



On the Sustainability of India's Growth Rate

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The Central Statistical Organization (CSO) recently declared the revised estimate of Real Gross Domestic Product (GDP) for India for the year 2005-06. While the advanced estimate for the year 2005-06 was 8.1 percent, the revised estimate was found to be 8.4 percent. It was widely covered by the media and the year was identified as one among the four highest growth rate years in India since 1950-51. Other highest growth rate years are 1988-89, 1975-76, and 2003-04. In these years, gross domestic product grew by 10.5 percent, 9.0 percent, and 8.5 percent, respectively.

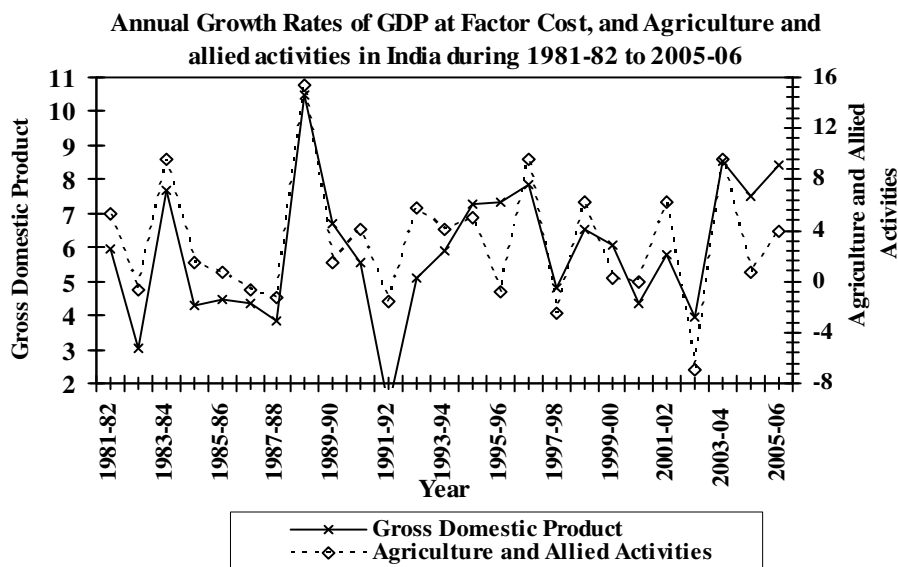
The Planning Commission, which has released the draft of the approach paper to the 11th Five-Year plan titled "Towards Faster and More Inclusive Growth", also, targets an average growth rate of 8.5 percent over the plan period (2007-08 to 2011-12). Moreover, at the conference on Indo-US Economic cooperation, the Honorable Finance Minister, Mr. Chidambaram said, "...we believe we may have reached an inflection point in India's economic progress. That we could now well be on a road that takes us on a sustained basis to 8 percent growth every year and gives us the capacity to dream for higher growth."

There is certainly a reason to be happy, as we have come a long way from the Hindu rate of growth of the 1960s and 1970s. But some doubts still persist about the possibility of attaining the GDP growth rate of 8-8.5 percent per annum without taking some serious policy actions in the agricultural sector. This becomes clear if one examines the behaviour of GDP and its sectoral composition over last 25 years, the major features of which are as follows:

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The performance of agricultural sector largely determines the best and the worst economic performance of India in terms of GDP. It is not to be forgotten that the above-mentioned outstanding GDP performance was driven by excellent performance of agricultural and allied activities. For example, the farm sector grew by 12.5 percent in 1975-76, 15.5 percent in 1988-89, 9.6 percent in 2003-04, and 3.9 percent in 2005-06. On the other hand, 1971-72, 1972-73, 1976-77, and 1979-80 were the four lowest GDP growth rate years since 1970-71. Again, the poor production in agricultural and allied activities sector was mainly responsible for these poor GDP growth rates. For instance, the farm sector had negative growth rates of -1.9 percent, -5.0 percent, -5.8 percent, and -12.8 percent, which, in turn, caused the GDP to grow only at 1.0 percent, -0.3 percent, 1.2 percent, and -5.2 percent respectively in the years just mentioned.

Thus, there has been a close association between the agricultural production and the gross domestic product in India (See Figure). Surprisingly, this remains true even when the share of agricultural production in GDP has been declining. For example, the correlation between the services sector and the GDP was found to be 0.28 and 0.53, whereas the correlation between agricultural output and GDP was found to be 0.94 and 0.61, respectively, in the pre- and post- reform periods.



Agricultural production is subject to large fluctuation. The variability of agricultural production has declined only marginally in the post-reform period, but it was found to be higher than that of industrial and services sectors, respectively (See Figure and Table). The declining trend in agricultural production has also become a matter of serious concern in the recent past. The growth rate in agricultural sector has declined from 4.4 percent during the pre-reform period to only 2.6 percent during the post-reform period.

Variability of Sectoral real growth rates in GDP at Factor Cost

	GDP at <i>Factor Cost</i>	Agriculture and Allied Activities	Industry	Service
Whole Period (1981-2006)	1.98	4.97	3.11	1.70
Pre-reform period (1981-1991)	2.20	5.35	1.88	1.15
Post-reform period (1991-2006)	1.88	4.84	3.61	1.89

Note: Variability has been measured by standard deviation.

The major reason for the excessive volatility of agricultural production is erratic monsoon, and the causes for its declining trend are unavailability of adequate credit, and lack of capital formation in agriculture. According to the Gupta Committee (1997) on Agricultural Credit, “.....for the crop loans there is a substantial unfulfilled demand which is being met by the money lenders, leading to the lower use of inputs and causing a loss of income to the farmers in both the situations”. The proportion of total bank credit for agriculture has fallen from nearly 18 percent in the mid 1980s to 10 percent in March 2003. The number of agricultural loan accounts with scheduled commercial banks has declined from about 27.74 million at the end of March 1992 to 20.84 million in March 2003. There has also been a fall in small borrowal accounts (credit limits of Rs.25,000 or below) from 62.55 million to 36.87 million in the above-mentioned time periods.

Similarly, the public sector capital formation in agriculture plays very important role in the production of agricultural sector. An increase in public sector capital formation causes an increase in private sector capital formation in India. But the share of public sector capital formation in agriculture to gross public sector capital formation has declined from 17.7 percent in 1980-81 to 7.1 percent in 1990-91 and 6.0 percent in 2002-03.

Therefore, it can be concluded that the performance of GDP and its sustainability in India largely depends on sustained growth of agricultural production. But agricultural production in India is subject to high volatility due to excessive dependence on monsoon and has also been witnessing a declining trend on account of non-availability of adequate institutional credit, and a decline in public sector capital formation in agriculture. Hence, the answer to ensuring sustainable growth rate of GDP lies to a large extent in ensuring faster and sustained growth in agriculture. For that, there is a need to increase the availability of bank loans to the small and marginal farmers at reasonable cost, increase public investment in infrastructure like irrigation, power, transport, and agricultural research so that the expected growth rate of 8-9 percent may become possible and also sustainable.