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Economic Growth, Poverty and Inequality: Paradox in India

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Abstract:

India is a country of continental proportions, and poverty is a multidimensional phenomenon. It is well recognized that the avowed objectives of our social planners immediately after independence of our economy were the ending of poverty, ignorance and the inequality of opportunities. Of course, there has been an evolution of policy strategies from time to time since independence towards this direction. But ironically even after the elapse of sixty eight years after independence about one-third of our total population still suffer from abject poverty and a large section of poverty afflicted people is entangled by the poverty trap i.e. they suffer from chronic poverty.

Focus of the Paper:

- The focus of this paper is an analytical examination of how the relationship between Gross Domestic Product (GDP) and poverty can be changed with the economic growth. By measuring the extent to which economic growth reduces poverty.
- The study will cover that the initial level of economic growth will have significant impact on the reduction of poverty as per given duration.
- It also demonstrates that the tradeoff between economic growth and poverty will lead increase in Human Development and will also lead reduction in economic inequalities.

This paper is a modest attempt to examine the temporal behavior of the growth and poverty since independence. But the main focus of the paper is to show the casual relationship between economic growth and poverty.

Key words: *Poverty, Poverty head count ration, GDP, inequality*

Introduction:

The incidence as well as intensity of poverty has also been reflected in its various dimensions viz, the social, regional, occupational, ethnical etc. in both rural and urban areas of our economy albeit with some degree of variations.

The poverty reduction has become a central goal for development. It can be achieved by economic growth and/or by the distribution of income. Issues related to the benefits of growth accrued to the poor have become a priority of development policy in the 1990s. An emerging consensus is that growth alone is a rather blunt tool for poverty reduction. In conjunction with emphasis on poverty reduction, policies as to the redistribution of income and assets have become increasingly more important. A policy agenda that addresses both distributional concerns and poverty reduction could lead to enhancing both economic growth and equity. Interestingly the government has made changes in the policy strategies towards the objective of alleviation of poverty depending on the dynamic behavior of our macro-economic scenario during the plan period. In fact up to the early 70s we actually followed the strategy of growth mediated development policies on the basis of the expectation of the operation of the" Trickle Down Hypothesis" such that the fruits of economic growth would automatically percolate amongst all sections of people irrespective of region, religion and castes etc. But astonishingly the proportion of people lying below the poverty line remained well above 50% up to mid-70s which was followed by a declining trend thereafter albeit with some degrees of fluctuation. Because of this pessimistic experience of the failure of trickle down hypothesis, our government has made a radical shift of her policy strategy towards the direct attack on poverty by pursuing various workfare and welfare programs viz different employment generating programs like IRDP, SJGSY (latter renamed as SGSY) and 8other social security programs like NREG etc. 9so that the benefits of this programs could reach the target group. These policies were followed up to the end of 80s.Of course this has led to the deceleration of poverty not only at the national level but also at the inter-state level. In fact the incidence of poverty declined up to 39 % at the national level. Majority of the states also experienced declining trends in poverty in varying degrees. Later in the early 90s i.e. since 1991 we have introduced the policy of economic reforms. This on-going process of reforms in various spheres viz, trade, Investment and finance, have indeed led to gradual withdrawal of the public sector coupled with the increasing reliance on the market fundamentalism. Interestingly, since 90s the government has been pursuing the policy of growth cum public action –led development strategy with its major focus on the participatory development process vis-à-vis the inclusive growth which has later been carried forward to the 12th five year plan(2012 to 2017) as its principal objective of faster sustainable inclusive growth. As a fall out of this policy evolution the incidence of poverty has 5 declined both at the national level (29.8% in 2009-10 as per Planning commission) and also at the inter-state level in varying degrees albeit at a lower magnitude. But unfortunately as per estimate of the Planning Commission about 354.6 million of our total population (278.2 million in rural areas and 76.5million in urban areas) still suffer from abject poverty in 2009-10.

