# "Make in India" Push-Crucial Lessons from History

Athreya Mukunthan and Omkar Raut

***Abstract*—*"Trickle-down" effect* has been a long standing talking point in economic history. Economists like Jagdish Bhagwati and Amartya Sen have had enormous arguments on the same topic through the literary medium. These and more of such debates instigated this paper, which attempts to investigate the effect of economic growth on the overall economy; most importantly the lower section of the income group. For achieving this objective, the paper delves into the evidences of the "Growth-Equity Trade-off" in two of the biggest Asian economies, China and India. Secondary data analysis on various macro indicators have been done to achieve the same. Both China's 1979 and India's 1991 reforms share common features in the sense – along with an increase in growth rates there has been an increase in inequality. With a lot of growth enhancing policies currently envisaged in India like the "Make in India" this paper seeks to identify the possible reasons for unequal growth in the past. After dwelling deep into the dynamics of economic transition during the reform period the paper goes onto recommend necessary policy interventions like skill development, strong competition policy, and a need for incentive to domestic small scale players which must be in place to ensure the benefits of the growth reach all sections of the society.**

***Index Terms*—Chinese growth story, Indian reforms, inclusive development, lessons from history, make in India, trickle-down effect.**

## I. Introduction

Simon Kuznets was an early proponent of the theory of "trickle down" in the 1950's, where he believed that inequality is said to rise initially with a rise in economic growth, but eventually it is said to fall and the economy is said to move towards a more equitable society. However, the evidences from the world and India have mixed responses to growth enhancing reforms. India in 1991 introduced a series of reforms in terms of Privatisation, Liberalisation and opened up their economy to the world. The results and impact of the reforms and its effect on inequality and poverty has been a mixed bag. Against this backdrop, the paper analyses the "Make in India" initiative of the Government in India, which aims at propelling the growth of the nation up. The paper explores the case of China, which in 1979 initiated a plethora of growth enhancing reforms and India which in 1991 opened its economy to the world and aimed at pushing the growth numbers high. What were the impacts on all sections of the society after reforms? Has growth been inclusive? The paper seeks an answer to these questions and aims at extracting crucial lessons from the same.

Manuscript received January 11, 2016; revised March 14, 2016.

Athreya Mukunthan is with the Public Affairs Centre, Bangalore, India (e-mail: athreya91@gmail.com).

## II. The Growth Equity Trade off-Evidences from the World

China in 1979-80 had initiated a series of market reforms, and envisaged an industry led growth path [1]. As a result they have grown at an average growth rate of 10% over the last 3 decades[1]. India on the other hand liberalised in economy in 1991, brought in a series of reforms which aided privatisation and wanted to be part of the global village, whose policy till then was only inward looking [2]. All the reforms are seen to have good results in terms of more investment, more trade and therefore more growth in all the cases [3]. However, one burning question that needs to be answered is that all this growth has come at what cost? Rather who's cost? Has this growth trickled down to the poor or has it made only the rich richer, are few questions we would explore

### A. China

The following graph tracks the movement of the Gini Coefficient of China post the economic reforms in 1979.

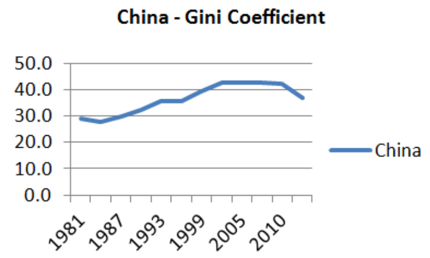


Fig. 1. China-Dini coefficient.

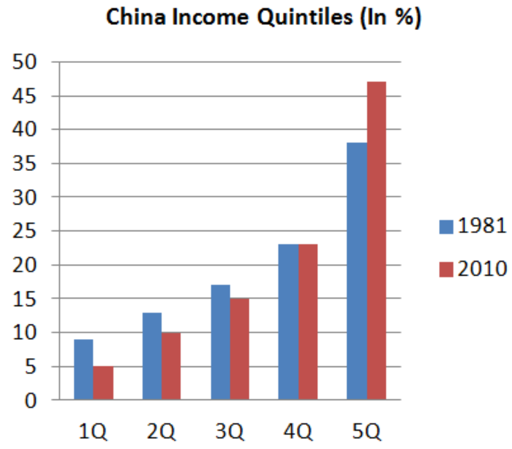


Fig. 2. China income quintiles(In %).

