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The Study of Challenges and Opportunities to Sustained Indian Economic Growth

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Abstract

India today can best be described as a restless nation, with calls for change coming from almost every corner of society. India is a young country; nearly 65% of its population is younger than 35. After independence in 1947, India followed inward-looking and state-interventionist policies that shackled the economy through regulations, and severely restricted trade and economic freedom. The result was decades of low growth, pejoratively termed the 'Hindu rate of growth'. Reforms beginning in 1991 gradually removed obstacles to economic freedom, and India has begun to play catch-up, steadily re-integrating into the global economy. The imminent shift in land from agriculture to urban use and industry constitutes another source of potential productivity gain. The success of the IT industry in India has had a material impact on productivity. Emergence of new technologies, especially mobile, in India has sparked social change that's difficult to quantify. Mobile, Internet, and social media penetration and growth can be quantified, but describing the changes in social values and lifestyles that have accompanied those trends is far more challenging. In any society, economic growth without shared prosperity ultimately spawns instability. In India today, people who feel left out of the nation's recent growth are actively seeking inclusion. At the same time, those who have been empowered by India's economic revolution are demanding fast and sustainable reform. Each sector of the Indian economy will need to execute solutions drawn from all three categories if India is to build its GDP and improve its HDI in an environmentally sustainable manner.

Keywords: Economic Growth, Economic Freedom, Sustainable Reform, GDP, HDI, India's Economic Revolution.

Introduction

In its seventh decade of independence, India stands on the cusp of major change: a transformation that could lead to unprecedented economic growth paired with radical improvements in the nation's Human Development Index (HDI). Each sector of the Indian economy will need to execute solutions drawn from all three categories if India is to build its GDP and improve its HDI in an environmentally sustainable manner. To foster the emergence of such world-class Indian companies, India's private sector will have to invest more in research and development (R&D), particularly for solutions to challenges facing emerging markets, where India has already established a leadership position. To drive rapid growth, Indian companies will need to align their top management and board to make everyone accountable for growth, embed integrity into their organizational culture, and uphold sustainability and social impact as core values of the organization. As information grows (in both access and volume) and Indian consumers and businesses are more able to apply this information in their decision making, they become more empowered. And with their increased empowerment, they will demand ever more value from the products and services they buy—including greater quality and convenience. Companies will need to rethink their business models and competitive strategies to profitably serve these customers. Like large, established corporations in India, entrepreneurial companies in India can play a critical role in developing and deploying Winning Leap solutions. Indeed, the large Indian companies of tomorrow will emerge from the entrepreneurial sector of today. A groundswell of entrepreneurial energy in India has sparked recent, well-publicized successes in the e-commerce sector alone. An additional benefit of improving ease of doing business in India could take the form of greater confidence in India on the part of multinational companies, which would translate into larger flows of foreign direct investment and know-how into India, two essential ingredients for growth and innovation. International and domestic news media are rife with critiques and warnings about India squandering its extraordinary potential because of an outdated sociopolitical system, and India's citizens are exerting increasing pressure for institutional reforms.

Objectives of the Study

1. To identify the opportunities to sustained Indian economic growth.
2. To identify the challenges for Indian economic growth.

Challenges for Indian Economic Growth

Improve Governance

India's governance problems overarch all its other problems. Without better governance, delivery systems and effective implementation, India will find it difficult to educate its citizens, build infrastructure, increase agricultural productivity, and ensure that the fruits of economic growth are well-distributed. Governance problems stem from the increasing inability of the government and public institutions to deliver public services in the face of rising expectations.

Raise Basic Educational Achievement

It is the case that India has a large number of highly educated people. But it has a population of 1.2bn and probably the highest absolute numbers anywhere globally receiving hardly any education.

Control Inflation

For a nation that is rightly proud of its democracy and has a history of reasonable stability in terms of inflation, inflation should be more defined and credible medium-term framework for macroeconomic stability. India is a very diverse nation, whose population shares a love for democracy. It would be a powerful signal for its 1.2bn people to know that macro-economic stability for the RBI is dominated by the goal of keeping inflation low and stable.

