forth. This is simply not debatable. Indeed, only in India do serious intellectuals dream of debating these issues." (page 57)

Reforms in India started in earnest in the early 1990s, and until then the growth story was disappointing. The lack of growth had led to a failure of the growth strategy as the principal means to 'pull up' the poor out of the trap. But once the growth picked up due to the reforms, poverty declined.

Since the population is huge while there was a decline in percentage, the absolute numbers still remain overwhelming.

Most Agree that Growth is Important, However....

Most commentators agreed that on the overarching importance of growth *albeit* to a varying degree – the forceful assertion by Professor Bhagwati. The contention that more attention to growth promotion policies is absolutely vital for developing countries like India with high initial levels of poverty mainly arise on account of three different perceptions, which tend to overlook certain positive aspects of growth.

First, a majority of those who underrate the role of growth believe that growth almost invariably leads to high income inequality because accrual of benefits thereof is biased in favour of the upper strata.

Some commentators including Jean-Pierre Lehman (page 42), Raymond Saner (page 44) and Ravi Chaudhry (page 77) pointed out the glaring and growing disparities between the rich and the poor in the context of India's post-reform experience. This proposition (that growth typically caters to generating wealth for those who are already rich) is unfair considering that rising income inequality does not prevaricate poverty reduction as argued by Professor Arvind Panagariya (page 25).

Alok Ray provided examples of direct and indirect poverty reduction effects of growth in absolute terms (page 28). On a related note, Shantayanan Devarajan argued that social spending could do little to reduce income inequality and may even raise it if not targeted properly by giving the example that 33 percent of public spending on health in India accrues to the richest 20 percent (page 66).

Secondly, the question whether growth leads to poverty reduction has been debated while mostly ignoring the fact that flow of causality between these two is not unidirectional and

static but circular and continuous. Many participants in the debate resonated reports in the popular media that growth has failed to deliver for the poor, while some shared instances of social spending failing to deliver real economic empowerment of the underprivileged (*High Growth Fails to Feed India's Hungry*, James Lamont, *Financial Times*, December 22, 2010). On the contrary, examples of reinforcement of the correlation between growth and poverty reduction were cited by G S Bhalla (page 67) and Professor Panagariya (page 68).

Ravi Chaudhry drew attention to the fallacy of considering the mutual effects of growth and poverty reduction as static and stated the importance of giving growth policies a head start to be accompanied by poverty reduction programmes after reaching a certain threshold (page 77). This view also buttresses the idea of sequencing Stage 1 and Stage 2 reforms as mooted by Professor Bhagwati in his parliamentary lecture.

Thirdly, some experts tend to harbour a belief that it is not feasible to target growth and poverty reduction through simultaneous policies. This view is epitomised by Abhijit Banerjee's comment which implies that governments are generally observed to be doing only one thing right at a time since there is always a trade-off (page 24). He stated that government's capacity to do anything new is always limited especially when the state is weak.

Professor Panagariya strongly countered this with the argument that governmental capacity to execute a mix of policies can vary considerably and improve significantly over time as has been observed in the Indian context (page 69). He further fortified his argument by proposing policy reforms on as many fronts as possible and through means that will impose a minimalistic burden on governments for their execution.

Additional responses on this issue stressed that the past trend of focusing on a single policy objective must give way

for setting multiple policy goals which is by no means impossible.

Given the underlying premise that growth must only be a means to an end: better quality of life for all, to which most experts adhere to, the debate provides an important synthesis by way of directions for future course of action. Several important insights emerged from this synthesis. Most of the commentators unanimously agreed that there is an urgent need to create favorable conditions for participation of unskilled labour in the growth process. Governmental support should be extended to improve the bargaining power and social security of employees in the unorganised sectors.

Arne Melchior adroitly argued that disguised unemployment in the agriculture sector has to be removed by generating new and productive non-agricultural jobs (page 74). At the same time, a solution must be sought for eradicating massive corruption running through public institutions and establishments. This, in turn, will help to substantially improve the exchequer's capacity for higher investment in health, education and other social sectors.

Indeed and this is happening in India as pointed out by Swaminathan S A Aiyar (*It's Social Spend Boom, Stupid*, Times of India, New Delhi, February 02, 2011, page 92): "Between 2004-05 and 2009-10, central plus state social spending more than doubled from ₹1.73 lakh crore to ₹4.46 lakh crore and from 5.33 percent of GDP to 7.23 percent. So, social spending has actually risen faster than GDP. Rapid GDP growth has financed, not hindered, rapid growth of social spending. The Economic Survey (2009-10) says gross central revenues more than doubled in 2004-05 and 2009-10, from ₹3.04 lakh crore to ₹6.41 lakh crore. This helped finance the social spending boom".