On the other hand, one cannot of course deny the fact that Indian Economy since her independence has gradually been moving towards the achievements of faster rate of growth of GDP after surpassing the long term (1950 – 75) persistence of Hindu Growth rate. We have indeed moved to the trajectory of high growth path by experiencing a sharp increase in our national income (i.e. about 7%to9%during 2000to 2007) which has made our country recognized as one of the fastest growing countries in the globe. Of course most of the states have also experienced sharp increase in their SDP during the same period. But this growth has mainly been informal service sector –led growth which is basically predatory and job destroying (Rakshit, 2007, 2009; Bhaduri, 2008).The usual perception is that this elite cantered as well as service sector driven growth process has led to the increase in both absolute and relative inequality in the distribution of income which in turn has led to boost the growth vis –a-vis the persistence of the inequality and poverty. The persistence of the trajectory of high growth both at the national and inter-state level and the higher incidence of poverty as well as inequality is indeed puzzling. So how can one reconcile between the persistence of high growth rate of our national income and the staggering dimensions of chronic poverty even after the pursuance of growth mediated and public action –led development strategies since 80s.

In this paper we show the relationship between economic growth and poverty between the post and pre reform period. To capture the impact of this we will take consideration the GDP at constant prices and on the other side we will take poverty ratio of both urban and rural area, poverty head count ratio and number of peoples. It is well known hypothesis regarding the relationship between growth and poverty is that growth is a necessary condition but not the sufficient condition for the reduction of poverty.

LITERATURE SURVEY:

Tendulkar and Jain (1995) were first to evaluate the impact on economic reform on poverty as early as 1995. This paper analyzed NSS consumption expenditure data of 1993-94 and concluded that the expenditure has reduced in real terms (at constant prices) thereby suggesting that the poverty levels have not changed significantly in the period 1987-89 to 1993-94. Sen (1997), using the same set of data form NSS confirmed the above conclusion regarding levels of poverty.

Chandrashekhar and Sen (1996) did not have 1993-94 NSS consumption expenditure data, but estimated that in 1991-92, the poverty level was 35 percent, while that in rural areas was 44 percent. According to Tendulkar and Jain (1995) the states of Andhra, Assam, Bihar, Karnataka, Maharastra & Rajasthan witnessed a significant decline in per capita consumption expenditure (at constant prices) thus indicating an upward movement in poverty.

Pant and Patra (2001) used NCAER survey data to estimate the rural poverty and concluded that the rural poverty declined in 1993-94 (after 2 years of reform), after showing initial increase due to other reasons (including reduced rural per capita expenditure on poverty alleviation programs). Significantly this analysis finds evidence that reducing the poverty level has also led to reduction in depth and intensity of poverty also

Deaton (2002) decomposes the change in the head count ratios into two components – a growth component and a distribution component. The growth component reflects the increase of per capita expenditure, while the distribution captures that may take place in the distribution of per capita expenditure over households. According to him the 'net' or 'actual'; change in HCR, between 1993-94 and 1999-2000 is 5.9 percent for all India. This exercise conducted state –wise, shows wide disparity (a reduction of more than 10 percent for Gujarat, Tamil Nadu, Haryana, Karnataka & Maharashtra while a less than 2 per cent for Assam and Orissa).

Sen (2004) using NSS data has come to the conclusions that the reforms have only benefited the elite and affluent classes (. Analysis of per capita consumption expenditure since 1980 in rural and urban India, the author has shown that top 20 percent richest persons have increased their consumption by around 40 percent over period 1989-90 onwards. This observation both, for rural and urban population is indeed surprising as it is totally contrary to the findings of these economic classes during the period 1965-66 to 1987-88. Chaturvedi A. (1990) in his study for BERF using NSS consumption expenditure data for rural India concluded that 'growth in consumption of non-food items specially the industrially produced consumer items is contributed to mainly by lower – middle, middle and upper middle classes, the size of which is continuously growing.

Though the major objective of reforms was to uplift the standard of living by bringing down the poverty level, reforms were also aimed at bringing down the regional disparity among regions and states/union territories. Economic reforms are generally praised to be able to bridge the regional disparities in the society. A parallel .case could be considered here is that of China, which also introduced reform (a little earlier than India did). Several studies conducted there Yanrui Wu (1999), Zhang (1998).