Liberalize Financial Markets

India's financial sector remains small and underdeveloped. The state still dominates the sector, holding 70% of banking assets, a majority of insurance funds and the entire pension sector. Additionally, markets are lacking in corporate debt, currency and derivatives. This leads to a lack of credit and low financial savings. To meet its growth potential, India needs to pursue financial reforms to channel savings effectively into investment, meet funding requirements for infrastructure and enhance financial stability. Savers need to have access to a broad range of financial instruments, while borrowers should be able to access local debt and equity.

Increase Trade With Neighbours

In the past decade or so, Indian trade with the rest of the world has ballooned. Lower tariff barriers encouraged by Indian authorities have been key, as has booming world trade. This impressive development needs to be kept in perspective, however, as it has come from an exceptionally low base. India currently accounts for no more than 1.5% of global trade. China is rising sharply, and China now ties with the US as India's biggest trading partner.

Increase Agricultural Productivity

Increasing agricultural growth is critical not only for India to sustain high growth rates, but also to move millions out of poverty. India's agricultural yields are a fraction of those of its more dynamic Asian neighbours. For instance, rice yields are a third of China's and half of Vietnam's. Agriculture will have to contend with two other problems. First, the loss of arable land for non-agricultural uses as India industrializes and urbanizes. Second, soil erosion due to intensive farming and environmental degradation. Since there are limits to enhancing area under cultivation, as forest cover is already dwindling, raising agricultural productivity will be key. It is widely acknowledged in policy circles that improving agricultural productivity is critical to sustain high growth and reduce poverty, and policies and implementation are the areas that need to see more progress.

Improve Infrastructure

India's constraints in infrastructure are obvious to first-time visitors or long-term residents. There are capacity constraints in managing and executing infrastructure, especially at the state level. At the state level, there is very little capacity for ownership and stewardship of infrastructure development in the municipal bodies. There is also a shortage of skilled engineers and technicians, which severely constrains rapid infra roll-out. Till very recently, the government dominated the infrastructure space, and private investment was negligible. Still, there are significant areas of infrastructure that are not open to private investment. User charges on water, road and power are not yet commensurate with marginal costs, as they are politically sensitive, thus impeding private investment. There are significant barriers to entry for firms, especially foreign firms, and FDI limits are still in place. Further, there are frequent changes in regulatory policy in all areas of infrastructure, including telecom, roads and power, which increase uncertainty and impede private investment.

Remove Regulatory Hurdles and Focus on Skills

For India to achieve its targets on the value-added-manufacturing vector, it needs to first remove regulatory hurdles that have made doing business in India difficult. That includes simplifying policies related to land, labour, and the environment and providing single window clearances for obtaining business permits.

Import Technology to Strengthen Manufacturing Capabilities

Importing foreign technology can help Indian manufacturers strengthen their capabilities. With the government's help, business can do so by increasing investment in research and development (R&D), with the goal of ultimately reducing dependence on technology imports.

Make Structural Shifts in Manufacturing

As Indian manufacturers shift their focus to high-tech industries, they will need to invest in R&D and develop new technological skills. Global giants like Toyota have invested heavily in R&D to reduce the lead time from design to production. For example, Toyota's central R&D labs have developed simulation models to predict the impact of noise, wind, and other factors on automobile frames and to use the resulting insights to design more robust frames. India needs to enhance such capabilities to "move the needle" toward value-added manufacturing.

The Opportunities to Sustained Indian Economic Growth

India Opens Up

With the onset of reforms in 1991, India began to unshackle its closed economy by gradually lowering its very high trade barriers and boosting exports. Average tariffs fell to below 15% from as high as 200% as the country began to re-integrate into the global economy. The impact of opening up has been significant. Exports have risen 14 times as India has rapidly gained trade share. This development has been most evident in the past three years, when trade has grown, on average, 25% a year. Increased openness has contributed significantly to increasing productivity: It provided domestic firms with access to superior inputs, ideas and technology. The increased competition from actual and perceived imports has focused domestic firms on the need to improve efficiency as critical to survival. It has rewarded the most efficient firms while penalizing the most inefficient domestic firms, thereby improving average productivity.

The Rise of the Financial Sector

India's financial sector is still relatively small compared with the size of its economy, as well as with those of its East Asian neighbours. Assuming that policies to open up the financial sector remain on track, including the entry of foreign banks starting from 2009, the expectation of financial deepening to continue and to contribute to increases in productivity in the medium term.

