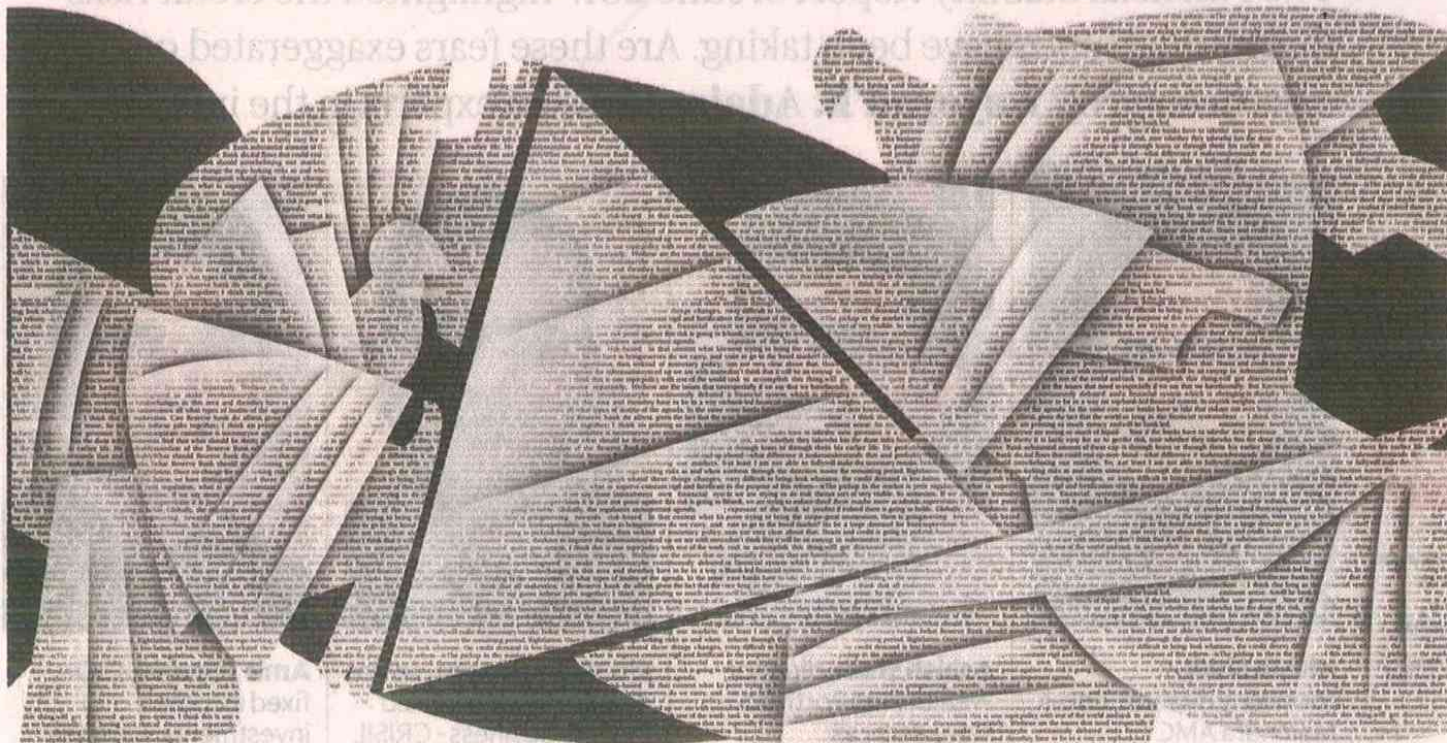


ourview

# India's potential for leading global growth

An innovative method of measuring economic growth and potential points to India's dominance over the coming decade



JAYACHANDRAN/MINT

**A**fter the best part of three years as the fastest growing major economy in the world, India fell behind China in the last quarter of FY17—headline material in the slightly shopworn story of the dragon versus elephant growth race. But according to growth projections released late last month by researchers at the Center for International Development (CID) at Harvard University, based on 2015 data, the reversal is an inconsequential blip. India took over from its neighbour as the “economic pole of global growth” over the past few years and will remain so at least through the decade to 2025. The economic logic underlying those projections raises some intriguing questions about India's growth trajectory.