Impact of Growth on poverty:

Since the level of income and its growth, other factors apart are the crucial determining factor for the levels of living as well as the incidence of poverty of people we, in this section highlight the growth performance of our

economy both at the aggregative level and also at the cross state level. One cannot of course deny the fact that Indian Economy since her independence has gradually been moving towards the achievements of faster rate of growth of GDP after surpassing the long term (1950 – 75) persistence of Hindu Growth rate. In fact, it has been found that our economy to achieve the trajectory of high growth path between 1975 and 1990, which eventually culminated by the crisis of 1991 caused by high fiscal deficit vis-à-vis the current account deficit. Obviously the fall out of the crisis was the switching of the economy from plan to market. Of course during the post reform period and especially during the first five years of new millennium the growth rate of GDP has reached such a conspicuous level (i.e. 8% - 9% per annum) that India has been recognized as one of the fastest growing economies in the world .Interestingly during the period of half a century the economy has also experienced remarkable structural transformation in respect of her composition of GDP. Parallely it has also been found
that in course of structural transformation of our economy the service sector has been enjoying a comparative advantage in playing a leading role towards the achievements of remarkable growth rate such that the service sector driven growth has been christened as 'service sector revolution' in our economy (Rakshit, 2007, 2009, Bhaduri, 2008).

Now as far as the incidence of poverty is concerned it is well recognized that because of the growth mediated strategy of development and later the inclusion of the direct public intervention
Programs of the government the magnitude of the incidence of poverty has declined not only at the national level but also at the rural and urban areas across the states in varying degrees. However the dynamics behavior of the extent of poverty clearly reveals that the rate of decline was almost negligible up to1970 because of the failure of the trickle down hypothesis so that about 51% of our total population lived below the official poverty line in the mid70s.Later since mid-70s the extent of poverty started declining at a faster space both at the national level and cross-state level such that between 1977-78 and 1987-88 national level poverty declined to 39% and thereafter by 2009-10 it has reached the figure of 29.8%.It is worth mentioning that while analyzing the temporal behavior of the incidence of income poverty across the states we have used the planning commission estimates of poverty .Now since the Planning commission has changed the methodology of estimation of poverty for 2004-05 and 2009-10 by switching over from Lakdawala methodology 18 to the Tendulkar methodology which covers broader perspective for measuring poverty, we have also used the same estimates for the periods 2004-05 and 2009-10 respectively. Obviously because of the change of methodology causing an upward shift in state specific poverty lines we find rather a mild increasing trend in the incidence of poverty across the states between 1999-2000 and 2004-05. This seems to have produced little impact on our panel regression analysis. Interestingly it discernable from the table -4 that almost all the states have experienced declining trend in the incidence of poverty in varying degrees over the period from 1993-94 to 2009-10 i.e. during the post reform period. It is worth mentioning that since there is a switch over of methodology of estimation of poverty between 1999-2000 and 2004 -05, we find relatively higher figures of head count poverty for almost all the states. However if we compare the figures of poverty estimated by using Lakdawala methodology for the same periods then we find almost all the states excepting M.P, Maharashtra, Punjab, Rajasthan, and Orissa have experienced falling trend in poverty (Ghosal, 2010) It also interesting to note that in all the states excepting Assam the incidence poverty has fallen between 2004-05 and 2009-10 estimates for both years are based on Tendulkar methodology. It is also interesting to note that our calorie based estimate of poverty for 2009-10 reveals same declining trend in the poverty with a relatively lesser degree of incidence of poverty across the states as compared to the Tendulkar based estimates for the same period. Now to judge the relative positions of states in respect of their ability towards the reduction of poverty we have ranked all the states such that the state having the lowest incidence of poverty has got rank one and so on. It is obvious from table-4 that no state has been able to retain constant rank. We find that the relative positions of the

states in respect of their ability of reduction of poverty varies remarkably at the inter temporal level over the period of our study.

Table (1)

Year	GDP in Rupee Billions	Poverty Head Count Ratio
1978	8565.34	88.97
1983	10195.60	84.79
1988	13304.86	83.77
1994	17717.02	81.73
2005	35432.44	75.62
2010	52961.08	68.72

Source: GDP from RBI and Poverty HCR from World Bank

Graph (1)

