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Economic Growth in India

ICT's Quiz - 3

1. India as a 'manufacturer' of mobile phones raises serious questions about the PLI scheme. Why must India put greater focus on growth through the export of services rather than through the export of manufactured goods?

The Indian government claims that in the past five years, the number of mobile phones manufactured has gone up by a significant number, and thus claims that they are a leading exporter of mobile phones. The government owes this huge success to the PLI (Production Linked Incentive) Scheme, which provides subsidies to companies if they setup production units in India. Thus, foreign investment in India is incentivised and it also leads to the decline of imports.

However, according to former RBI Governor Raghuram Rajan, if we look closely at the data, it is very immediately obvious that those numbers do not paint the complete picture. While he does recognise that the PLI scheme helps compensate for the disabilities in the Indian economy, like poor infrastructure and unskilled labour, he also mentions that it's a temporary fix because we aren't targeting the root of the problem.

a. **Assembling vs Manufacturing:**

One of the major issues that he points out is that there is no real manufacturing taking place, but just assembling.

- Apple in India hires workers to make semi-finished shells of the iPhones that are then taken to China for final assembly.
- Manufacturing itself contributes very little value to the final product and even though it does help create low-skilled jobs, we cannot be certain that these jobs will last.
- It is uncertain if we are paying the companies more than the value of the assembly jobs they actually help create.

b. **Performance-linked incentive:**

Since the PLI scheme provides benefits based on how much a company invests in the industry, a lot of companies will try to scam the invoice price and enhance the data.

- If we have to import parts to make the product that is then going to be exported, then the net exports comes out to be negative. So while total exports may have gone up, the net exports are still negative and we are still exporting half-finished goods.

c. **Wasted resources:**

- Rajan also questions if we really have to pay Apple to come set up shop in India. The billion-dollar company has already made it clear that wanted to look for alternatives to China to set up their factories.
- Taking this into consideration, it makes us question if the government really has to pay them to come or if they would come even without any sort of incentives. In the case of the latter, the money could be better spent on increasing the value of the jobs the company helps create and spend more on creating skilled labour.
- If companies are willing to make investments on their own, the government is paying them more than what is necessary.

Thus, the PLI scheme is not a one-stop solution to the challenging problem of the Indian economy.

Rajan also mentions that if we look at data from the past few years, especially after the COVID pandemic, the industry that has been contributing the most is the service industry. He thinks that instead of following the footsteps of China and trying to force ourselves into the manufacturing industry, India should instead walk its own path and invest in services.

- For example, he mentions that the chip designing industry in India is flourishing and has created the most jobs. Chip manufacturing is also the least valuable (and the last stage) of the semiconductor chain.
- Thus, it only makes sense if we invest our resources in creating intellectual engineering minds, which involves giving more budget to schools and universities. This means switching to a more service-based industry, which is also where most of the demand is.
- Also, India is late to the game of investing in the manufacturing industry and with competitors like Vietnam and China, we have a long way to go before we get there. And since this doesn't involve improving human capital, it will not guarantee useful returns in the future too.

Hence, in conclusion Rajan states that the Indian government shouldn't get too caught up in the manufacturing craze just because it has worked for China. India has flourished in the service industry in the past and will continue to do so only if the government realises the potential it has to create jobs and solve our crisis.

2. How are India's credentials and strength as a liberal democracy important for the country's economic future?

It goes without saying that economic and political development go hand in hand. The liberalisation of India in 1991 opened up the gates of development and the private sector contributed the most to the economy. In his interview, Rajan mentions that if we let our governments become authoritarian, it has a direct negative impact on our economy.

- Before the global economic crisis in 2008, India tried investing in the then flourishing manufacturing industry but found that there were several things in the way. For instance, the government needed land for setting up factories but acquiring land from the people for infrastructure was not an easy thing to do and went against our democratic code. In other words, the very nature of democracy is to go against investments in manufacturing and to instead focus on services.
- When we look at our competitors (China and Vietnam), their governments are majoritarian and authoritarian and so, they don't have the most friendly laws that would attract companies looking for services. Our democratic institutions would also mean that we could offer privacy for their data and minimal government intervention.
- A democratic government also focusses on the people. This has a direct correlation with increase in skilled human capital because investment in people means educating them and producing skilled labour, which is especially valuable in the service industry. Since the very nature of our government enhances the quality of our labour, it is a positive feedback cycle.
- Because of the decentralised nature of our government and the fact that our judicial system is not under the influence of the ruling party, privacy is always of utmost importance and the companies can use their services as is needed. Our democratic government is also a good incentive because of the fact that our labour laws will be more relaxed and friendly to both the people and the company itself.

Hence, in conclusion if India continues to present itself as a liberal and democratic country that is open to the investment of services, our economic growth will also go up. We must ensure that our democratic ideals are always maintained and that we have a system of checks and balances in place to prevent misuse of this power.