



Australian  
National  
University

**CRAWFORD  
SCHOOL**



## *Crawford School Dialogue*

# Asia's Economic Transformation: Implications for Australia

Presented by the Arndt-Corden Department of Economics and the Crawford School

Tuesday, 12 March, 2011

Weston Theatre, J G Crawford Building 132, Lennox Crossing, ANU

# India's Recent Economic Growth — A Review

*Ragbendra Jha, Australia South Asia Research Centre*

In 2010 India's GDP in PPP terms was \$3.92 trillion. By this India is the fourth largest economy in the world after the US, China and Japan.

In a decade India is expected to become the third largest economy. Between 2000–01 and 2007–08 India's real GDP growth averaged 7.3% per annum. Growth rates have recently been around 9% and, sometimes in excess of 9% except for the period since 2008–09. In that year GDP growth fell to 6.7% in the face of the GFC. GDP growth rate picked up the very next year when it was 8%. In 2010–11 real GDP growth is estimated to be 8.6% and in 2011–12 go back to 9% (Table 1). With a population growth rate of about 1.7% per annum (according to the latest Census of India (2011)) real GDP growth per capita has been in excess of 7% per annum for several years. At this rate real GDP per capita will double in about 10 years. Since the 1970s average annual decadal growth rates have gone up even as the standard deviation of year to year growth has gone down (Figure 1).

**Table 1: Rate of Growth of Real GDP at Factor Cost at 1999–2000 Prices (until 2008–09)  
and in 2004–05 Prices Thereafter (%)**

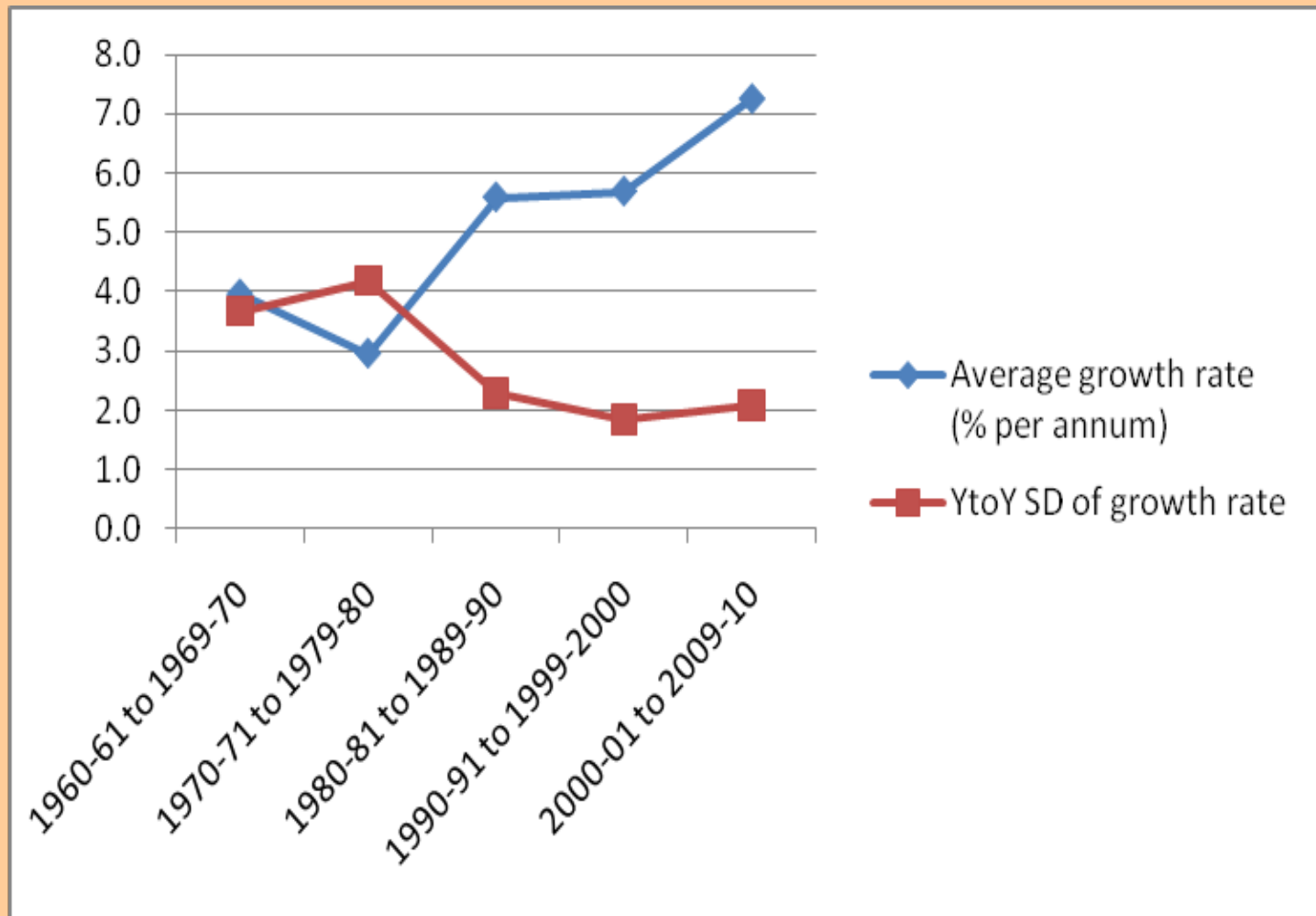
	2000–01 to 2007–08 average	2005–06	2006–07	2007–08	2008–09	2009–10	2010–11	2011–12*
Agriculture, Forestry & Fishing	2.9	5.2	3.7	4.7	1.6	0.4	5.4	3.0
Mining & Quarrying	4.9	1.3	8.7	3.9	1.6	6.9	6.2	7.5
Manufacturing	7.8	9.6	14.9	10.3	3.2	8.8	8.8	9.0
Electricity, Gas & Water Supply	4.8	6.6	10.0	8.5	3.9	6.4	5.1	7.0
Construction	10.6	12.4	10.6	10.0	5.9	7.0	8.0	10.5
Trade, Hotels & Restaurants	10.3 <sup>a</sup>	12.4	11.2	9.5	5.3	9.7	11.0	11.0
Transport, Storage & Communication		11.5	12.6	13.0	11.6			
Financing, Insurance, Real Estate & Business Services	8.8	12.8	14.5	13.2	10.1	9.2	10.6	10.5
Community, Social & Personal Services	5.8	7.6	2.6	6.7	13.9	11.8	5.7	8.8
GDP at Factor Cost	7.3	9.5	9.7	9.2	6.7	8.0	8.6	9.0