We can clearly see in the above graph that since the growth enhancing reforms have been initiated in China the

[1] China's Economic Rise: History, Trends, Challenges, and Implications for the United States, Wayne M. Morrison, Congressional Research Service, August 21, 2014.

Gini shows a constant increase from 29.1 in 1981 to 42.6 after two decades. However, the shape of the curve is hinting at an Inverted "U" shaped curve off late, wherein the inequality is decreasing. It is also important for us to see the income share held by every section of the society to see who has benefitted from the growth. The graph below depicts the same.

As the above figure clearly shows, after reforms in China the highest quintile which consists of the top 20% income holders have gradually become richer, while the lowest 20% have become poorer. The income share of the lowest 20% has declined from 9% in 1981 to 5% in 2010, which is evident from the above figure. Quintiles 2 & 3 have also shrunk in terms of income held over the years. All the above analysis is clearly indicative of the fact that though China has grown at a tremendous rate, the bottom quintiles have not managed to benefit out of this.

### B. India

Indian growth equity trade-off has been a highly debated issue over the years. The problems in data add fuel to fire. Income data in India is not collected by NSSO; rather it collates consumption expenditure data every 5 years. World Bank gives an income inequality data, which is again highly criticized for its methodology. Therefore we explore the World Bank Income based Gini coefficient data and also the NSSO data.

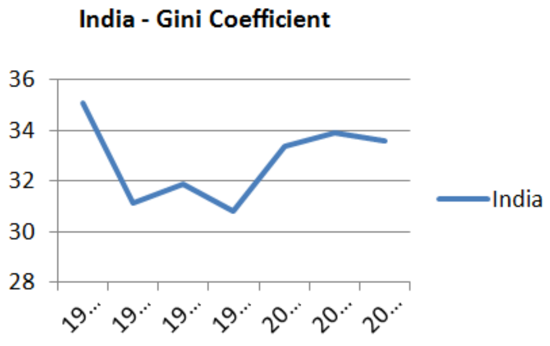


Fig. 3. India- Gini coefficient.

As the above World Bank Gini coefficient depicts, the inequality which seemed to have decreased marginally after the 1991 reforms, has continuously risen after 1994. The shape of the Gini Coefficient curve is showing signs of inverted "U" as propounded by Kuznets. Since income data in India is said to be ambiguous, we move to NSSO data set based on consumption expenditure.

TABLE I: SOURCE: DUBEY AND THORAT (2012)

| Year | Gini(Nominal) | Gini(Real) |
|---|---|---|
| 1983 | 0.33 | - |
| 1993-04 | 0.326 | 0.2844 |
| 2004-05 | 0.363 | 0.2997 |
| 2009-10 | 0.37 | 0.3059 |

Sarkar and Mehta (2011) have used the wage data in NSSO to compute the Gini coefficient based on the NSSO.

A point to be noted in the both the tables is that the 1999 round of NSSO has not been included in as the methodology in that round was different and therefore making a comparison not possible.

In a nut shell, it is clearly seen that post reforms inequality in India has increased to a large extent. In fact in some of the data it is seen that pre reforms the inequality showed signs of falling also. We move onto the quintile based analysis for India pre and post reforms.

TABLE II: SOURCE-SARKAR AND MEHTA (2011)

| Year | Gini |
|---|---|
| 1983-84 | 0.337 |
| 1993-94 | 0.347 |
| 2004-05 | 0.376 |

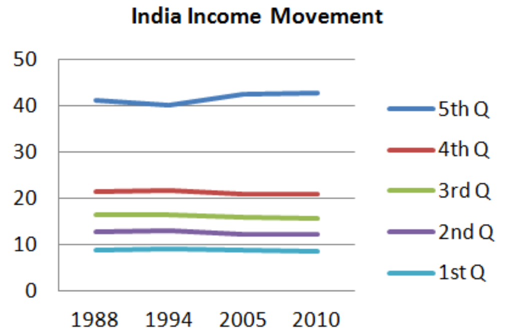


Fig. 4. India income movement.

