Economics beyond the Economists

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If inclusive growth and development are to be economically and politically sustainable, they cannot rely only upon ex post transfer measures. This is the fundamental error in conception that growth is to be followed by "redistribution". Inclusivity must be anchored in a productive process characterised by the wide distribution of productive capabilities and thereby of the fruits of growth. An exploration of the "growth vs distribution" debate.

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Recently, Jagdish Bhagwati and his collaborator Arvind Panagariya have accused Amartya Sen of showing insufficient regard for the importance of economic growth. Quite apart from the questions of individual intellectual responsibility that are involved, there are issues of public interest raised by the resulting debate.

Growth vs Redistribution

Bhagwati and Panagariya rightly note that there is little point in "redistribution" if there is little to distribute. A country with a low per capita income, such as India at Independence, could not readily escape mass poverty through redistribution alone, notwithstanding the presence of some notable concentrations of wealth. This is a reason why the attention of Indian planners in the early years of its development was squarely on how to achieve economic growth. It is another matter that their efforts achieved rather modest success. As Sen points out, he like other economists at the time, devoted a large share of his intellectual energies to elaborating the reasoning needed to identify the growth strategy appropriate for the country, contributing diverse ideas which were influential in associated debates, and even editing a volume with the title *Growth Economics*. Although there were sharply divided views on such matters as appropriate policies with respect to landownership, investment, regulation, and international trade, these cannot be characterised as involving differences as to whether or not growth was a desirable objective to pursue.

Bhagwati and Panagariya separately accuse Sen of not advocating pro-growth policies, i e, policies that actually promote growth, as opposed to having growth merely as their objective. However, it has never been self-evident what such policies are. It is possible to learn about the effectiveness of policies through experience, and indeed the policies that work better may vary from period to period. As Dani Rodrik and others have argued, the foundations of subsequent economic growth may have been put in place in the import substitution period, and indeed an acceleration of economic growth began in India in the mid-1980s, prior to the 1991 reforms. The combination of policies that have enabled China to achieve unprecedented levels of sustained economic growth does not fit any pre-existing formula and indeed is difficult even to characterise as a policy framework. Sen can hardly be faulted for not embracing the truth from on high as declared by Bhagwati and Panagariya. Bhagwati and Panagariya's favoured example of Gujarat does not prove the case for their favoured national-level economic policies, since there are diverse reasons for its relative success in promoting economic growth (including geographical and social factors), because the sub-national initiatives involved are more in the nature of pro-business actions by the state (such as high-level clearing of obstacles to project investment) than of pro-market economic policies as such, and because that success is less dramatic than they suggest. It is well known that in recent years Gujarat has had a lower growth rate than numerous other well performing Indian states. The elixir of growth can be, to a degree, mysterious.

Eat the Fruit before Growing It?

Sen recalls that in the early years of his advocacy of greater attention to the development of broad-based human capabilities, especially in the form of basic health and education, the eminent left-wing economist Joan Robinson accused him of advocating eating the fruit of the tree before growing the tree. This is an attack that has more recently been made by certain right-wing critics. However, even pro-market thinkers such as Milton Friedman – who, Sen points out, criticised the insufficient attention to investment in such capabilities in early Indian investment plans – and Theodore Shultz, the author of "human capital theory", emphasised its relevance for growth and development. There is little doubt that successful east Asian development experiences benefited from such investment, even if it was driven by private as well as public investment.

In the case of South Korea, for instance, prior land reforms enabled smallholders to invest in the education of their children, who later became the skilled and technical, managerial and professional workers of a transforming country, as widely recognised in systematic studies of Korean development. As Sen has pointed out, Korea had much higher literacy and school enrolment rates than did India at the onset of the former's rapid industrialisation and this was perhaps relevant in that subsequent trajectory. Although the initial social conditions may have been neither necessary nor sufficient for subsequent economic growth, they may well have played a conducive role, certainly in sustaining growth beyond the first stage centred on the absorption of relatively unskilled labour into the production of unsophisticated manufactures. To note this is hardly to be indifferent to growth, nor to suggest that the public sector must be the sole or even primary means through which improvements in human capabilities are realised, even if it is evident from historical experiences that it has a constructive role to play.

There is little doubt that the high level of literacy of Chinese workers today is a major reason for Chinese manufacturing prowess. A recent article in the *Financial Times* described how the same processes which are done by literate Chinese workers require an elaborate "workaround" system of matching patterns on punchcards when applied by illiterate workers in Indonesia. The demographic dividend of plummeting fertility rates associated with better survival rates of children and maternal education, even where household incomes are not as dramatically rising, is well known. Bangladesh provides a remarkable recent example as previously have Kerala and Tamil Nadu. There can be no guarantee that any investment pays for itself but this is as good a case as any – quite apart from the intrinsic value of access to good health, knowledge and public participation.

A Democratised Market Economy

The Government of India has rightly emphasised the concept of inclusive growth, even if it has been widely interpreted in an insufficiently demanding way. One of the virtues of this concept is that it is constituted of two parts, namely "inclusivity" and "growth". For inclusive growth to take place, growth must both occur and be sufficiently broadly realised. In particular, inclusivity of economic growth entails growth in incomes that is sufficiently broad-based to include diverse persons (ideally, the vast majority, including most especially poorer persons) distributed across regions and social groups. The growth process which has been taking place in India has certainly been unsatisfactory in this regard, given its unbalanced nature: the presence of a few limited zones of prosperity and dynamism alongside large sections of the population realising insufficient improvements in living standards and marked regional unevenness.

