
UNIT 1 GROWTH AND STRUCTURE OF INDIAN ECONOMY

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1.0 OBJECTIVES

After reading this unit, you will be able to:

- explain the concept of growth and its broader dimensions in form of 'development';

- discuss how economic development brings about fundamental change in the structure of an economy;
- bring out the relationship between development and structure of an economy;
- appreciate the growing influence of the manufacturing and the tertiary sector in the growth process; and
- talk about the changes that are witnessed in such phenomenon as occupational structure of the economy, distribution of national income, and composition of exports in the economy.

1.1 INTRODUCTION

The Indian economy has accumulated development experience spanning a little over six decades. There are some deep changes that have taken place in India, which suggest that the economy's fundamentals are strong. *First*, the current rate of savings and investment have reached levels that even ten years ago would have been dismissed as a pipedream for India. On this important dimension, India is now completely a part of the world's fast-growing economies. Since these indicators are some of the strongest correlates of growth and do not fluctuate wildly, they speak very well for India's medium-term growth prospects. It also has to be kept in mind that as the demographic dividend begins to pay off in India, with the working age-group population rising disproportionately over the next two decades, the savings rate is likely to rise further. *Second*, the arrival of India's corporations in the global market place and informal indicators of the sophisticated corporate culture that many of these companies exhibit also land to the optimistic prognosis for the economy in the medium to long run.

In the medium term, it is reasonable to expect that the economy will go back to the robust growth path. To begin with, there has been a revival in investment and private consumption demand. *Second*, India's exports have recorded impressive growth. Further, infrastructure services, including railway transport, power, telecommunications and, more recently but to a lesser extent, civil aviation, have shown a remarkable turnaround. The favourable capital market conditions with improvement in capital flows and business sentiments, as per the RBI's business expectations survey, are also encouraging. *Finally*, and even though it is too early to tell if this is a trend, the manufacturing sector has been showing a buoyancy rarely seen before. There is also a substantial pick-up in corporate earnings and profit margins.

Over the last half decade or so, India has shown that it can withstand the worst economic recession to have tested the world since the 1930s. It also aptly justifies the remark, made in somewhat different context, that "The Blue Billion Rises".

There are certain critical lessons to be learnt from the sixty years of development experience.

- i) Macro-economic stability is an essential prerequisite for achieving the growth needed for development.
- ii) Growth does not trickle down; development must address human needs directly.
- iii) No one policy will trigger development – a comprehensive approach is needed.

- iv) Institutions matter, sustained development should be rooted in processes that are socially inclusive and responsive to changing circumstances.

1.2 MEANING AND MEASUREMENT OF ECONOMIC DEVELOPMENT

1.2.1 'Development' Distinguished from 'Growth'

Traditional View

Traditionally, economic development has been considered as synonymous with economic growth. Economic growth has been defined as “*an increase in real terms of the output of goods and services that is sustained over a long period of time, measured in terms of value added.*”

Modern View

The modern economists, however, have begun to question this identity between ‘economic growth’ and ‘economic development’; “development is not the same thing as economic growth”. Suppose, by analogy, we were interested in the difference between ‘growth’ and ‘development’ in human beings. Growth involves changes in overall aggregates such as height or weight, while development includes changes in functional capacities, physical coordination, leadership capacity, of ability to adapt to changing circumstances. Growth is an engine, not an end in itself. The end being development.

The traditional concept of viewing economic development as synonymous with economic growth was based on what came to be known as the ‘trickle-down strategy’, which implies the effects of rising incomes and output would ultimately trickle down to the poor so that they would benefit as well as rich. The modern economists reject this view and stress the need for strategies designed to meet the needs of the poor directly. Hence, economic development has come to be redefined in terms of the reduction or elimination of poverty, inequality, and unemployment within the context of a growing economy. Prof Dudley Seers poses the same question about the meaning of development very clearly when he writes:

The questions to ask about a country's development are therefore: What has been happening to poverty? What has been happening to unemployment? What has been happening to inequality? If all three of these have declined from high levels then beyond any doubt this has been a period of development for the country. If growing worse, especially if all three have, it would be strange to call the result “development” even if per capita income doubled.

1.2.2 Concept of Economic Development

In view of the above considerations, economic development, now, is being defined “as the process of increasing the degree of utilisation and improving the productivity of the available resources of a country which leads to an increase of the economic welfare of the community by stimulating the growth of national income.”

Economic Growth = Size of output (A Quantitative aspect)
Economic Development = Size of Output + Economic Welfare (A Qualitative aspect)

It follows from this definition that the progress of development has to be assessed by reference to two separate indicators, namely, the indices of 'production' or 'national income', and of the 'economic welfare' of the community.

- 1) The former covers what may be designed as the 'growth' aspect of development.
- 2) The economic welfare indicator, on the other hand, brings to light the pattern of allocation of resources and of the distribution of income among different groups and classes of the community; in a sense, it combines the 'equity' and the 'growth' aspects of development.