N.B. a = This refers to Trade, Hotels, Restaurants, Transport, Storage & Communication

Source: Economic Survey, Ministry of Finance, Government of India, 2009–10, 2010–11, Reserve Bank of India,

\*Source: Report of the Economic Advisory Council to the Prime Minister.

# Figure 1: Average Decadal Growth Rates and Standard Deviations of Year to Year Growth Rates



Source: Reserve Bank of India: Handbook of Statistics on the Indian Economy

# Structure of Economic Growth in India

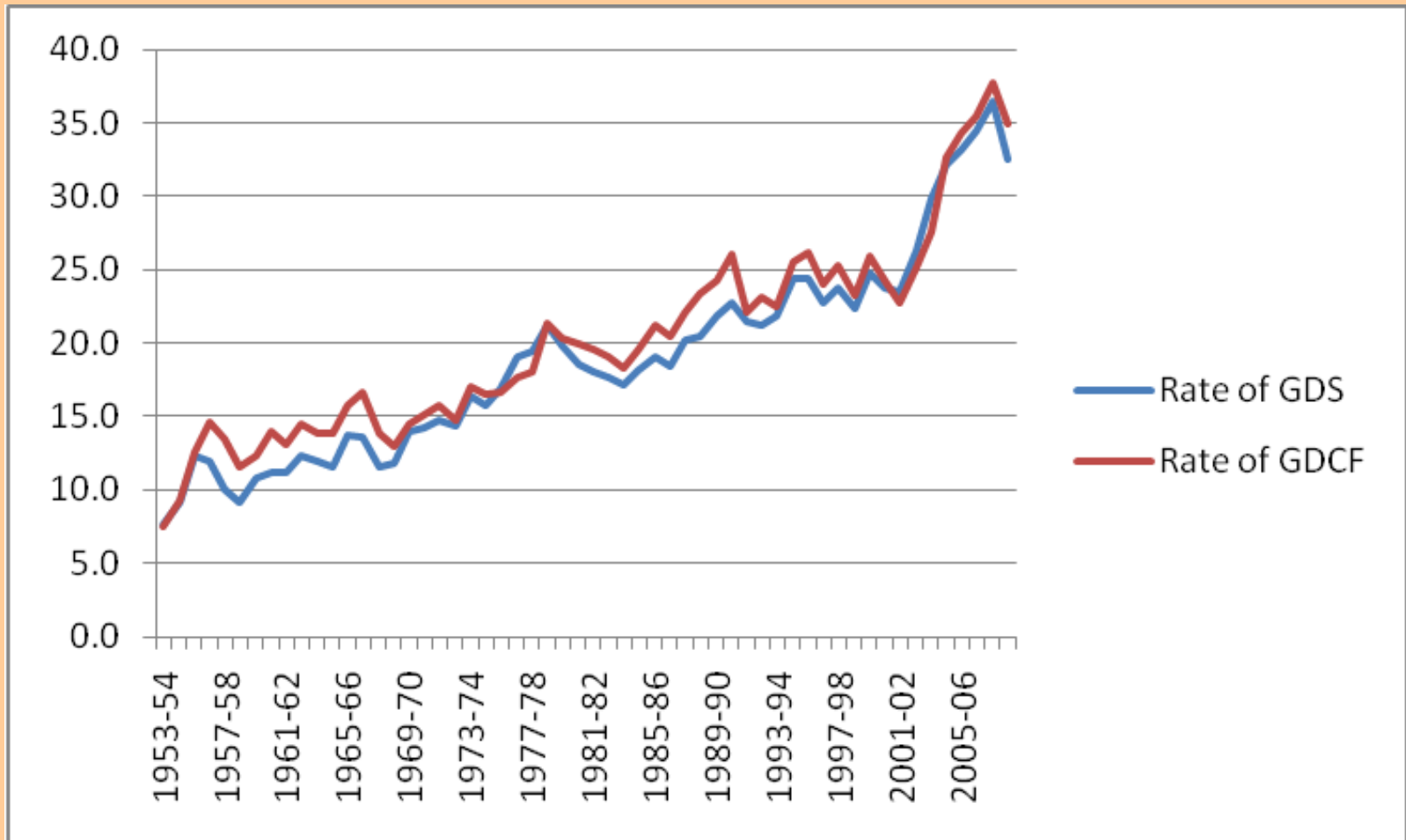
The structure of India's GDP has undergone immense transformation in the face of such rapid economic growth and has in, turn, contributed to it. During the decade 1961–70 agricultural value added as a percentage of GDP was 42.5%. Corresponding magnitudes for industry, manufacturing and services were, respectively, 20.3%, 14.3% and 37.2%. In 2008 agriculture contributed 17.6% of GDP whereas the contributions of industry, manufacturing, and services were respectively 29%, 16% and 53.4%, respectively. This is an indicator both of India's potential for further economic growth as well as that of a fundamental problem facing the Indian economy — how does one sector (agriculture) that contributes less than 18% of GDP support more than 60% of India's population? Within manufacturing India has increasingly specialized in higher value added manufacturing.

# Contributors to India's higher economic growth

In a growth accounting sense capital, labour and productivity growth have all contributed to enhanced rates of economic growth in India. Savings rates have gone up to about 34% and investment to about 36%, particularly since the 1990s, from very low levels in earlier decades (Figure 2). Growth is largely domestic consumption driven.

There is a very strong 'demographic dividend' as the median age of the Indian population hovers around 25, indicating that India is home to more than 600 million people below the age of 25. Further, this labor force is getting better trained (literacy rates have gone up to 74% in the 2011 census).

**Figure 2: Rates of Saving and Investment in India (percentage of GDP)**



Source: Reserve Bank of India: Handbook of Statistics on the Indian Economy

Total Factor Productivity in the production of aggregate GDP, and in the Manufacturing and Services Sector have each gone up, particularly post 1994. Agricultural productivity has not grown very fast. Openness to trade and investment went up sharply, particularly during the period 2002–07.

Even after the GFC India continued its policy of trade liberalization, with average manufacturing sector tariffs now down to 12% or less. No Indian bank failed during the GFC and stimulus is being rolled back. Fiscal situation is improving.