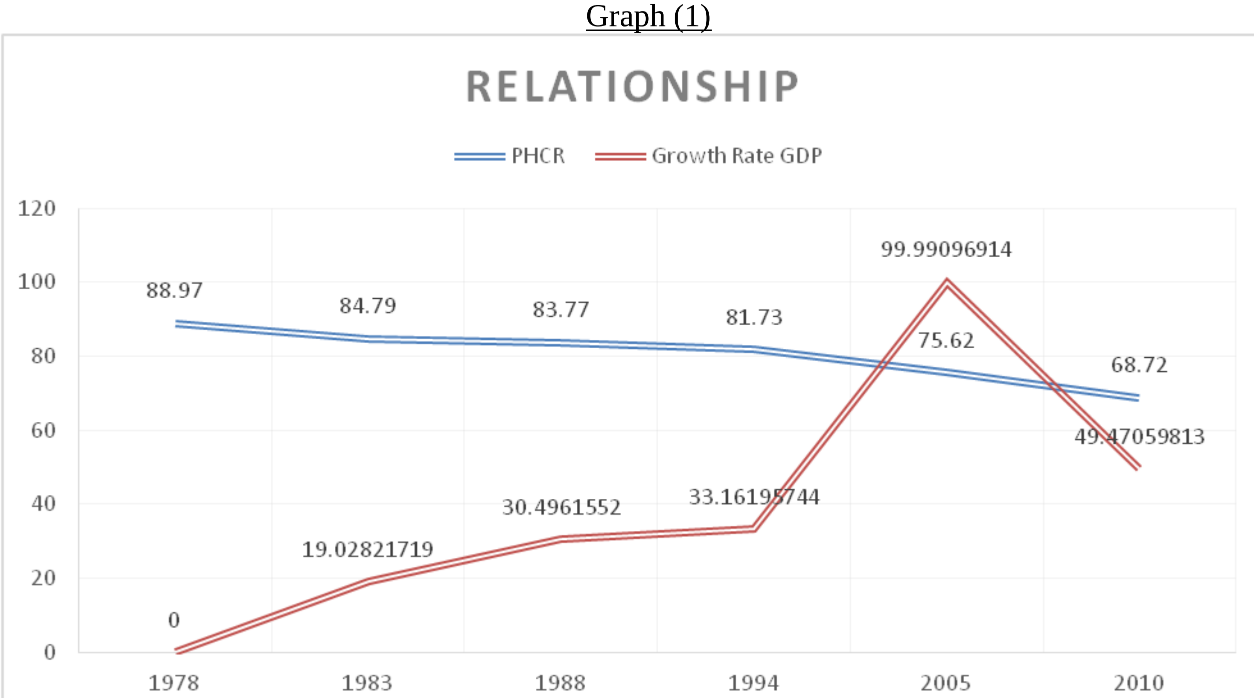


Figure (1) below gives an overview of the dynamic behavior of the level of GDP and Poverty which is being calculated in the form Poverty Head Count Ratio. It reveals more or less an increasing trend over the period between 1978 t0 2010.GDP has a strong impact on poverty. It shows a inverse relationship between GDP and poverty due to increase in GDP poverty ratio declines. We can see with the help of table (1) that when our GDP is 8565.7 Billion in the year 1978 the poverty head count ratio (PHCR) was 88.97 for the same year when GDP increases 10195.6 in the year 1983 the PHCR declines from 88.97 to 84.79. So we can say that when GDP increases the poverty line declines in more simple words poverty reduction of the country depends on Economic Growth. So if we look over the past few years with the increase in standard of living the poverty ratio is declining. If we look over the table (1) the (PHCR) poverty head count ratio has declined significantly from 88.97 in the year 1978 to 68.72 in the year 2010. We also find out the growth rate which you can see with the help of graph (1) which also shows that with the increase in economic growth leads decrease in poverty.

Impact of GDP on Inequality:

The measurement of the effect of inequality on poverty is a difficult task because inequality in distribution can change in infinite ways. It is not possible to establish a simple formula, relating changes in aggregate measures of inequality such as the Gini index to changes in poverty. The larger will be the increase in poverty for a given increase in the Gini index. This suggests that economic growth if accompanied by an increase in inequality may not lead to an increasingly proportional increase in poverty, as was the case when growth did not change inequality.

Table: (2)