On the other hand, there were still critics who seemed to think that growth had not been 'inclusive' and growth was an

obsession to be discarded. In particular, Professor Amartya Sen, who was on the CUTS Trade Forum but did not join the Forum debate while writing elsewhere, condemned the preoccupation with growth and suggested that growth had little to do with helping the poor and the underprivileged, and that obsession with growth comparisons of India and China was also misplaced.

In response, Professor Bhagwati and Professor Panagariya (in two responses in his monthly column in *The Economic Times*, New Delhi) have noted that the post-reforms growth has indeed been good, not just for the elite or the upper middle class, but also for many underprivileged groups. The findings come from detailed empirical studies, many of them organised by Professors Bhagwati and Panagariya.

Again, some critics agreed with the proposition, apparently embraced by Professor Sen, that social expenditures rather than growth matter. But Professor Bhagwati argued that these expenditures cannot be sustained unless growth generates revenues. As he said, focus on growth matters for India as it “pulls the poor into gainful employment and also provides the revenues with which one can finance the direct programmes on health and education, which I call Stage 2 reforms” (www.financialexpress.com/news/economists-endorse-bhagwati-line-for-upa/736850/0).

This important lesson is now at the heart of the successful model of development embraced by the immediate past President of Brazil: Luiz Inácio Lula da Silva and espoused by the newly-elected President of Peru: Ollanta Humala. They embrace ‘neoliberal’ policies that promote prosperity and then use the resulting revenues to boost the budgets for health, education etc. for the poor. In fact, the ‘moderate’ advisers to the new President of Peru talk exactly in these terms, suggesting that they have been hearing the arguments in the CUTS Forum!

Many other subsidiary themes of interest surfaced in the many exchanges. To enable a proper evaluation of the multifaceted theme of the interaction between growth and poverty, in particular, this selection of the Forum contributions is supplemented by writings on the theme by Professor Bhagwati and others over the last four decades.

The Indian experience corroborates with the general pattern of growth and poverty linkage that is observed from the international experience. The share of people in poverty, defined as those living on less than a dollar per day (poverty ratio), almost always declined in countries that experienced growth. High growth allowed many East Asian countries to reduce the share of the poor in their population during 1987-1998 – from 26 percent to 15 percent and the number of poor from 417 million to 278 million. With an annual growth rate of nearly 9 percent since 1979, when it began introducing market reforms, China alone has pulled more than 100 million people out of poverty.

According to the Santiago-based Institute for Liberty and Development, Mexico's per capita growth rate of 1.5 percent in 1990s did not affect the share of people living in poverty, while Chile's 7 percent average growth rate between 1987 and 1998 reduced its poverty rate from 45 to 22 percent. Between 1993 and 1998 Vietnam's per capita growth rate averaged about 6 percent per year and the World Bank reported that its population living in poverty declined from 58 to 37 percent. Uganda's per capita growth of more than 4 percent in 1990s reduced its share of poor people from 56 to 44 percent between 1992 and 1997.

And these are not isolated cases. David Dollar (*Globalization, Poverty, and Inequality since 1980*, The World Bank Research Observer, Oxford University Press, Issue 2, Vol. 20, 2005) found that “the trends toward faster growth and poverty reduction are strongest in developing economies

that have integrated with the global economy most rapidly, which supports the view that integration has been a positive force for improving the lives of people in developing areas”.

While the role of growth in poverty reduction is undisputable, a basic disagreement among some of those who participated in this debate was regarding the extent of reliance to be placed on growth alone as the panacea for poverty reduction. A closer look at various views reveals the vacuousness of a popular perception (particularly among some Indian NGOs and their foreign supporters who have little or no understanding of the subject of economics and how it works but more often than not express their views on this subject) that growth leads to inequality.

Our discussion underlined the fact that diverse viewpoints can indeed be reconciled which is an important pre-condition for a more viable and effective policy response so that other than achieving a US\$6tr economy by the year 2020, India can reduce its level of poverty to a negligible figure (World Bank and IMF Report – Global Monitoring Report 2011: Improving the Odds of Achieving the MDGs – *High growth in India and China helps eradicate poverty: A Report, Financial Express*, New Delhi, April 17, 2011, page 134).

By successfully implementing Stage 1 reforms not only that India has achieved high growth rates but also either old institutions have been revamped or new institutions have come in place and as compared to the past the growth impact on poverty reduction is there to see (much more robust than in the past).

We would want the larger debate in future to be on the implementation of Stage 2 reforms (agriculture in particular – reform measures to get people out of agriculture and engage them more productively in other sector, particularly in manufacturing sector, and labour market reforms) and their political economy aspects. Already the Government of India

has formulated a strategy to raise the manufacturing contribution to the GDP from the current level of 15-16 percent to 25 percent by 2025 to create 100 million new jobs. This would certainly help moving people from the rural sector to the manufacturing sector, but the biggest impediment to this ambitious plan is getting land for industrial use from the current farm lands. Looking at the current highly contentious debate on land acquisition, this is going to be a tough agenda.

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