The above graph supports the inequality data of table 2&3, showing that it is the richer class who have benefited from the reforms. Though there is a certain ambiguity in the data in calculating inequality in India, there is considerable evidence from all the above tables and graphs that the growth benefits does not seem to have trickled down to the very bottom of the Indian Pyramid. The possible causes and the way ahead is discussed in the next section.

## III. INDIA'S EXPERIENCE WITH ECONOMIC REFORMS

The cases preceding this section were evident enough to portray a negative effect of growth on income equality. This has been consistent even with India's economic reforms. This proves that the reforms did lack the 'inclusive' component and one of the primary reasons for the structural change in reforms after the experience of the Asian Crisis. There have been many reasons in the favour of the economic reforms in India, but there have been loopholes which have led to the increase in inequality seen in the current context of Indian economy.

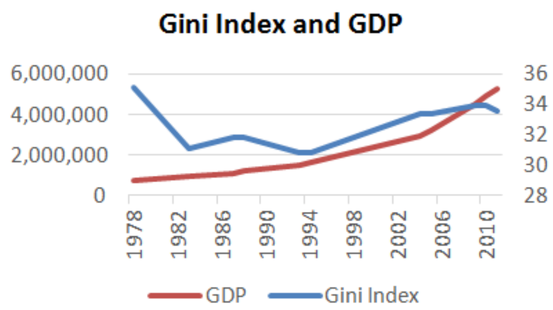


Fig. 5. Gini index and GDP.

The graph above clearly shows the increasing inequality after the reforms were implemented in India. The Gini India has been consistently increasing over the years suggesting that the "Trickle-down" effect has failed to materialize in India. On the other hand, GDP has been consistently rising after the implementation of reforms. Till 2004, Gini Index was moving together with GDP. However, there are signs that the Gini Index is coming down and 2010 has been a testament to the fact that Gini Index is showing signs of decrement while GDP is continuing to rise. This is in line with Simon Kuznets's argument of the inverted "U" theory. This implies that an increasing number of people are slowly reaping the benefits of the growth in the economy.

The initial response to the reforms was impressive looking at an annual GDP growth, which averaged 6.7 percent in the first half of the reform period (1992-97)[2] [4]. However, in the second half of the reform period (1998-2003), the growth rate decelerated to an average of about 5.7 percent. Thus, it invoked serious concern about the longevity of the impact of the reforms. The deceleration can also be however linked to two global factors – global economic growth slowed down in the wake of the East Asian crisis and the collapse of the technology boom in the United States. The second factor is the weakening in the pace of reforms.

The description of the reforms till now suggests that India's results from the reforms have not been as expected [5]. However, India's experience has been that the pace of reforms has been dictated by the economic and political forces, which cannot be forced beyond a certain point. India has a highly pluralist and participatory democracy, which made infusion of reforms a gradual process.

Another experience of India's economic reforms has been the special challenges posed when attempting second generation reforms, which are much more complex. This was evident in India's attempt at bringing private participation in infrastructure building like electricity generation and distribution, telecommunications, and roads.

Reforms have a chain reaction of their own. Sometimes, reforms in a certain sector are necessary to be successful for a careful implementation in another sector. Hence, for successful reforms, successful sequencing is required. This aspect is even more vital looking at the gradual way of reforms being implemented in India because huge lags reduce the effectiveness of certain reforms. Indian policy toward sequencing got it right in some areas like liberalization of the capital account, but failed miserably in others like reserving many areas for the non-performing small scale industries. Many countries had liberalized capital flows before developing a strong financial sector, and suffered as a result. India avoided this problem. It had traditionally followed restrictive policies toward external debt. The government never borrowed abroad, and commercial organizations could not incur external debt without government permission—and the government was very restrictive in granting such permission.

The role of government is also important while implementing reforms. Earlier, the Central government had a control over private players and provided access to the resources according to the holistic needs. However, in a liberalized environment, resources will flow to states where conditions are considered most favourable for investment. This tendency was heightened by the fact that state governments responded very differently to liberalization. More enlightened states adopted investor-friendly policies, trying to attract both domestic and foreign investors. Less enlightened states were ignorant about this fact and lagged behind the competition from other states. So, while India as a whole experienced faster growth, many states saw a deceleration. This was not because the central government followed a discriminatory policy, but it was because states responded differently to the reforms leading to higher inequality among them. This generated pressure on the central government to adopt a more proactive approach to ensure a more egalitarian process. It started to provide more funds to slow-growing states, but the resources were not sufficient. Moreover, there was an ambiguity over the conditions of the funds provided to the states.

