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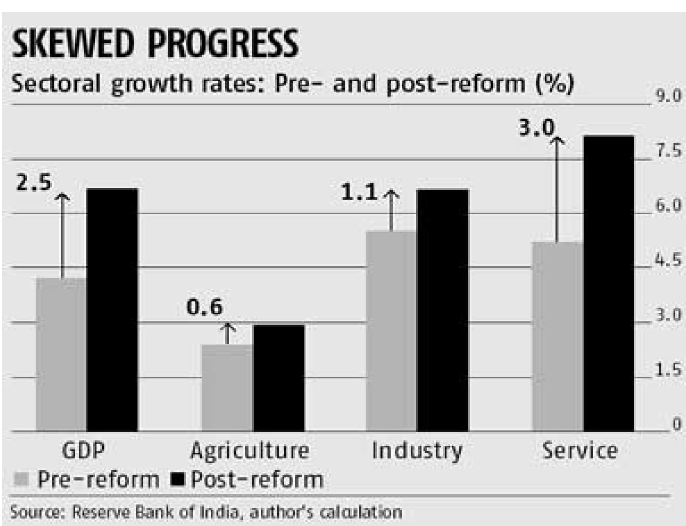
India has a problem with inequality, and it won't be solved easily

Why government policy and jobless growth have let inequality worsen in recent times

The *Forbes* list of billionaires features 55 Indians in 2013. The estimated net worth of only the top ten is $102.1 billion or approximately 5.5 per cent of India's gross domestic product. Paradoxically, every third poor person and every second malnourished child in the world is also an Indian. India also adds 7.5 million babies with low birth weight annually, the highest anywhere in the world. In 2011, India was 73rd out of 88 countries listed in the annual Global Hunger Index, six places down from the previous year. The 2010 Multidimensional Poverty Index indicated that eight Indian states account for more poor people (421 million) than in the 26 poorest African countries (410 million) combined.

This picture of stark contrast brings forth the essence of a nation which, despite being one of the fastest-growing economies in the world, has failed its poor, given the sharp rise in inequality over the years. What is even more disconcerting is that inequality in India has actually increased during the post-reform period.

According to the World Bank, between 1994 and 2005, the income share held by the highest 10 per cent of the population increased from 26 per cent to 28.3 per cent while that of the bottom 20 per cent decreased from 9.09 per cent to 8.64 per cent. According to the OECD, between 1993 and 2008, India's Gini coefficient increased from 0.32 to 0.38. As per the recently released Human Development Report (HDR) 2013, India ranked 136th (134th in 2011) in Human Development Index (HDI). Strikingly, when the HDI is adjusted for inequality, the index loses its value by as much as 29.3 per cent.



What then explains this development? Essentially, India's reform process unleashed opportunities that could be taken advantage of by a limited few. The liberalisation of economic policy affected the nature of India's growth pattern and led to a structural change of the economy wherein the service sector grew at a much faster rate during the post-reform period and propelled India to a higher growth path.

This has not helped enough with employment generation. Currently India's education system is not geared to address the need for high-quality individuals at the scale necessary. Poor quality of education, especially those provided by the states, results in a large proportion of graduates in India being unemployable.

As per available data, a little more than 50 per cent of India's population continues to be engaged in agriculture (which barely accounts for 14 per cent of GDP), while less than 30 per cent of the population works in the service sector, which accounts for more than 67 per cent of GDP. Given the sharp dichotomy between the percentage share of employment in the service sector and its contribution to GDP, average salaries in the service sector went up manifold over the years. However, high levels of productivity (higher output per worker) of India's knowledge workers have kept service-sector inflation under check. The average annual rate of service-sector inflation during the post-reform period was 6.7 per cent, as compared to 6.5 per cent for industry. According to India's 2013 Economic Survey, the finance, insurance and real estate (FIRE) segment, which accounts for roughly 40 per cent of the service-sector GDP but less than two per cent overall employment share, has labour productivity that is nearly 25 times that of the agriculture sector, which has 50 per cent employment share. Thus, although non-agricultural sectors continued to grow faster, this failed to wean away people from agriculture at the desired pace, leading to a lopsided structure of employment distribution in India.

The fact is that the most significant link between growth and poverty reduction is employment generation. Unfortunately, for India, the last decade is widely recognised as a decade of jobless growth, thereby further exacerbating the problem. Stagnation of agriculture, a sharp decline in employment elasticity of the manufacturing sector and a generally poor quality of education has resulted in much lower absorption into gainful employment of those looking for a job.

This is reflected in India's employment statistics. Given the lack of viable employment opportunities, self-employment accounts for roughly 60 per cent of India's working population. A big chunk of this includes low-paying activities like hawking magazines, flowers at traffic signals and the like. Casual workers (who get jobs at times and remain unpaid at others) account for 30 per cent, while only 10 per cent of the working population is in regular employment. Moreover, if one looks at the disaggregated data of employment in terms of educational attainment, unemployment is least among rural unskilled workers while it is highest among educated urban youth.

The inequality is being perpetuated by notoriously unequal access to health and education between the poor (whose ability to pay for better quality private services is very limited) and the rich. In fact, inequality in access to education is so glaring, that in HDR 2013, India's education index loses more than 40 per cent of its value once adjusted for inequality. These have to do with misplaced policy priorities of the government that are only aimed at short-term benefits with an eye towards political gain. Thus, while the Indian government spends less than five per cent of the GDP on health and education, it spends close to six per cent of GDP on (leaky and poorly targeted) subsidies (which, according to the IMF, benefits the rich more than the poor) and interest payments. Higher expenditure on subsidies (which doesn't help in capacity-building) and interest payments comes at the cost of health and education for the teeming millions, thereby blunting future growth potential. India's poor I-HDI score, therefore, does not come as a surprise.

Thus, while India's policy makers are basking under the glory of relatively high GDP growth rate, the increasingly poorer quality of growth is a reminder that they have failed the very people they claim to represent.

The writer is an independent economist