Evolution in Global Competitive Rank of India since 2007-08

Year	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	1013-14	2014-15	2015-16
Rank	48	50	49	51	56	59	60	71	55

Source: World Economic Forum

Back-Office to the World

The success of the IT industry in India has had a material impact on productivity. Apart from the direct productivity gains of the major IT firms, it has had spillover benefits through two channels: „It has provided powerful incentives for students to invest in IT skills. This has created a pool of technology-skilled labour that firms in other industries can tap into. It has had a demonstration effect on other domestic firms, leading them to ramp up their own technology spending, thereby boosting productivity. The rapid spread of mobile phones from a very low base provided a fillip to communications, further boosting productivity. Today, India is the fastest-growing market for mobile phones, with average growth rates of over 80% every year since 2000. India's technology spending is still low and there remains substantial scope for catch-up and productivity gains.

The Great Migration

Urbanization is spurred by both push and pull factors. Deteriorating agricultural productivity, caste barriers and unemployment in villages push rural inhabitants out, while better opportunities in cities, very high growth in the construction industry and demonstration effects from other migrants pull rural workers into urban centers. The implications for productivity growth are significant.

India's Growth Performance compare to Other Lower Middle- Income Countries (2014-15 to 2015-16)

Countries/ Sectors	**Education**	**Employment**	**Asset Building**	**Financial Intermediation**	**Corruption**	**Basic Services**	**Fiscal Transfers**
India	3.35	3.14	3.04	3.26	3.99	3.82	2.70
Indonesia	4.68	3.71	3.37	3.27	3.96	4.43	3.42
Lao PDR	2.94	4.60	3.12	3.36	3.97	3.54	3.24
Philippines	4.07	4.06	3.30	3,24	3.65	4.38	3.49
Thialand	5.21	4.17	3.62	4.28	3.47	5.03	3.56
Vietnam	4.68	4.70	4.05	2.75	4.12	4.38	3.39

Source: World Economic Forum.

The Land Factor

The imminent shift in land from agriculture to urban use and industry constitutes another source of potential productivity gain. Land is a critical input needed to keep the development process moving, allowing for the shift of people from the rural to the urban sector. Access to land is needed for factories and housing projects, and to create tens of millions of jobs in construction in the short run, as well as longer-term employment. When land moves from low productivity agriculture to urban use and higher productivity sectors, overall productivity improves. However, India will need investments in agriculture to boost productivity, especially in rural connectivity, storage, etc., to improve the yield of remaining agricultural land.

Productivity gains for the economy tend to be a cumulative process. Higher productivity leads to more confidence and increased openness, which means more technology and investment and sustained productivity growth. The building of highways will not only lower costs for companies but also enable rural-urban migration, the development of cities and the process of moving land from agriculture to industry and services. These in turn attract more investment through agglomeration effects, and thus sustain growth.

Rise of the Emerging Middle Class

When people change their purchase behaviour, the result is often nonlinear shifts in demand. The aggregate demand may look linear, but at an individual level, there are usually demand spikes that are difficult to explain. For instance, a consumer who typically travels using low-cost options may inexplicably buy an expensive TV with many fancy features or demand high-end facilities from his or her educational institution. Such consumers' numbers are growing rapidly in India. And they could ultimately become one of the largest voices for change in the nation, owing to their aggregate economic power and their informed, discerning nature.

Conclusion

With the onset of reforms in 1991, India began to unshackle its closed economy by gradually lowering its very high trade barriers and boosting exports. For India to achieve its targets on the value-added-manufacturing vector, it needs to first remove regulatory hurdles that have made doing business in India difficult. Importing foreign technology can help Indian manufacturers strengthen their capabilities. With the government's help, business can do so by increasing investment in research and development (R&D), with the goal of ultimately reducing dependence on technology imports. As Indian manufacturers shift their focus to high-tech industries, they will need to invest in R&D and develop new technological skills. The imminent shift in land from agriculture to urban use and industry constitutes another source of potential productivity gain. Till very recently, the government dominated the infrastructure space, and private investment was negligible. Still, there are significant areas of infrastructure that are not open to private investment. User charges on water, road and power are not yet commensurate with marginal costs, as they are politically sensitive, thus impeding private investment. There are significant barriers to entry for firms, especially foreign firms, and FDI limits are still in place. Further, there are frequent changes in regulatory policy in all areas of infrastructure, including telecom, roads and power, which increase uncertainty and impede private investment.

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