

Opinion **Opinion****India must avoid squandering its economic potential**

The nation's strengths are many but endemic corruption and weak job growth threaten

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The digitisation of the economy has been transformational with digital payments becoming the norm © Francis Mascarenhas/Reuters

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The Indian economy is doing exceptionally well, with many reforms undertaken in past years finally paying off and paving the way for solid growth. Still, there are several blemishes on this growth and the government could yet squander a favourable constellation of domestic factors and geopolitical realignments.

The good news is compelling. India is likely to register the highest growth rate among major economies this year, and [some prognosticators](#) give its economy short odds of one day rivalling America's in size. The nation boasts political stability, a young and growing labour force and a rising middle class, all of which have made it the darling of foreign equity investors.

It is a landing spot for manufacturers looking for alternatives to China as supply chain bases, and prime minister Narendra Modi's government has adroitly staked out the country's independence in pursuing its own economic interests.

India's [economic](#) success is thanks to a number of reforms the Modi administration has undertaken, building on some measures taken by the previous government. A national goods and services tax has led to the elimination of state-level taxes that acted as barriers to interstate commerce. Labour regulations have been streamlined, with many states taking advantage to ease restrictions on hiring and firing workers. Government spending has upgraded the physical infrastructure, from roads to ports.

Macroeconomic [policies](#) are also largely in order. The banking system is in decent shape thanks to the Reserve Bank of India's effective oversight. The operational independence given to the central bank to run monetary policy has helped stave off runaway inflation. The government seems committed to fiscal discipline and to reining in the high level of public debt.

Most of all, the digitisation of the economy has been transformational. Digital payments have become the norm and even low-income households have access to bank accounts for managing savings and credit. The government now makes cash transfers to indigent households rather than subsidising their food and energy purchases, which was an inefficient use of state money and fuelled corruption. The formalisation of the economy has reduced various frictions to doing business.

Extrapolating India's current growth into the future is, however, a fraught exercise. The country's infrastructure still has many gaps in supporting a vibrant manufacturing sector. The educational system is not equipping young people with the vocational and technical skills needed for a modern economy. Job growth has been weak, with little net employment creation in the manufacturing and services sectors. A young labour force with dim prospects of economic advancement raises risks of social instability, turning one of India's boons into a curse.

Endemic corruption continues to hold back overall business dynamism. A few politically well-connected conglomerates have accounted for a significant share of growth, leading to a concentration of economic power. Small businesses still face the tedium of dealing with corruption at many levels of government. Weak private investment, including in infrastructure, and the recent fall-off in foreign direct investment inflows, are indicators of the problems that still bedevil enterprise in the manufacturing and services sectors.

Agriculture remains important to the Indian economy and accounts for large fractions of employment and recent employment growth, which is discouraging as it is intrinsically a low-productivity sector. The Modi government looked willing to pay the political price for much-needed agrarian reforms, including to the government-managed procurement and pricing systems. But it [backed off in 2021](#) when the political price proved too high.

This is a troubling portent. In the run-up to national elections next year, the unfinished reform agenda could take a back seat to the government's [nationalistic and conservative](#) social agenda. Another concern is the attrition of India's institutional framework. A well-functioning legal system, a free press, and other checks and balances are key to maintaining investor confidence. Each of these pillars has been eroded in recent years by a government prickly about criticism, hampering oversight of the corporate sector and limiting government accountability.

India's enormous promise will go wanting if the government switches into triumphalist mode rather than pushing forward with the unfinished economic reform agenda and bolstering its institutions. There is much work ahead to ensure that the nation's moment in the sun does not prove fleeting.

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