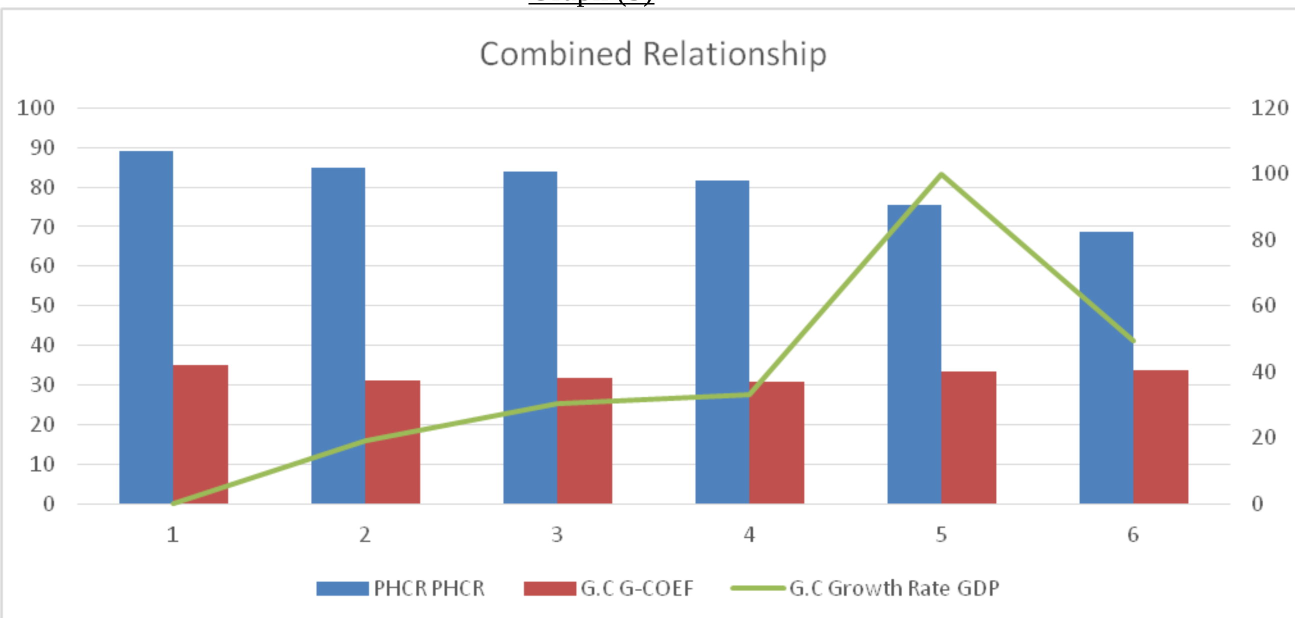
Year	GDP in Rupee Billion	Gini- coefficient
1978	8565.7	35.09
1983	10195.6	31.1
1988	13304.87	31.9
1994	17717.02	30.08
2005	35432.44	33.4
2010	52961.08	33.9

Source: GDP from RBI and Gini- coefficient from World Bank

Graph (2)

If we take a closer look on table (2) we can find out that from the year 1978 to 1994 GDP has a strong impact on the value of Gini-coefficient. If we look over the Economic theory like Kuznets curve it also shows that economic growth led decline in inequality which has been also proved by this data. As the size of GDP has increased from 8565.7 rupee billion in the year 1978 to 17717.02 rupees billion in the year 1994, the value of Gini-coefficient has improved from 35.09 to 30.08 for the same time period. It means during the pre- reform period an increase in the size of GDP has led to the decline in income inequality. But an interesting fact can be note down from table (2) that after economic reforms (from 1994 onwards when its impact started to realized) an increase in the size of GDP has widened the economic inequality. This can be seen in table (2) that in 1994 the size of GDP was 17717.02 and Gini-coefficient was 30.08 in the same year. When GDP increased to 35432.44 in 2005, the Gini-coefficient value increased to 33.4 and when the former increased to 52961.08 rupees billion in the year 2010 then the later increased to 33.9 in the same year. It is a clear indication that after reforms the income inequality has widened. If we look over the graph (2) the growth rate of GDP is increasing inequality is reducing this shows also that with the decrease in inequality poverty reduces.

Graph (3)



This histogram shows the combined relationship between PHCR, GDP and Gini coefficient.

Conclusion:

In this paper, we have demonstrated analytically that the initial levels of GDP and income inequality matter for the reduction of poverty. This paper shows the relationship between GDP, Poverty Head Count Ratio (PHCR) and inequality which is being measured by Gini- coefficient. We showed that the GDP elasticity of poverty decreases monotonically with the initial level of development. That is to say, under the distribution neutral assumption the higher initial level of development leads to a greater reduction in poverty at a given rate of growth. In the paper, we have demonstrated analytically that the initial levels of economic development and income inequality matter for the reduction of poverty.

We showed that the growth elasticity of poverty decreases monotonically with the initial level of development. That is to say, under the distribution neutral assumption the higher initial level of development leads to a greater reduction in poverty at a given rate of growth.

The study also confirmed that inequality will reduce the poverty we can prove it with the help of Economic theory Lorenz curve, so economic growth and reduction in inequality will reduce poverty.

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