The economic reforms:looking back to look ahead

(Mains GS 3 : Indian Economy and issues relating to planning, mobilization, of resources, growth, development and employment.)

Context:

> The crisis caused by the novel coronavirus pandemic in the country and at global level has led to a debate about fresh thinking and new approaches to manage the economy and the future of humanity.

A critical reading of reforms:

- In India, various efforts are under way to enhance **economic growth** thus, it is important to briefly look at the economic reforms of the last 30 years.
- Evidence shows that the economic reforms which were launched in a major way in 1991 have enabled some credible gains for the country.
- Over a period of 30 years, burgeoning foreign exchange reserves, sustained manufacturing contribution in GDP, increased share in global exports (from a mere 0.6% in the early 1990s to 1.8%), robust information and communication technology software exports, and sustained economic growth in the range of 6%-8% are clear hallmarks of success.

Focus on technical nature:

- The economic reforms, so far, have been more focussed on the technical nature of the economy than the system, process and people.

- As a result, quite a few primary drivers of the economy — human capital, technology readiness, labour productivity, disposable income, capital expenditure, process innovation in setting up businesses, and institutional capacity — have not got enough recognition.

Human resource capital formation:

- The human resource capital (HRC) formation, a good determinant of labour productivity, has been found wanting over the entire period of reforms.
- The lack of quality education, low skilled manpower and inadequacies in basic health care have resulted in low HRC.
- The HRC rank for India stands at 103; Sri Lanka is at 70, China at 34, and South Korea at 27, as brought out by the Global Human Capital Report, 2017.

Low disposable income:

- As indicated in the World Bank database on GDP for 2019, the low per capita GDP in India, at $2,104 (at $6,997 in PPP terms, ranked 125th globally) against the world average of $11,429 (at $17,678 in PPP terms) has direct links to low per capita family income.
- Closely linked, the report by Deloitte (Global Manufacturing Competitiveness Index in 2016) reflects that the hourly wages in India have been $1.7; they are $38, $24, $20.7 and $3.3 for the United States, Japan, South Korea, and China, respectively.
- Low wages have a direct bearing on the disposable income of families and leave little room for the majority of households to have enough disposable income to purchase consumer durables or industrial products, affecting demand.

Research and development:

Low research and development expenditure at 0.8% of **GDP**, *vis-à-vis* higher value for other fast emerging economies such as South Korea (4.5%), China (2.1%) and Taiwan (3.3%), is resulting in lower capacity for innovation in technologies and reduced ‘technology readiness’, especially for manufacturing.

Labour productivity:

- The lack of HRC and low technology readiness have impacted labour productivity adversely.
- In India, labour productivity in manufacturing is less than 10% of the advanced economies including Germany and South Korea, and is about 40% of China, as reflected in a World Bank publication of 2018, *The Future of Manufacturing-Led Development*.
- Low productivity has unfavourable consequences for competitiveness, manufacturing growth, exports and economic growth.

Fundamental deficiencies:

- Due to a lack of capital expenditure and institutional capacity, and inefficiency in business service processes, there are difficulties in acquiring land for businesses, in efficient utilisation of economic infrastructure, and in providing business services, leading to a long time and more cost in setting up enterprises, resulting in a loss of creative energy of entrepreneurs.
- For years, the economy has been hit internally due to low consumer demand as a result of low household incomes as well as externally on account of lesser competitiveness and inadequacies in integration with global supply chains for trade.
- A Business as Usual (BAU) approach is resulting in diminishing returns.

Paradigm shift:

- In order to drive the economy, there needs to be fresh thinking to address the underlying issues comprehensively in an integrated manner.
- The new reforms approach should be systemic and address structural issues — HRC, skills, **research and development** (R&D), land management and institutional capacity.
- The focus should be on quality of business services, technology readiness, labour productivity and per capita income.

Structural changes required:

- To attract large investment in manufacturing and advanced services, at a basic level, investment in human capital and technology is a prerequisite.
- Raise HRC by way of enhanced public sector outlay to 8% of GDP, from current about 5%, for education, skill development (including for advanced technologies) and public health.
- The reports (by McKinsey and the World Economic Forum) on advanced manufacturing suggest that Industry 4.0 will be defined by new technologies such as robotics, 3-D printing, artificial intelligence (AI), the Internet of things (IoT), etc.
- These technologies could usher in rapid changes of a higher order up to 10X or more in speed, scale and scope; technology obsolescence will be much faster than ever before.
- Consequently, efforts for technology readiness are very essential to stay competitive. It demands enhancing public research and development expenditure to 2% of GDP over the next three years.

Concerted calibrated approach:

- There is a need to work on strategies to enhance per capita income by more wages for workers through higher skills and enhancing minimum wages, besides improving the social security net.

- This calls for a concerted calibrated approach through collaborative efforts of government, industry and workers' unions.
- On the issue of increased cost of labour, it can be compensated by higher productivity, some tax-benefits in the initial period of wage reforms especially for Micro, Small and Medium Enterprises, besides reducing transaction costs in business and improving infrastructure utilisation efficiency.

Systemic approach:

- Using insights from the work of Nobel laureate (1993) Douglass C. North on the role of institutions in advancing the economy in a country, it is necessary to build the capacity of public institutions to create a good environment for business and industry.
- Policy reforms should lay an emphasis on process innovation and promote a business-centric approach to implementing pre-determined service quality levels (SQLs).
- It is also required to create a friendly ecosystem by having a state-of-the-art plug-and-play model for new enterprises, and for efficient internal supply chain management to integrate with the global supply chain**.**

Innovative policymaking:

- Apart from rapid globalisation and rising aspirations, the future of the economy should be particularly viewed in the backdrop of a significant and irreversible shift in terms of a reliance on the global supply chain
- This is the result of the knowledge-intensive nature of businesses and exponential effects caused by advanced technologies under Industry 4.0, since the 2010s.
- Therefore, the strategies adopted since the 1990s till now may not ensure adequate returns, and call for innovative approaches in public policymaking.

Conclusion:

It is necessary to have a systemic approach for policy reforms for setting the economic fundamentals right, in order to unlock creativity and innovation in the economic system, raise the total factor productivity (TFP), or a measure of productive efficiency, and to achieve higher growth.