It follows that in pursuit of economic development, the following five types of growth processes should be avoided:

- i) Jobless growth, implying a growth process which does not create additional jobs or which reduces the existing job opportunities;
- ii) Ruthless growth, implying a growth profile which aggravates inequalities in the system;
- iii) Futureless growth, implying a growth paradigm which creates non-sustainability through environmental degradation;
- iv) Voiceless growth, implying a growth process which does not improve the income of the deprived sections of the society; and
- v) Rootless growth, implying a growth process which destroys the cultural roots and traditional life styles of the society.

In view of the above, the *quality of life* is regarded as an important index of development. It is contended that such quality is not adequately reflected in the index of per capita income growth. Several factors are involved in the measurement of such 'quality'; such as education and literacy rates; life expectancy; the level of nutrition, consumption of energy per head, etc. Some of these factors are 'non-monetary', while others can be measured as 'monetary'. There is a need to set up a synthetic index of these different factors to measure economic development and the quality of life.

Some attempts, undoubtedly, have been made in this direction, e.g., some economists have proposed an index of "effective" economic growth, which is the product of the growth rate of real GDP and an index of inequality. Similar attempts have been initiated by individual researchers, multinational institutions and social organisations. Very soon a synthetic index to measure both growth and equity may emerge.

All the same, till such an index is formulated and in the absence of any other reliable indicator a rise in the real per capita income can be and is being employed to measure 'growth' and 'development' in the economy and hence the two concepts can be used synonymously — *even a leaking canopy is best discarded only when a better alternative is in sight.*

1.2.3 Economic Development and Structural Change

Econometricians have attempted to measure structural changes in economies as development proceeds. Much of the pioneering work was done by Prof. Simon Kuznets on the basis of historical data, and the analysis has been extended and

refined using current data, notably under the leadership of Hollis Chenery. Such studies seek to reveal how key economic parameters change as countries develop. We may note the following as important changes:

i) Constituents of GDP Change

More generally, in terms of percentage shares, saving rates increase as income grows; government revenues (and expenditure) increase, food consumption drops and non-food consumption increases, relative output of services – and, of course, also industry – increases, while agriculture falls.

ii) Employment Changes

Employment changes reflect the shift in output and changes in productivity. Labour in the primary sector of the economy does not fall as rapidly as its share in output; the reverse is true for employment in industry where increase in labour productivity is more easily secured.

iii) Shift in the Composition of Exports

As development proceeds and the economy increasingly gets opened to the rest-of the world, exports will account for a larger proportion of incomes and there will have been a marked *shift in the composition of exports*, so that the value of export of manufactures rises relative to that of primary products. Imports will also have risen and earnings and payments will be roughly balanced.

iv) Rate of Increase in Population

As incomes increase, the rate of increase in population may be expected to fall, as the birth rate declines along with a fall in the death rate. The population would still be increasing, but gradually the rate of growth will tend to peter out.

v) Distribution of Income

Income would at first become more unequally distributed and then this trend would be reversed. Equity influences development in two ways: inequalities of power and wealth result in waste and inefficient use of productive resources, and impair institutional development. Unequal power also impedes innovation and risk-taking.

Check Your Progress 1

1) What do you mean by the term ‘economic growth’?

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2) Distinguish between ‘economic growth’ and ‘economic development’.

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- 3) Mention the major changes in the structure of the economy as an economy develops.

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1.3 STRUCTURAL CHANGES IN INDIAN ECONOMY

The national income data can be employed to study important structural changes taking place in the Indian economy during the last six decades.

The process of growth of the underdeveloped economy of India began in right earnest with the launch of the First Five Year Plan in April 1, 1951. The First Plan was a modest plan. It aimed largely to restore stability to the economy. Well-formulated strategy of growth was launched in the Second Five Year Plan. The subsequent Plans primarily gave primacy to this strategy, although modifications were made in response to the changing needs of the economy. The earlier plans aimed largely to build up the production capacity of the economy, and not rapid growth. The strategy affected both the rate of growth and the composition of growth. During the 1980s, the strategy, the rate and composition of growth underwent a change. A new strategy of growth came to be adopted with the onset of the 1990s. The rate of growth accelerated from 3.5 per cent during 1951-1975, to 5.5 per cent during 1975-1990, to 6.5 per cent during 1990-2005, to accelerate further to about 7 per cent during 2005-2012. The changes in strategy and the rate of growth of national income affected the structure of the economy.

1.3.1 Composition of Gross Domestic Product

The composition of GDP of an economy explains the relative significance of the different producing sectors. When a country is in a state of underdevelopment, primary sector (agriculture and allied occupations) makes the largest contribution to the national income. As the country grows and gets developed, the contribution of the industrial and services sectors gradually increases.

The explanation for this shift is as follows: Income elasticity of demand for agricultural products is relatively low; as a result, with rising levels of income, the demand for agricultural products relatively declines and that for industrial goods increases and, after reaching a reasonably high level of income, demand for services of different sectors in the national product get determined by the changes in the pattern of demand. On the supply side, agriculture, being mainly dependent on a fixed factor of production, namely land, faces a limit on its growth and is subject to early operation of the law of diminishing returns. Industry, specially manufacturing, on the other hand, offers large scope for use of capital and technology, which could be augmented almost without limit with human effort. The same applies to services where application of technologies seems to offer much larger scope.