India's experience in reforms also provides a useful insight on solutions regarding poverty alleviation. It shows that growth is good for poverty alleviation. Poverty did not decline in 1970s, but it decreased when growth increased in 1980s and 1990s. Even independent international experts like Angus Deaton concluded that poverty declined during 1980s and 1990s and the decline was greater in 1990s. The debate in India is about the reliance on growth for reduction in poverty or reliance on anti-poverty measures for poverty reduction. India has used both strategies. India has relied on growth and given more emphasis on income generation in agriculture. However, the growth in agriculture lost its momentum in the second half of the 1990s, and hence the dissatisfaction with the equity aspect of the reforms. The anti-poverty programs are in action, but limited in scope. Pro-poor growth helps in alleviation of poverty, but sensitive sectors like agriculture have to be focussed into for better results at the macro level [6].

Though successful in poverty reduction, the reforms were unsuccessful in decreasing the inequality in the society. Further it has been observed that it has aggravated the inequality.

Given the bitter experience with the 1$^{st}$ leg of reforms in 1991 with respect to inequality, a sequel in the form of "Make in India" initiative was brought about on 25$^{th}$ September 2014 by the Prime Minister. It is said to be the next generation initiative to enhance the infrastructure in India and to rebrand India in the global manufacturing arena.

## IV. "Make in India" Initiative

"Make in India" is an international marketing campaign slogan coined by the Prime Minister of India, Narendra Modi.

Concentrating on the international trade sector, this initiative will minimize the imports of such products into the country thereby reducing the pressure on the trade deficit. On the export side, it will augment and diversify the exports from the manufacturing sector. It will also bring in latest technology into the country combined with reduced trade restrictions with many countries. The focus on world-class domestic manufacturing may also be the best way to

[2] Ministry of Statistics and Programme Implementation (MOSPI)

cope with globalisation and accrue maximum benefits out of it. The size of the domestic market in India with a skilled manpower at lower wages can be leveraged for inducing foreign investors to make India their manufacturing hub in their operations [7].

The "rub-off effect" is one more major plus point, the Make in India initiative is expected generate. It is often witnessed that when domestic players co-exist with foreign players, they gain in terms of knowledge, technological know-how and better and efficient techniques for production. This in turn paves way for domestic producers to compete in the global market in key sectors.

## V. Criticism of "Make in India"

Re-entry of black money through Foreign Direct Investment (FDI) has been a worry since India started attracting FDI after liberalization. The infamous Mauritius route has been used by many MNCs to avoid taxes and also by many High Net-worth Individuals and firms to bring in the black money legally. Therefore, laws regarding the scrutiny of funds coming into India have to be graduated to the next level for better usage and application of "Make in India" initiative.

Also, building on the Infant Industry Theory, there is a thin line between where the support should end and the firms should be exposed to international competition. Currently, many Small & Medium Enterprises (SMEs) in India are still a loss-making area. They have not reached the global competitive level of firms. Therefore, inflow of foreign competition through FDI would adversely affect the SMEs leading to even shutdown of indigenous firms and creating unemployment.

## VI. Conclusion — Lessons from the past and Way Forward

In both the cases we have examined in this paper (China 1979, India 1991) inequality has increased along with growth enhancing reforms. However it is also seen that in the long run the inequality shows signs of decrease and moves slowly towards the inverted "U" framework. This has taken about two and a half decades in China while it has taken about two decades in India. In today's economic condition and increasing aspiration among the all sections in the society is it feasible to wait for such a long time? One recalls the golden words of John Maynard Keynes "In the long run, we are all dead". Therefore we put forth few policy suggestions to make this Make in India more inclusive wherein all sections of the society can reap benefits out of the same.

The idea of large scale job creation would materialise only if the labour force are equipped with adequate skill sets. Therefore there is an urgent need to develop policies in those lines. It is to be noted that the current Government has already initiated a National Skill Development Programme in the country. It should be ensured that this reaches all sections of the society and there is holistic development of skill sets across the nation. With increasing skill sets, job creation in the lower strata would be better in the long run.