A strategy to bring about greater inclusivity must have many legs, combining measures to accelerate aggregate growth with inducements to regional development (including relevant infrastructural investments), broad-based investment in human capabilities to enable persons to take advantage of opportunities, efforts to bring about asset distribution (including through financial inclusion), and the development of intermediary organisations which can enable smallholders to thrive and to upgrade their activities in competitive conditions (dairy cooperatives such as Amul are one Indian example). Developing the rule of law and democratic character of institutions at all levels can also help to ensure that growth does not take the ultimately illusory "low road" form of illegitimate private appropriation and depletion of shared resources on which mass livelihoods and living conditions depend.

The role of social protection mechanisms such as the Mahatma Gandhi National Rural Employment Guarantee Scheme and the public distribution system, whatever the specifics of their design, is as a mere complement to such measures, which can together begin to constitute the framework of a more democratised market economy. Such an economy ought to create opportunities and empower persons to grasp them. Social protection is needed for those who do not have or cannot take advantage of such opportunities, and to directly promote human well-being to the extent that the society now has the required means, and market processes do not suffice. Such protections must, like all others, be designed carefully with a view towards their possibly complex effects, for instance on food and labour markets, which in turn influence human well-being, and their design should be periodically revisited with these effects in mind. Although considerations of state failure affect the viability of rights-based governmental programmes there is no reason for the comprehensively sceptical view that all such efforts must be thoroughgoing failures. It must be recognised that they are made necessary due to prior societal and market failures as well as that state failures can be addressed through various means. Indeed, corruption said to undermine anti-poverty programmes can also undermine the case for actions proposed by the self-proclaimed enthusiasts of growth, as evidenced by scandals that have accompanied the sale of resource extraction privileges or state assets. The lesson is not merely to focus governmental energies appropriately but to take measures to improve their effectiveness, which is today the focus of much greater attention.

Ultimately, if inclusive growth and development are to be economically and politically sustainable, they cannot rely only upon ex post transfer measures. This is the fundamental error in conception that growth is to be followed by "redistribution". Rather, inclusivity must be anchored in a productive process characterised by the wide distribution of productive capabilities and thereby of the fruits of growth. Where ex post redistribution is the perpetual object of fiscal attacks and tax revolts, inclusive distribution achieved in this way is linked not to the deployment of the exchequer but to the fabric of the productive economy. From a developmental perspective, an approach which anchors inclusion in the productive economy can lead to an ascending spiral of cumulative causation, as human beings, the "ultimate resource", show their ingenuity and productivity. By augmenting and diversifying demand and supply, they can create still more opportunities for others. Through their activities they can also bolster the revenues needed to engage in further growth-promoting investment and public activities of which they are beneficiaries as well as contributors.

Such an alternative requires breaking the chokehold on the imagination of the existing growth model based on expanding existing islands of prosperity, instead aiming to fill the ocean with such islands, until there is no distinction between land and sea. A productivist approach to inclusive growth and development bets on the weak, that they may become strong.

India in the Chinese Mirror

If enthusiasts of economic growth are not yet persuaded, they may be convinced by the fact that aspects of India's present macroeconomic difficulties, and in particular its persistent and widening current account deficit, are linked to its insufficiently inclusive pattern of economic growth. The burgeoning consumption demands of the rising middle class and wealthy are import-intensive whereas export revenues are realised disproportionately in activities concentrated in a few globally interlinked centres dependent on a limited and increasingly costly skill base and uncertain global demand in specific areas. The result has been current account deficits that are only at times compensated by foreign investment receipts. This has created a situation in which maintaining the confidence of foreign investors, in particular through policy changes which create sufficient inducement for new investment, has become all important, lest India experience the death spiral of a "sudden stop" in capital inflows, triggering asset price deflation and attendant knock-on consequences for financial stability and, once again, investor confidence. This is the sense in which the favourite metaphor of advocates of economic liberalisation on the existing pattern, that one must keep riding the bicycle of "reform" in order for it to stay up, is correct.

The result has been policy reforms (such as those relaxing foreign ownership limits and retail entry restrictions) that have been motivated by short-term exigency. The alternative approach, based on a more deliberate tilt towards widespread empowerment of individuals as producers and then as consumers, combining deliberately decentralised investment in people, productive enterprises and collaborative organisations with the disciplines of markets, would aim to create a more distributed production and export capability as well as ultimately a stronger basis for self-sustaining economic growth linked to domestic demand. As production for the world and the domestic market expands, productivity will improve and costs fall due to the resulting division of labour, economies of scale, learning and upgradation. This will make improvements in wages and living standards possible and in turn augment domestic demand.[1]

China has been following such a pattern, although in an unbalanced way. Having gone through a phase in which it has relied on labour-intensive manufacturing exports to create employment, build surpluses and improve its production system, it now faces the necessity to augment domestic demand by improving wages and living standards across its length and breadth.

Amartya Sen has insisted that growth is a means towards valuable human ends, not an end in itself. To this we can add the emphasis that inclusion is means as well as end.

NOTE

1 I am grateful to Vittorio Valli for his insights in this regard.