It would be seen that over the period, the primary sector's share has fallen by 40 per cent, while those of the secondary and tertiary sectors have increased. This trend is projected to go further in wake of liberalisation of the economy. This may

happen primarily because of the following factors: (a) reduced restrictions on private sector involvement in areas like software development and information services, (b) technological advances, and lower fixed capital requirements.

Table 1.1 below shows sectoral shares in India's national income and their Growth Rates during the era of planning in India.

**Table 1.1: Composition of Gross Domestic Product and Growth Rates.
(at constant Prices)**

	Primary		Secondary		Tertiary		GDP
	Share	Growth Rate	Share	Growth Rate	Share	Growth Rate	Growth Rate
1950-51 to 1959-60	56.0	2.3	16.0	5.7	28.0	4.1	3.7
1960-61 to 1969-70	47.0	2.5	21.1	6.5	31.4	4.9	3.0
1970-71 to 1979-80	42.8	1.3	22.8	3.7	34.4	4.5	3.5
1980-81 to 1989-90	36.4	4.4	25.0	6.8	38.6	6.6	5.4
1990-91 to 2000-01	28.6	2.9	27.1	5.9	44.3	7.6	5.9
2001-02 to 2007-08	22.9	3.2	20.4	6.1	56.7	8.5	7.6
2008-09	17.1	2.6	18.7	4.7	64.2	9.2	6.7
2009-10	20.3	1.7	25.15	8.6	54.55	8.5	8.4
2010-11	14.5	6.8	27.8	7.4	57.7	8.9	8.4
2011-12	13.9	1.9	27.0	4.5	59.0	9.6	7.1

Note: Till 1999-2000 at 1993-94 prices, and beyond at 1999-2000 prices.

It would be seen from Table 1.1 that the rate of growth of the secondary and tertiary sectors has been more than double that of the primary sector, with the secondary sector having an edge over the tertiary sector during the first two decades. In the subsequent decade, the tertiary sector grew faster than either of the other two sectors. During the 1980s, when all the three sectors were growing at a faster rate, the secondary sector was the fastest. Subsequently, the tertiary sector has been growing the fastest. To an extent the growth of the services sector may have been overstated as new technologies and competitive pressures have led to widespread outsourcing of non-core activities by manufacturing firms, which then show up as services' growth. Also, one suspects that in the system of National Accounts, services are a residual category that ends up including some household and cottage sector production activity. Nevertheless, the growth momentum generated by the services sector cannot be denied.

As a result, the service sector has become the growth-driver in the Indian economy. Presently, about two-thirds of the incremental growth in the Indian economy can be attributed to the tertiary sector.

This pattern of structural change in Indian economy has deviated from the development pattern of western and South East Asian economies. Those economies

experienced first a shift from primary to secondary sector and only in their advanced stage did they experience a significant shift in favour of tertiary sector. That pattern of development enabled them to transfer growing labour force from primary to secondary sector. In India this has not been possible because secondary sector has not expanded fast enough to absorb growing labour force. The unskilled and uneducated rural masses have continued to struggle in the primary sector and those who have been forced out by economic, social and political factors have joined the urban slum sector. Moreover, the sharp increase in the share of tertiary sector in GDP in India has occurred at a much lower level of per capita income than that in the developed countries when they experienced a similar expansion. *This pattern of growth underlines the link between the growing poverty and unemployment and the inadequate growth of manufacturing and building activity in the country.*

1.3.2 Causes of Rapid Increase in Tertiary Sector

The tertiary, i.e., the non-commodity sector, has been growing at a much faster rate than the commodity sector. This in essence means that income generated in the process of circulation grew at a much faster pace than that in the directly productive process, and thereby resulting in an increase in the share of the non-commodity sector. This trend can be attributed to a number of factors, among which the more important are as follows:

- i) A very important factor has been the advent of information technology and the knowledge economy. This has enhanced the growth of the high productivity segment of the services involving low productivity activities catering to a large mass of people.
- ii) A large part of the service sector consists of infrastructure such as banking, insurance, finance, transport and communication and social and community services such as educational and medical facilities. An urgent requirement of development is the proper expansion of infrastructure to cater to the needs of other sectors of the economy and the expansion of the social and community services for the well-being of the people.
- iii) Public services grow more rapidly where national Governments have significant role in planning and production in the economy as a whole. In fact, the 'visible hands' of the modern governments as reflected in the government policies and in the expansion patterns of the national and international authorities during the last few decades are directed towards the creation of fast economic and social infrastructures.
- iv) Operation of the demonstration effect as a consequence of the growing mobility due to expanding foreign trade, tourism and cultural and educational tours is another important factor.
- v) Increasing urbanisation may be regarded as another cause of expansion of the service sector in the economy. In fact, urbanisation is closely associated with a rise in demands for infrastructure services such as communication, public utilities and distribution services. A substantial change in the private consumption pattern of the economy is observed with increasing urbanisation. Many new goods and services enter into the consumption basket.
- vi) Tourism is becoming more and more international as knowledge is being spread through television and Internet, and hotel accommodations quite comfortable. Tourism, in turn, has promoted all types of services.