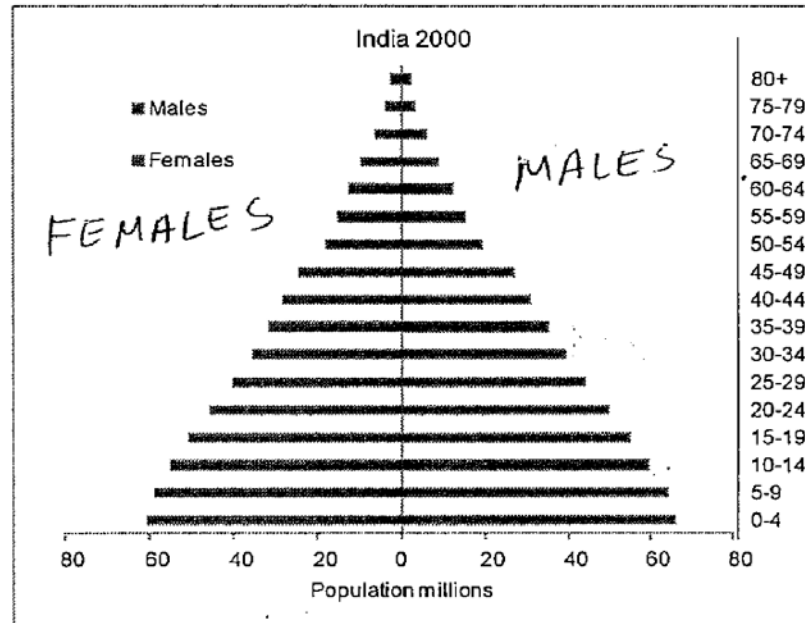
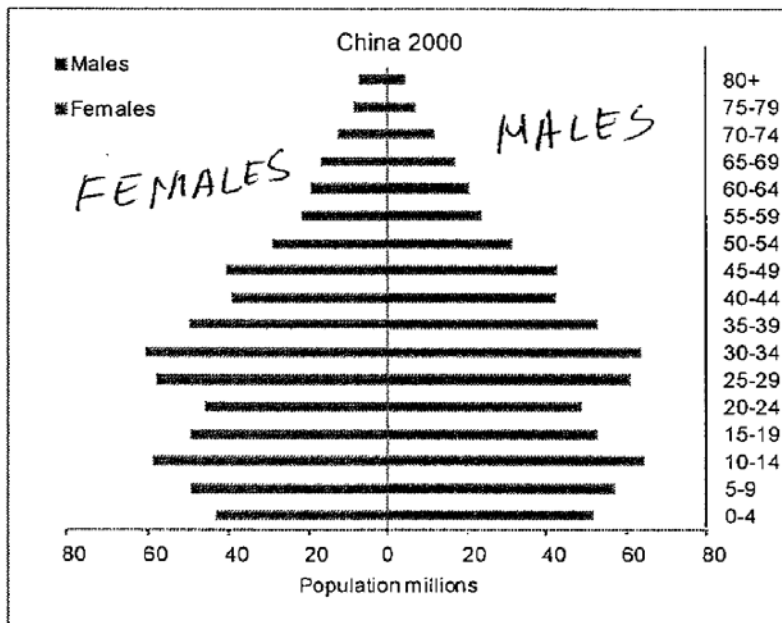
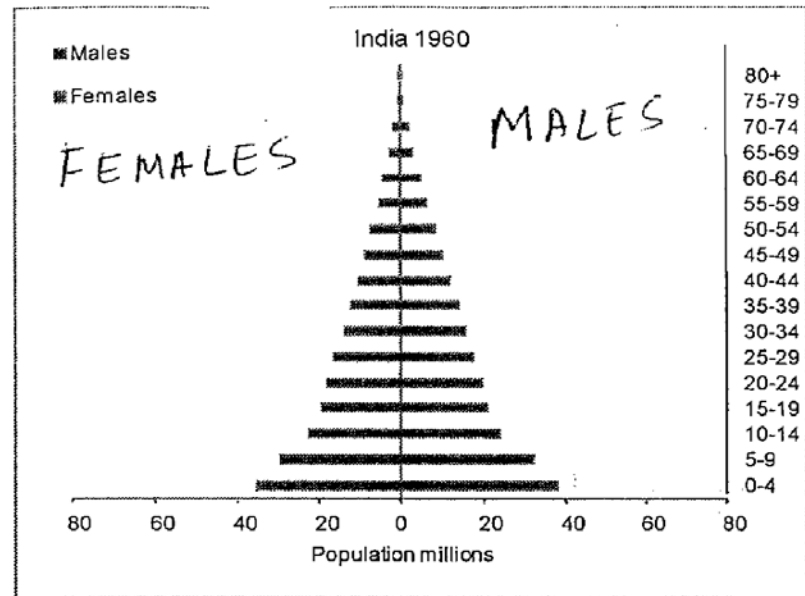
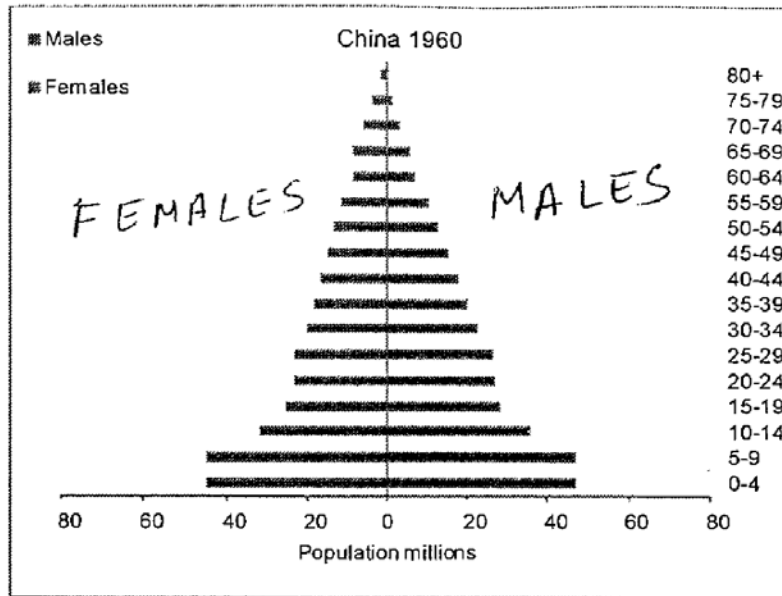
All these factors imply that economic growth rates in India will stay high and, given the increasing demographic dividend, may even accelerate.