It must also be ensured that the local industries are not adversely affected by the foreign competition. Therefore a possible solution would be to hike the local content requirement in production of foreign firms. Also, tax breaks and incentives could be increased for domestic industries. However the WTO norms should be kept in mind while doing the same.

It is a given that the SMEs in India still suffer from issues like lack of credit, access to technology, limited capital, unavailability of adequate services such as electricity, water and labour. Therefore small industries need to be protected from the highly evolved foreign firms. This could be in the form of tax breaks, cheaper land, cheaper services from Government and availability of timely credit.

Indian manufacturing sector has to move on from the negative aspects of production like ownership and control, enterprise-specific performance requirements, which constraint decision-making. Rather, the focus of the foreign investment policy in India should be on the positive aspects of the efficiency of the production of goods in India with the new technology available in hand. It would lead to higher productivity for the firms at micro level and nation at the macro level.

India also requires a strong Competition Policy before embarking on such an adventurous initiative. The huge MNCs can collude and control the whole share of the Indian market. This would lead to unfair practice and exploitation of consumers. It would spoil the entire objective of competition and welfare enhancement of consumers.

## References


[1] W. M. Morrison, "China's economic rise: History, trends, challenges, and implications for the United states," *Congressional Research Service*, 2014.

[2] S. Yao, "Economic growth, income inequality and poverty in china under economic reforms," *The Journal of Development Studies*, vol. 35, no. 6, 1999.

[3] X. Zhu, "Understanding china's growth: Past, present, and future," *Journal of Economic Perspectives*, vol. 26, no. 4, pp. 103-124, 2012.

[4] A. Panagariya, *India in the 1980s and 1990s: A Triumph of Reforms*, International Monetary Fund, 2004.

[5] M. Agarwal and J. Whalley, *China and India: Reforms and the Response: How Differently Have the Economies Behaved*, Cambridge, Massachusetts: National Bureau of Economic Research, 2013.

[6] K. Deininger, S. Jin, and H. K. Nagarajan, *Land Reforms, Poverty Reduction, and Economic Growth: Evidence from India*, The World Bank, 2007.

[7] G. Bhagowaty, *How can the New Government Make India a Global Manufacturing Hub?* CRISIL.



**Athreya Mukunthan**, a programme officer in the Public Policy Research Group graduated in commerce from Chennai, after which he pursued masters in Economics from Symbiosis International University, Pune. While in college he was awarded the outstanding student of the year for two consecutive years (2014, 2015). He has worked with the Confederation of Indian Industry (South) as a research intern on a project for identifying the infrastructural gaps in industrial parks in Chennai, India. He has also worked in the Tamil Nadu Planning Commission as an intern on a project titled "A Review of the MSME Sector in Tamil Nadu". He has been part of a recent study submitted to GRIDCO (Electricity wing of Government of Orissa), which aimed at forecasting the monthly and quarterly power demand of all states in India for 5 years. His research interests lie in Development Economics, Growth-equity Trade off and Macro Issues on which he has published research papers in many national seminars across the country. Athreya has represented Tamil Nadu State Junior Cricket team for 2 years. His other interests include yoga, philosophy and poetry.

**Omkar Raut** is from Bangalore, India. His educational background is in economics with bachelors [B.Sc (economics)] and masters [M.Sc (economics)] from Symbiosis School of Economics, Pune, India in year 2013 and 2015 respectively.

He is currently employed as a research analyst in the Advanced Analytics and Consulting Department of Nielsen India Pvt Ltd in Bengaluru, India. In the past, he has been involved as a summer intern in NABARD (National Bank for Agriculture and Rural Development), where he worked on a project of Soybean Value Chain in India after an active on-field survey.

He was also involved in a Time Series Analysis & Forecasting Project under Prof Manasi Phadke. His other internships involve Value Notes Database Pvt Ltd as a Marketing Intern and in Trendy Investments as Research Intern. His paper on "India's Resurgence in the Global Economic Order" was selected for an International Economic Symposium in St. Petersburg State University, Russia. A paper of his related to Law and Economics, "An Account of Third Gender in India" was selected for the National Conference held in the Government Law College, Thrissur, India. Also, his paper on "E-health: The Way ahead" was selected for the LEAD symposium of Loyola College, Chennai, India under the theme of Health Economics and published in their book with ISBN 978-81-8286-025-4.