- vii) With the increasing complexities of modern industrial organisation, manufacturing industries have become service oriented. This has been reflected in the increasing functions of accounting finance, legal services, advertisement, marketing, public relations etc. Because of the prevalent labour laws, these services are being increasingly outsourced, so that growth in industry is actually being counted as growth in services.
- viii) A very important factor has been the favourable international environment, which opened up immense possibilities for the exports of India's service sector. An important contribution has been made by the IT sector, as also entertainment industry, etc.

In addition to the above factors, an increase in the share of the non-commodity sector in the GDP can also be attributed to slow growth in the commodity producing sector. While a part of this is explained by difficulties inherent in bringing about a fast rate of growth in the primary sector, a part is undoubtedly due to the failure of the secondary sector and its major component, which is manufacturing and construction, to grow at the much faster rate that was necessary to give the commodity sector a comparable status with the non-commodity sector in the growth rate.

1.3.3 Prospects and Opportunities

Both domestic and international factors augur well for the growth of services sector in India.

A. Domestic Factors

Some of the important factors can be briefly stated as follows:

- i) As real per capita GDP grows, demand for services increases more than proportionately and this, in turn, reinforces GDP growth itself.
- ii) Within the services sector, demand for producer and government services, which constitute mainly intermediate consumption, have strong multipliers impacting on real GDP.
- iii) The growth of such dynamic service activities, which are intensive users of communication and information technology, will generate employment opportunities on a rising scale.
- iv) The process of economic growth has itself led to the emergence and expansion of new services such as advertising, publicity, marketing, etc. These sub-sectors provide essential service inputs to other sectors in the economy, thereby developing strong linkages with the rest of the economy.
- v) Efficient delivery of services increases the productivity of both labour and capital in the economy as a whole. In general, services sector appears to be highly growth inducing with positive externalities for other services, making services a catalytic agent of growth.

B. International Factors

Some of the recent global developments which provide opportunities for substantial growth are as follows:

- i) The fastest growing segment of services is the rapid expansion of knowledge-

based services, such as, professional and technical services. India has tremendous advantage in the supply of such services because of a developed structure of technological and educational institutions, and lower labour costs.

- ii) Progress in IT is making it increasingly possible to unbundle the production and consumption of information-intensive service activities. These activities – research and development, computing, inventory management, quality control, accounting, personnel administration, secretarial, marketing, advertising distribution and legal services – are performed in all economic sectors.
- iii) Unlike most other prices, world prices of transport and communication services have fallen dramatically. The cost of communication is becoming independent of distance. India's geographical distance from several important industrial markets is no longer an important element in the cost-structure of skill-based activities.
- iv) India does not necessarily have to be a low-cost producer of certain types of goods (e.g., computers or discs) before it can become an efficient supplier of services embodied in them (e.g., software or music). It is possible now to provide value added services without waiting to 'catch up' in technology for production of sophisticated equipment or products.
- v) The decline in the share of manufacturing in the output of rich countries implies a relative decline in their demand for industrial raw materials and fuels. It means that growth in exports of developing countries in the future will depend less on natural resource endowments and more on efficiency in providing service-intensive goods.
- vi) The aging of population in the developed world implies that the demand for services will continue to grow.

As a result of the above development, the sources of comparative advantage of nations are vastly different now from what they were 50 or even 20 years ago. And, there are very few developing countries which are as well placed as India to take advantage of the phenomenal changes that have occurred in production technologies, international trade, capital movement and deployment of skilled manpower. It is now possible for India to take advantage of a virtuous circle of higher growth, higher capital inflows and higher domestic incomes and savings, which in sum can lead to further growth.

1.3.4 Implications

The expansion in the services sector has wider implications for population, employment, and trade prospects of the economy, some of which are as follows:

- a) The growing share of the services sector points to the need for policy initiatives towards introducing greater competition and efficiency in this sector so as to ensure its sustained contribution to exports (especially software) and to higher long-term growth.
- b) The gains in productivity in the agricultural and industrial sectors resulting from technological progress and innovation will have the effect of shifting employment away from the non-service sector to the services sector. This may also indicate a shift in real expenditures from commodities to value added services.

- c) The services sector constitutes a tax-base with vast but unexploited potential, and therefore its growth has long-term implications for the fiscal policy.

1.3.5 Limitations

However, the service sector, at present, suffers from low productivity and quality in spite of fairly large investment in technology.

The sector faces multiple challenges for sustained growth over the years. A number of services where India enjoys comparative advantages experience lack of clear policy thrust. A number of services in India are either predominantly associated with the Government or are not liberalised enough to ensure growth through organised private initiatives. Services like professional, legal, postal, accountancy and insurance need further liberalisation to harness their potential.

Unless sustained efforts are put in to improve these, with the increasing importance of the services in wake of structural adjustment and liberalisation in the economy we may get into two alternate scenarios.

- a) Economic and social position of workers in the service sector will steadily go down — since real incomes cannot be higher than productivity for any extended length of time. This means economic stagnation and consequent social tensions; or
- b) The workers in this sector will use their numerical strength to get wages higher than their economic contribution justified. This will impoverish others — reducing everyone's income and increasing unemployment.

