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AT THE ROOT OF INDIA’S MANUFACTURING CHALLENGE

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‘it is with respect to education that India has fallen most behind the countries that are the manufacturing successes of the world’ | Photo Credit: Getty Images/iStockphoto

The issue of manufacturing or services as the desirable path for India’s economy makes the rounds in public fora periodically. In the early part of this century, when India’s software exports were booming, it had been asked why India’s services sector should not leapfrog over manufacturing to propel the economy forward. This proposal challenged the standard model of economic development, for, in most successful economies, industrial expansion had come first. The frustration of the Indian economic policy maker can be well understood.

The economic reforms of 1991 had almost exclusively focused on manufacturing, but the significant scaling down of tariffs and the dismantling of the ‘licence-permit Raj’ did not lead to an increase in the share of manufacturing in the economy. Of course, India’s manufacturing sector ought not to be seen only in terms of its size. There has been a qualitative change after 1991. The range and quality of products manufactured in India have undergone an impressive increase. The rising quality and variety of the goods produced, without the expansion of manufacturing in relation to the economy, suggests a rising inequality of income.

After the economic reforms of 1991, the next time manufacturing came into the government’s view was after 2014, when ‘Make in India’, with its emphasis on foreign direct investment, was launched. More recently, there has been the Production-Linked Incentive scheme, which essentially subsidises production of certain products. Though announced with fanfare, the first within months of the Narendra Modi government assuming office, the record of these schemes has not been impressive.

The first advance estimates of the national income for 2022-23 show manufacturing growth to be 1.3% for the year, less than that for agriculture and all main segments of services. While the data unambiguously point to the role of the demonetisation of 2016 in the slowing of the manufacturing sector, the persistence of low rates of growth in the presence of policy initiatives that were focused on manufacturing point to something ‘structural’ holding back the sector in India.

This issue reportedly came up for discussion at a private event, where it was agreed that the economy needs a manufacturing push for the creation of jobs and to raise the growth rate. We

are told that during the ceremony, the Finance Minister addressed the corporate leaders gathered with the remark, “I am sure the Indian private sector is ready. Are you?” Even on earlier occasions, the Minister has publicly referred to the many policy initiatives favouring the corporate sector. Among them, the tax rate had been lowered substantially in 2019 and the government also claims to have improved the ease of doing business. There is also another factor, namely, public investment. In the last Union Budget, capital expenditure was raised by 18.5%. This unusually high increase should come to the aid of the private sector by raising aggregate demand.

Despite the favourable measures undertaken by the government, it would be simplistic to expect industry leaders to achieve a manufacturing push on their own. There is demand to be reckoned with, and this is largely independent of the supply side, which the government has acted upon. Household demand for manufactures inevitably follows the satisfaction of its demand for the necessities of life — food, housing, health and education, none of which can be postponed. For a substantial section of India’s households, food occupies a large share. This constricts the growth of demand for manufactures.

The relationship between per capita income and the share of food in household expenditure is strongly negative globally, with the richest countries, such as the United States and Singapore, having low such shares. Of the large economies of the world, the share of food is the largest in India, and its GDP per capita the lowest. Industry leaders have no control over the demand side of the equation. However, the possibility of exporting means that the manufacturing sector of an economy can sidestep a narrow domestic market. After all, the smaller countries of East Asia would never have been able to grow their manufacturing base to such an impressive level had they relied on their domestic markets alone. Taking this route, however, does require that an economy’s manufactures are globally competitive.

In a comparison with the economies of East Asia, we can see what is necessary for an economy to be a successful exporter. One is infrastructure and the other is the skill level of the workforce. These determine the cost of production and the type of products that a country can produce, respectively. The export of manufactures is largely by sea. The challenge of reaching the seaports faced by companies located in north India can be imagined. Goods have to first reach the coast by road, and then exporters must deal with the relatively poor infrastructure and practices in India’s ports. The competitive disadvantage faced by India’s exporters can be seen in the much higher turnaround time for ships in India’s ports with that in Singapore. The importance of ports for exports may be seen in a public statement recently issued by a section of Kerala’s traders: that they are forced to use ports outside the State as they cost much less to use. While transportation is a big factor, it is not everything yet. Inexpensive power, space and industrial waste disposal services all matter.

But it is with respect to education that India has fallen most behind the countries that are the manufacturing successes of the world. The ranking of countries by the Programme for International Student Assessment reveals this directly. In a group of about 75 countries, the countries of East Asia are at the very top while India barely manages not to be the last. Now, if we do not wish to rely on tests administered by international bodies, we may turn to our very own non-governmental organisation Pratham, which assesses learning outcomes in India’s schools. Its widely publicised findings point to the very low reading ability and numeracy of Indian children in their early years. These tests are for schoolchildren.

While there is no standardised test for university graduates, we have leading Indian employers issue statements on the lack of employability of these graduates. This dismal assessment has extended even to an Indian Institute of Technology. India’s universities expanded to serve the aspiration of its middle class who wish to avoid manual work. However, for those headed for a

life as a skilled worker, ranging from carpenters to plumbers and mechanics, university is not an aspiration at all. This cohort has been neglected in economic policy-making in India. There is no formal assessment available of the state of the vocational training institutes in India, but we certainly know that they are few and far between. When it existed, the Planning Commission had released data showing that only about 5% of Indian youth have had any kind of technical training. The figure for South Korea was over 85%. It would be naïve to expect India to make a mark on the global stage for manufacturing with such a labour force.

The economic reforms of 1991 were undertaken with a view to raising the presence of manufacturing. To this effect, the trade and industrial policy regime had been overhauled. However, it overlooked the need for an entire ecosystem, including schooling, training and infrastructure for manufacturing to flourish. This has to be built. It cannot be achieved merely through legislation. Liberalising reforms have run their course in India.

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