My colleague, Creina Day, will speak more about the demographic dividend in her presentation. Suffice it to say here that the 2001–2011 period is the first decade — with exception of 1911–1921 — which has actually added lesser population compared to the previous decade. For the first time, there is a significant fall in the growth rate of population in the Empowered Action Group states (the relatively poor states of Uttar Pradesh, Bihar, Rajasthan, Uttarakhand, Jharkhand, Madhya Pradesh, Chhattisgarh and Orissa) after decades of stagnation.

Aiyar and Mody (2011) show that an increase in the working age ratio can raise the rate of economic growth, and hence confer a 'demographic dividend'. People of working age are on average more productive than those outside this age group. Also, because workers save while dependants do not, a bulge in the working age ratio contributes to higher savings rates, increasing the domestic resources available for productive investment. The literacy rate has gone up from 64.83% in 2001 to 74.04% in 2011 showing an increase of 9.21%.

**Figure 3: Population Pyramid in India and China, 1960 and 2000**



**Table 2: Sources of Economic Growth in India: Aggregate and by Major Sectors  
(% per year)**

<i>Aggregate Economy</i>							
				<i>Contribution of</i>			
<i>Period</i>	<i>Output</i>	<i>Employment</i>	<i>Output per worker</i>	<i>Physical capital</i>	<i>Land</i>	<i>Education</i>	<i>Factor productivity</i>
1978–04	5.4	2.0	3.3	1.3	0.0	0.4	1.6
1978–93	4.5	2.1	2.4	1.0	-0.1	0.3	1.1
1993–04	6.5	1.9	4.6	1.8	0.0	0.4	2.3
<i>Agriculture</i>							
1978–04	2.5	1.1	1.4	0.4	-0.1	0.3	0.8
1978–93	2.7	1.4	1.3	0.2	-0.1	0.2	1.0
1993–04	2.2	0.7	1.5	0.7	-0.1	0.3	0.5
<i>Industry</i>							
1978–04	5.9	3.4	2.5	1.5		0.3	0.6
1978–93	5.4	3.3	2.1	1.4		0.4	0.3
1993–04	6.7	3.6	3.1	1.7		0.3	1.1
<i>Services</i>							
1978–04	7.2	3.8	3.5	0.6		0.4	2.4
1978–93	5.9	3.8	2.1	0.3		0.4	1.4
1993–04	9.1	3.7	5.4	1.1		0.4	3.9

Source: Bosworth and Collins (2007)

# **Economic Growth and Poverty Alleviation in India**

High rates of economic growth in India imply that there has been substantial poverty reduction. But the elasticity of poverty reduction with respect to economic growth is lower in India than in many Asian countries, essentially because of the structure of economic growth. (My colleague, Peter Warr, will talk more about this in his presentation.)