1.3.6 Need for an Integrated Policy

To make services-led growth more widespread and sustainable, it is important to systematically and simultaneously remove those constraints from which the sector suffers presently. To do this, a coherent integrated services policy (in line with the agricultural and industrial Policies) needs to be developed. Reforms in services in India have evolved in an ad hoc manner rather than as part of an overall strategy. Consequently, the depth and pace of reforms lack uniformity across sectors. Given the strong interlinkages between different services, opening a particular services sector may not yield results if not backed by corresponding reforms in other complementary services. Such an integrated services policy should also define the sequence as well as the pace of reforms to be undertaken simultaneously in different services. Liberalisation should be followed in a phased manner accompanied by social policies in sectors that have surplus labour so as to avoid creating unemployment and social unrest. This will go a long way in sustaining the dynamism of services-led growth.

Check Your Progress 2

- 1) What major changes have taken place in the Indian economy over the last six decades?

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- 2) Account for the rapid growth in the tertiary sector in the Indian economy.
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- 3) Examine in brief the prospects of the growth in service sector of the Indian economy.
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1.4 DISTRIBUTION OF GDP BETWEEN AGRICULTURAL AND NON-AGRICULTURAL INCOME

The per capita GDP in agriculture has increased barely by 37.5 per cent in 60 years while that in the non-agricultural sector increased by over 580 per cent. As a result, the difference between the per capita GDP in agriculture and non-agriculture has been growing steadily; the ratio of the per capita GDP in non-agriculture to the per capita GDP in agriculture was 0.68 in 1950-51; it increased to 3.60 in 2010-11.

There are two reasons for the growing disparity between the agricultural and non-agricultural sectors.

- i) The growth rate of the agricultural sector is much smaller than that of the non-agricultural sector; the annual growth rate being 2.38 per cent in agriculture and 4.83 per cent in non-agriculture over the whole period from 1950-51 to 2010-11.
- ii) In spite of the high differential between the two sectors, population does not move from one to the other. The differential stays and grows because the population in agriculture does not or rather cannot freely enter into the non-agricultural sector. The non-agricultural sector is in part an 'organised' sector and entry into that sector is highly restricted. That sector does not take in any more people than it can remunerate at the relatively high level. All the rest may stay behind in agriculture and share whatever they may grow there. Agriculture is a parking lot for the poor.

This may have several implications:

- The use of scarce public resources to boost output in this sector will generate at best limited growth dividends.
- The best way of raising per capita incomes in the sector is to facilitate the redeployment of additions to the rural labour force away from agriculture.
- The redeployment of elements of the underemployed rural work force into more productive areas, in industry and the service sector — has tremendous potential of raising overall GDP growth.
- Higher rural incomes and higher overall incomes would result in a rapid reduction in poverty.
- To drive this redeployment, the natural process of urbanisation – the expansion of the smaller towns and cities – must need to be facilitated.

1.5 SHARE OF THE RURAL AND URBAN SECTORS

A classification of the economy between rural and urban areas is useful for a study of the organisational set-up of industries, the type of activities dominating the economic system in the rural and urban areas and the way of living of the population residing in areas categorised under the two groups.

Information relating to rural-urban distribution of domestic product is available from various research surveys and studies, including those by the NCAER.

During the last two decades the rural economy has grown much faster (7.5 per cent per annum) compared to urban (5.6%) on the back of strong growth in the rural non-farm sector. As a result, whereas in 1980-81, the rural sector accounted for 41 per cent of the GDP, in 2010-11 this proportion has been estimated at 51 per cent, i.e., the rural sector is estimated to have overtaken the urban sector.

Growth in per capita income in rural India has been almost double compared to urban India, though on a much lower base. It would mean that the fruits of economic reforms are finally getting filtered down to rural areas.

Another important feature is that the rural economy is no more predominantly agrarian. Whereas in 1970-71, 73.8 per cent of the rural GDP got generated in the farm sector, this proportion has declined to 41.6 per cent in 2010-11, i.e., about 60 per cent of rural GDP gets generated in the non-farm sector. With this rural India has moved up the income groups, as would be seen from Fig.1.

