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GDP IS A MEANS, NOT AN END

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MIT economists Abhijit Banerjee and Esther Duflo, who, along with Michael Kremer, won the 2019 Nobel Prize for Economics for their "experimental approach to alleviating global poverty", have published a new book, Good Economics for Hard Times. *The book explains where the economy has failed, where ideology has blinded us, and where and why good economics is useful, especially in today's world, write the authors in the preface. An excerpt:*

Growth in India, like that in China, will slow. And there is no guarantee it will slow when India has reached the same level of per capita income as China. When China was at the same level of per capita GDP as India is today, it was growing at 12% per year, whereas India thinks of 8% as something to aspire to. If we were to extrapolate from that, India will plateau at a much lower level of per capita GDP than China. The growth tide does raise all boats, but it doesn't lift all boats to the same level — many economists worry that there may be such a thing as the middle income trap, an intermediate-level GDP where countries get stuck or nearly stuck. According to the World Bank, of 101 middle-income economies in 1960, only 13 had become high income by 2008. Malaysia, Thailand, Egypt, Mexico and Peru all seem to have trouble moving up.

Of course, there are many pitfalls in any such extrapolation, and India should treat it as what it is: no more than a warning. It is quite possible that India's growth, in spite of all its problems, has very little to do with some special Indian genius. Instead, it has a lot to do with the flip side of misallocation: the opportunities of being an economy with a large pool of potential entrepreneurs to draw upon and lots of unexploited opportunities.

If this is the right story, India should start to worry about what happens when those opportunities begin to run out. Unfortunately, just as we don't know much about how to make growth happen, we know very little about why some countries get stuck but others don't — why South Korea kept growing but Mexico did not — or how one gets out. One very real danger is that in trying to hold on to fast growth, India (and other countries facing sharply slowing growth) will veer towards policies that hurt the poor now in the name of future growth. The need to be "business friendly" to preserve growth may be interpreted, as it was in the U.S. and U.K. in the Reagan-Thatcher era, as open season for all kinds of anti-poor, pro-rich policies (such as bailouts for over indebted corporations and wealthy individuals) that enrich the top earners at the cost of everyone else, and do nothing for growth.

If the U.S. and U.K. experience is any guide, asking the poor to tighten their belts, in the hope that giveaways to the rich will eventually trickle down, does nothing for growth and even less for the poor. If anything, the explosion of inequality in an economy no longer growing has the risk of being very bad news for growth, because the political backlash leads to the election of populist leaders touting miracle solutions that rarely work and often lead to Venezuela-style disasters.

Interestingly, even the IMF, so long the bastion of growth-first orthodoxy, now recognises that sacrificing the poor to promote growth was bad policy. It now requires its country teams to include inequality in factors to take into consideration when providing policy guidance to countries and outlining conditions under which they can receive IMF assistance.

The key, ultimately, is to not lose sight of the fact that GDP is a means and not an end. A useful means, no doubt, especially when it creates jobs or raises wages or plumps the government budget so it can redistribute more. But the ultimate goal remains one of raising the quality of life of the average person and especially the worst-off person. And quality of life means more than just consumption. While better lives are indeed partly about being able to consume more, even very poor people also care about the health of their parents, about educating their children, about having their voices heard, and about being able to pursue their dreams. A higher GDP may be one way in which this can be given to the poor, but it is only one of the ways, and there is no presumption that it is always the best one.

The bottom line is that despite the best efforts of generations of economists, the deep mechanisms of persistent economic growth remain elusive. No one knows if growth will pick up again in rich countries, or what to do to make it more likely. The good news is that we do have things to do in the meantime: there is a lot that both poor and rich countries could do to get rid of the most egregious sources of waste in their economy. While these things may not propel countries to permanently faster growth, they could dramatically improve the welfare of their citizens. Moreover, while we do not know when the growth locomotive will start, if and when it does, the poor will be more likely to hop onto that train if they are in decent health, can read and write, and can think beyond their immediate circumstances. It may not be an accident that many of the winners of globalisation were ex-communist countries that had invested heavily in the human capital of their populations in the communist years (China, Vietnam) or countries threatened with communism that had pursued similar policies for that reason (Taiwan, South Korea). The best bet, therefore, for a country like India is to attempt to do things that can make the quality of life better for its citizens with the resources it already has: improving education, health and the functioning of the courts and the banks, and building better infrastructure (better roads and more liveable cities, for example).

For the world of policymakers, this perspective suggests that a clear focus on the well-being of the poorest offers the possibility of transforming millions of lives much more profoundly than we could by finding the recipe to increase growth from 2% to 2.3% in the rich countries.

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