This implies that inequality (both personal as well as spatial) has increased, particularly of incomes (as opposed to consumption where inequality is lower), but is still well below that in many emerging economies.

**Table 3: Economic Growth and Poverty Reduction in Select Asian Countries (1995–2005)**

Country	Average annual growth of per capita GDP	Annual rate of poverty reduction (PPP \$0.75 a day ultra poverty line)	Ratio of annual rate of poverty reduction to annual per capita GDP growth rate
<b>India</b>	<b>4.9%</b>	<b>-2.6%</b>	<b>-0.5</b>
Bangladesh	3.7%	-3.9%	-1.1
Sri Lanka	3.4%	-10.3%	-3.1
Viet Nam	6.2%	-13.5%	-2.2

*Source: IFPRI 2010*

**Table 4: Comparable Estimates of Poverty and Inequality — All India**

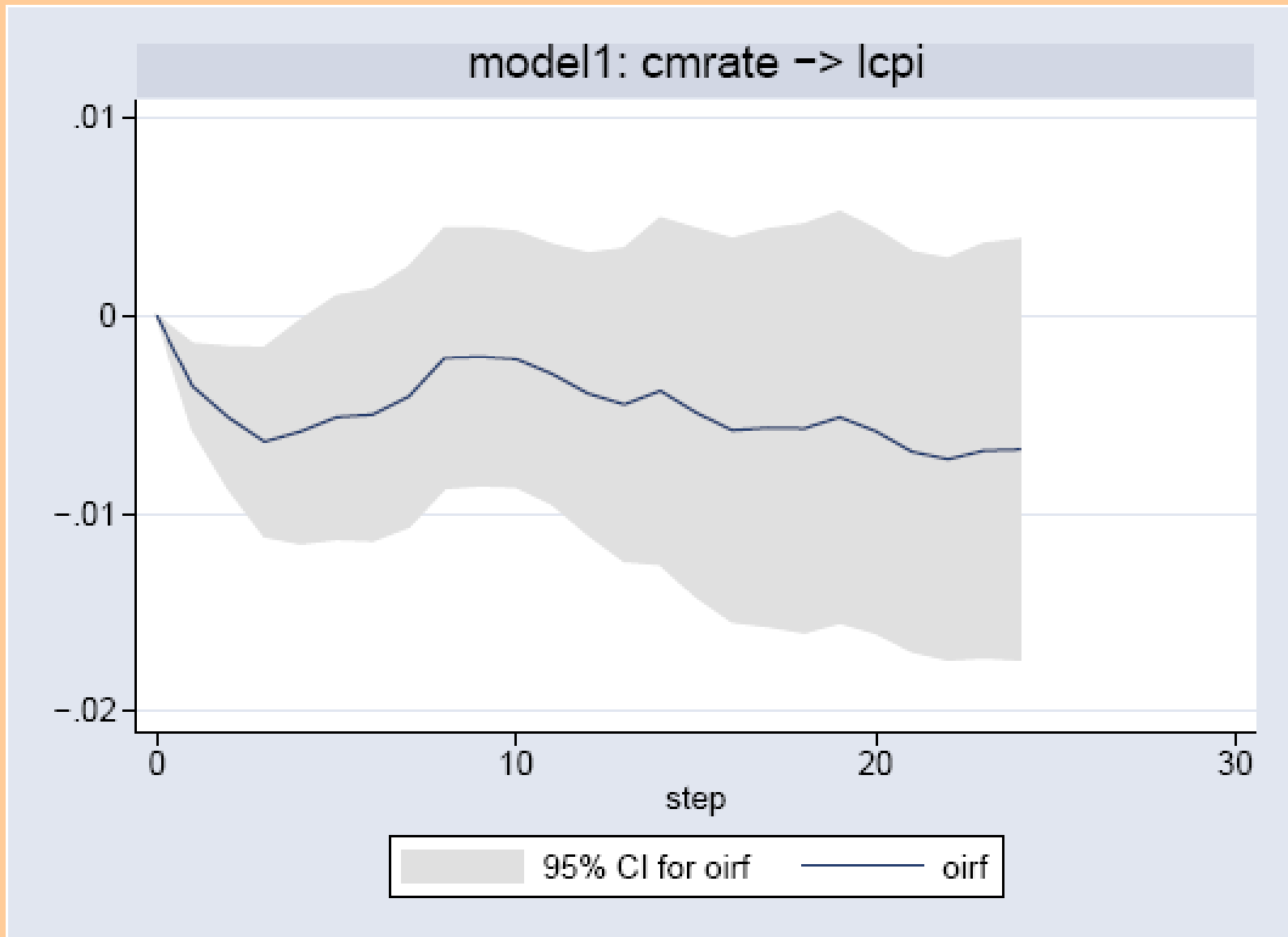
	Rural															
	<i>Head Count ratio (% HCR) Uniform 30 day rule using official poverty lines</i>				<i>Poverty Gap using official poverty lines</i>				<i>Squared Poverty Gap using official poverty lines</i>				<i>Gini Coefficient</i>			
	1983	1987 –88	1993 –94	2004 –05	1983	1987– 88	1993 –94	2004 –05	1983	1987– 88	1993 –94	2004 –05	1983	1987 –88	1993 –94	2004– 05
All-India	46.5	39.0	37.2	28.7	12.36	9.29	8.5	5.8	4.87	3.23	2.84	1.76	30.4	29.9	28.6	30.5
	Urban															
	<i>Head Count ratio (% HCR) Uniform 30 day rule using official poverty lines</i>				<i>Poverty Gap using official poverty lines</i>				<i>Squared Poverty Gap using official poverty lines</i>				<i>Gini Coefficient</i>			
	1983	1987 –88	1993 –94	2004 –05	1983	1987– 88	1993 –94	2004 –05	1983	1987– 88	1993 –94	2004 –05	1983	1987 –88	1993 –94	2004– 05
All-India	43.6	38.7	32.6	25.9	11.4	10.2	8.0	6.2	4.4	3.8	2.9	2.0	33.9	35.0	34.4	37.6