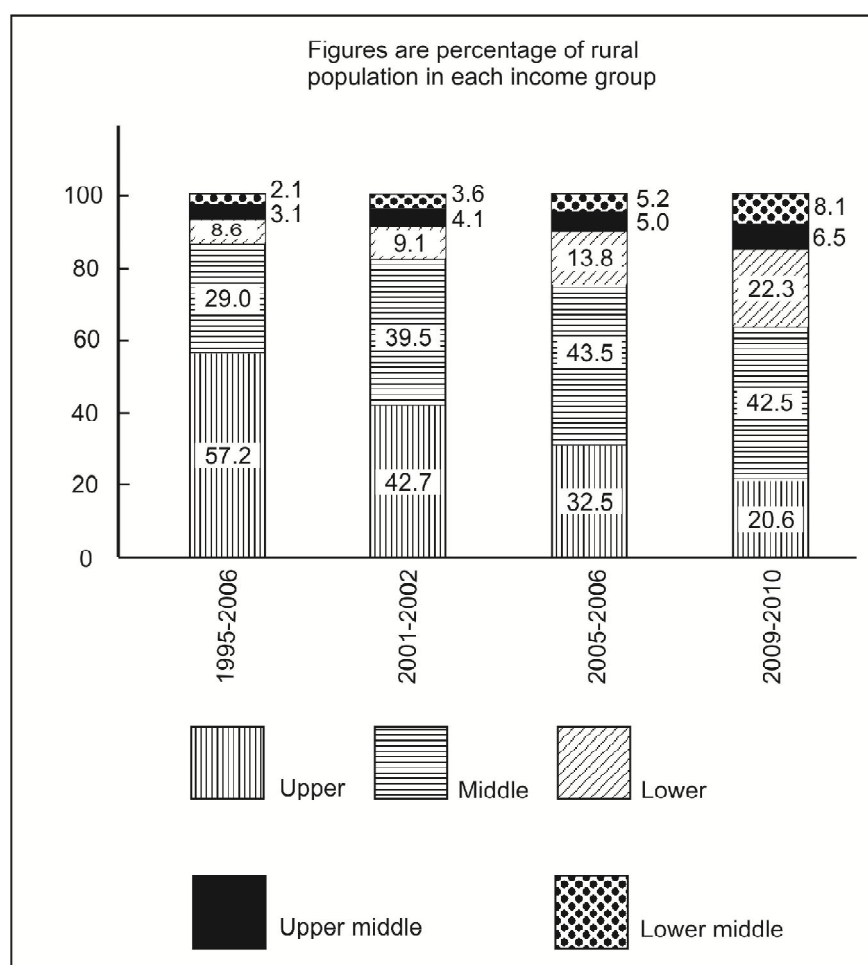


Figure 1.1

Source: Rama Bijapurkar: *We Are Like That Only*.

Moreover, rural India has been far more resilient in the face of the abrupt turnaround in the economy than the rest of India. There are several reasons for this.

- i) The government is no longer spending only on programmes that deliver the final product to the beneficiaries – whether in the form of subsidised food, electricity or building a dam to provide irrigation water to farmers – but has added a new dimension wherein funds are transferred to the beneficiary. This, in fact, gives the beneficiaries the freedom to spend the money and mitigate leakages.