The projections are based largely on CID's new 2015 Economic Complexity Index—part of the Atlas of Economic Complexity, a brainchild of economist Ricardo Hausmann and physicist César A. Hidalgo. In a 2009 paper, *The Building Blocks Of Economic Complexity*, Hausmann and Hidalgo laid out their reasoning for this new model to judge economic growth. They have argued that a country's economy consists of different capabilities—everything from postal services to the ability to mass produce a certain kind of screw—that are combined in various ways to produce goods and services. The more diverse these building blocks and the more robust the networks that can be used to combine them, the stronger a country's economy with higher gross domestic product per capita. It's back to basics in a way—an extension of Adam Smith's insight on a nation's wealth being linked to effective division of labour.

To give a practical example, the rural poor in several districts of India lack the physical infrastructure to travel far or communicate with more than a limited set of people. This limited interaction and communication means they are poor in knowledge and productive capabilities—and consequently in economic opportunities. Both the economic networks they are part of and their ability to make economic gains via those networks are poor. The reverse also holds true. Make it easier for people to communicate and share and use knowhow—the agglomeration economies of urban centres—and economic benefits follow.

Since measuring these capabilities and networks is an impossible task, the Atlas uses exports as a proxy. Richer countries will export a greater variety of products exported by few other countries, while poorer countries will export fewer, simpler products that are also exported by many other countries. For instance, if Japan, ranked at the top of the index, has vehicles, machinery and electrical machinery as its top exports, Ghana, ranked near the bottom, relies on crude petroleum, gold and cocoa beans.

It makes intuitive sense. And it can be used for predicting growth

more accurately than conventional methods that look at land, labour, institutions and human capital. The greater an economy's potential to build on existing capabilities and diversify, the greater its growth potential—and the larger the disparity between its complexity and wealth, the faster that growth can be. That is why the CID researchers have painted such a rosy picture of India's prospects; it remains poorer than its economic complexity, based on its branching out into chemicals, vehicles and electronics exports, suggests. Productivity structures for services matter as well—another area in which India has done well, although the current woes of its information technology sector reiterate the necessity of moving up the value chain to more sophisticated offerings.

The tricky bit, of course, is using this as a policy aid. Hausmann has recommended that governments function as venture capital does—searching out areas of the economy which could serve as stepping stones to greater diversification and innovation, pumping money into them and moving on if they turn out to be unproductive. This is unfeasible for multiple reasons. Gauging the optimum horizon for such investment is not easy. And predicting which areas are worth investing in at a time when automation is leading to rapid, unforeseen industry shifts is fraught with risks and unacceptable opportunity costs. Then there is the risk of public investment crowding out private investment.

That said, the ECI does offer insight into why financial inclusion and inclusive growth are so important in India. Less complex economies that produce less sophisticated goods usually have more lopsided distribution of wealth. Diverse economies with sophisticated products cannot come about without economic inclusivity that draws more people into productive networks. Nor will a country produce sophisticated goods on a large scale without a robust domestic market for them—something that requires higher median income. In other words, a lack of inclusive growth could spoil the CID's growth narrative for India.

Hausmann has pointed out that complexity is a more accurate predictor than the measures used in endogenous growth theory, such as investment in education and innovation—improving human capital, essentially. But thus far at least, while CID's work has given us useful new tools to measure growth and economic potential, there are no shortcuts to developing the capabilities that form the building blocks of economic complexity. Inclusive growth, better penetration and quality of education and better infrastructure, both tangible and intangible, to enable networking of diverse capabilities, remain India's best bet.

Can India be the lynchpin of global growth over the next decade? Tell us at [views@livemint.com](mailto:views@livemint.com)