Source: Adapted from Himanshu (2007)

# Short-run Issues with Economic growth

Drought in 2008–09 following from the sharp global rise in food prices in 2007 led to high food inflation, which has now been passed on to the general price level, particularly in light of recurrent commodity price shocks. Anti-inflation policy in the form of higher lending rates has tended to dampen investor sentiments somewhat.





Source: Figure 3 from Jha (2008)

# Prospects for Australia

Australia-India trade and investment relations are strong but well below potential (only around A\$19 billion in 2009–10). Trade with Africa is worth \$45 billion and with China about \$60 billion. Bi-directional trade is heavily in favour of Australia. Australian exports to India are mainly in the resource area and there are some service exports. Indian exports to Australia are largely in the areas of Information Technology, Pearls and Gems, some electronic equipment and some service imports. FDI in each direction was to the tune of A\$3 billion in 2008–09.

There is substantial room for expansion of both trade and investment. India is expected to invest more than US \$1 trillion in infrastructure in the near future. There is substantial room for Australian investment and expertise in this area. Other areas of possible economic collaboration include food processing, educational institutions in India and the use of service sector expertise to enhance manufacturing sector growth, an area in which India has done very well. Australia could benefit from India's expertise in this area.

**Australian Merchandise Trade with India, 2009–10 (A\$ million),  
Total, YOY Growth**

Exports to India	Year on Year Growth	Imports from India	Year on Year Growth
16,179.8	4.9%	1,846	-12.7%
Major Australian Exports to India, 2009–10 (A\$ million)		Major Australian Imports from India, 2009–10 (A\$ million)	
Gold	7,126	Pearls and Gems	142
Coal	5,532	Rotating, Electric Plants & Parts	121
Copper Ores & Concentrate	1,180	Jewellery	107
Crude Petroleum	499	Medicaments (including veterinary)	87
Major Australian Service Exports to India (A\$ million)		Major Australian Service Imports from India (A\$ million)	
Education related travel	3,148	Personal travel (excluding education)	403
Personal travel (excluding education)	252	Information Technology	98

Australian FDI to India in 2009–10 was approximately A\$ million 3,066,278  
Indian FDI into Australia in that year was approximately the same.

## **Conclusions**

The Indian economy is likely to be a very strong engine for economic growth not just in the region, but globally as well. Greater Australia–India collaboration can only enhance favourable economic outcomes for both countries.