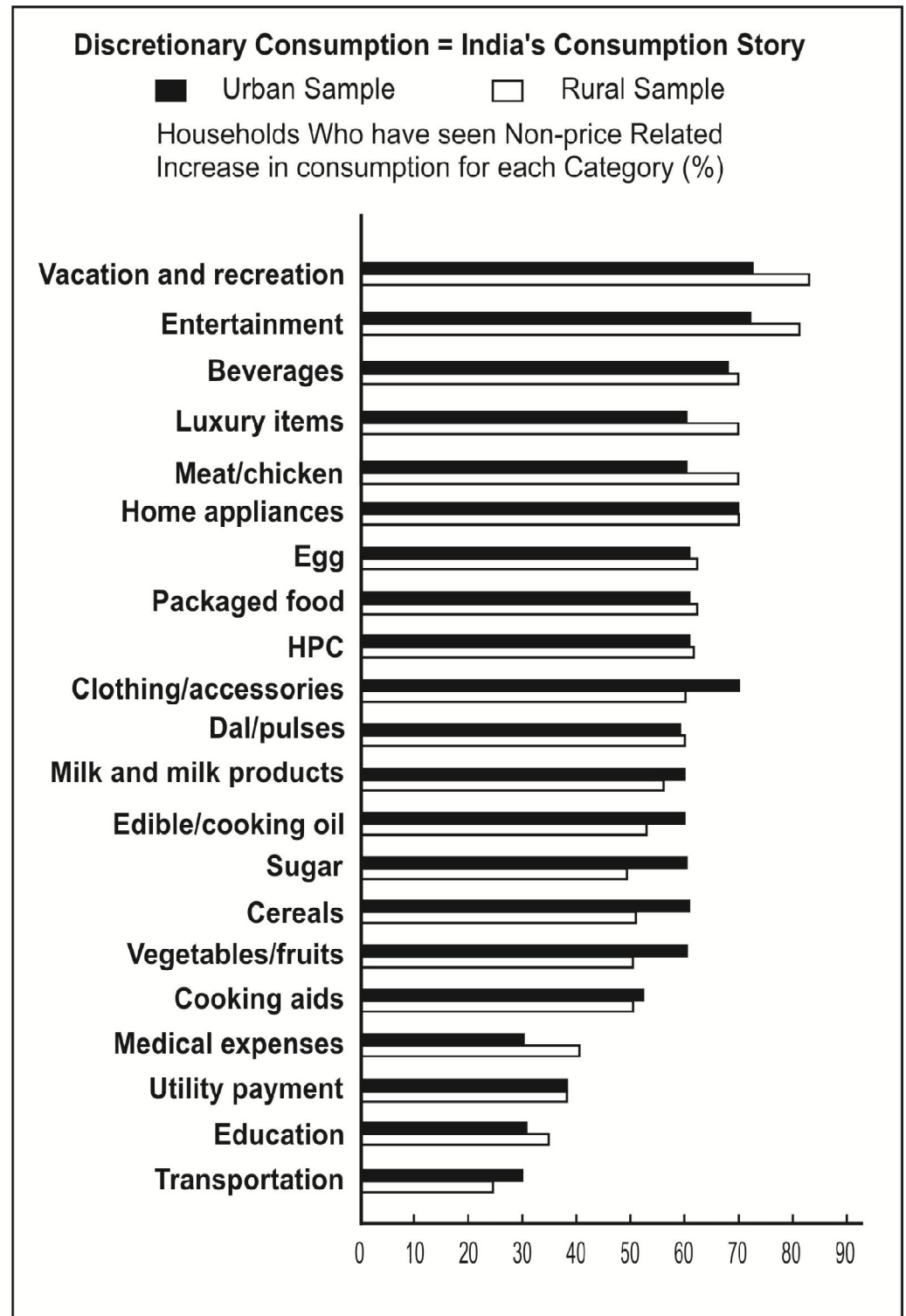


Figure 1.2: Lifestyle Spending on the Rise Across Urban and Rural Households.

- ii) India's agriculture has been at the receiving end of a clutch of positive imperatives. Between 2004-05 and 2011-12, MSPs were raised for common paddy by 40 per cent and for wheat by 80 per cent, while inflation between these two periods rose by around 24 per cent.
- iii) The global commodities boom has ensured new agricultural export markets that strangely seem insulated, even after the onset of a global recession.
- iv) Farmers have hardly seen an increase in input costs, with the exception of higher wages for labourers in the recent past, ensuring that their surpluses are maximised.
- v) Rural areas are now significantly more connected to the rest of India, largely due to fast spread of mobile phones and road network.
- vi) Several thousand farmers across the country have benefited from the record Rs. 65,318 crore farm loan waiver.

1.6 SHARE OF THE ORGANISED AND UNORGANISED SECTORS

Another way to look at the structural change in the income is to look at the organisational pattern of the economy.

The NAS divides the economy into two sectors: organised sector which is identified with a modern market economy and unorganised sector or traditional economy. The unorganised sector or traditional economy. The unorganised sector is defined to include "all unincorporated enterprises and household industries — other than organised ones and which do not maintain annual accounts and balance sheets."

During the last couple of decades, organised sector has been growing faster than the unorganised sector. This trend has been facilitated by policies like reduction in excise duties and tariffs. It indicates growing modernisation in the organisation pattern of the economy.

However, notwithstanding all these changes and trends towards modernisation, the unorganised sector continues to dominate the economy with two-thirds of the NDP and this is not due only to the agricultural sector. In fact, the unorganised sector is to be found not only in the unincorporated and individually-owned, if not also in the individually-operated, enterprises, in most other sectors of industrial origin, except, of course, public administration and defence. A basic change here could influence the economy considerably.

1.7 SHARE OF THE PUBLIC AND PRIVATE SECTORS IN THE GDP

In view of the emphasis that has in the recent past been placed on the development of the public sector in India, it would be useful to look at the changes that have taken place in the structure of the Indian economy in respect of the relative shares of the public and private sectors in the GDP. This can be done with the help of the data given in Figure 1.3.

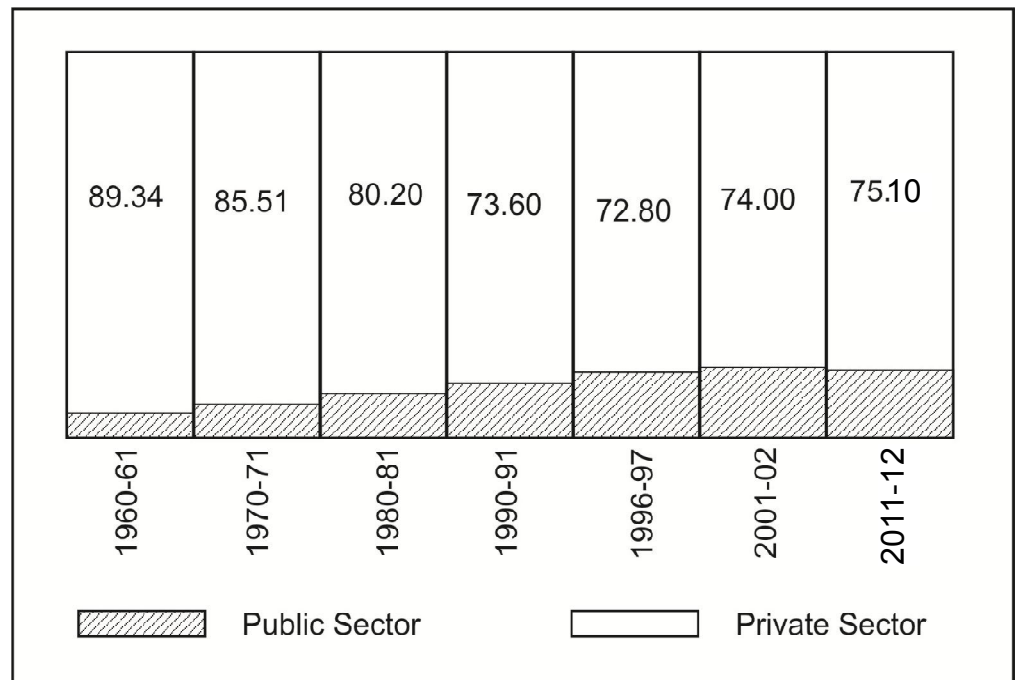


Figure 1.3: Share of the Public and Private Sectors in GDP.

It would be seen from the figure that during the period, the public sector has practically doubled its share in the structure of the economy. In terms of the increased importance of the public sector in domestic activity; over the period the growth rate of the public sector was 6.0 per cent per year, whereas that of the private sector was only 2.8 per cent. If, in spite of this, the private sector still continues to dominate the structure of the economy with 75 per cent of the GDP, it is partly because of the importance of agriculture which still retains a dominant position in the economy.

1.7.1 Factor Shares

The functional distribution of national income, i.e., the relative shares of factors of production in national income, broadly indicates the elasticities of aggregate output with respect to each of these factors of production. The traditionally accepted factors of production are land, labour, capital and enterprise, and their shares are described as rent, wages and salaries (or employee compensation), interest and profits. In Indian economy, there is still another category known as 'self-employed' whose income is known as 'mixed income'. If we analyse the data relating to the factor shares available in the National Accounts Statistics, we reach the following conclusions:

- 1) Mixed income of the self-employed constitutes a large single component, about 40 per cent of the NDP. This would indicate that a large segment of the Indian economy is run by self-employed persons. Sector-wise, the primary sector holds the predominant position among the sectoral mixed incomes, although its share has registered a significant decline over the years. The share of the sector comprising transport, communications and trade, which emerges as the second important sector, has increased over the years, whereas the share of the secondary sector has remained almost unchanged over the years. These trends indicate that:
 - a) the Indian agriculture is becoming more capitalist with less of self-employed labour.

- b) transport, communications and trade are becoming less capitalistic with more of self-employed labour.

In the current decade, beginning with 2000-01, the share of mixed income has shown a declining trend. This is significant and alarming in view of the fact that while the share of population dependent upon mixed income has increased, the share of income received by this group has fallen.

- 2) Another 40 per cent of the GDP in the economy generates in the form of “employee compensation”, and over the years this proportion has been rising. During the period 2000-01 to 2004-05, the share of employee’ compensation came down marginally. This included both workers’ wages, which came down quite sharply, and remuneration of salaried employees, which went up. A sector-wise analysis of the share of employee compensation leads us to the following conclusions:
 - i) The share of the primary sector in total of employee compensation generated in the economy has gone down. This *per se* indicates growing mechanisation;
 - ii) The share of the secondary sector has been stationary which indicates the lack of employment orientation on the part of the industrial growth;
 - iii) The share of the tertiary sector has been rising. It is this sector which seems to be most employment-oriented.

The large role of employee compensation in the NDP is bound to accelerate the forces of inflation in the economy because of the neutralisation that has been brought about in DA to compensate the rise in the cost of living. As, however, neutralisation is either nil or only partial in the case of the unorganised sector, their employees will face more the actual brunt of inflation.

- 3) The share of operating surplus of companies, which includes both private and public enterprises has been increasing, it leapfrogged from about 12 per cent of GDP in 2000-01 to about 15.9 per cent in 2011-12. This jump has been driven primarily by an increase in corporate profitability. The sharp rise in profitability can be explained by the combination of the low interest rates and numerous tax concessions and implicit subsidies that have significantly increased retained profits over this period.
- 4) Remittances: Remittances are calculated as the sum of workers’ remittances, compensation of employees, and migrant transfers. Remittances currently account for 3 per cent of India’s GDP. These play an important role in the process of economic development:
 - i) These can help in increasing overall income levels in a poor household. These can help reduce poverty.
 - ii) These can help household’s smooth consumption and can act as automatic stabilisers in a period of an economic shock.

During a recession a constant inflow of remittances will help in stabilising a household’s consumption and income levels. During a boom or economic upswing, remittances can fuel household consumption or saving, which eventually increases a country’s aggregate consumption. There has been a phenomenal increase in remittances largely due to the following factors:

- a) A huge rise in the number of Indians migrating abroad,
- b) India has become one of the most attractive countries for investment in the world, thereby attracting more remittances,
- c) Easing of the exchange rate, regulations and a gradual opening up of the capital account, etc.

To sum up, an important structural change in the Indian economy has been the rising proportion of wages and salaries (employee compensation) in the NDP. The magnitude of employee compensation in the Indian economy makes it particularly vulnerable to the adverse impact of inflation and also tends to strengthen the cost-push factors in accelerating the inflation. It, therefore, requires that more attention should be paid to non-inflationary aspects of financing economic development than has been done so far.

Check Your Progress 3

- 1) Examine, in brief, the changes in the relative share of the agricultural sector and non-agricultural sector over the last six decades.

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- 2) Examine, in brief, the changes in the share of the organised and unorganised sector in India's GDP during the last six decades.

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- 3) Discuss, in brief, the changes in the share of the public sector and the private sector in India's GDP.

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1.8 GROWTH AND OCCUPATIONAL STRUCTURE

By Occupational structure we mean the distribution of work force in different occupations. In an industrialising economy, going by the vast empirical work of Simon Kuznets, we may expect the following type of structural changes:

- The percentage of the population dependent on agriculture should decline over time in the long run. The converse is an increase in non-agricultural employment over the same period.

- The percentage of the population dependent on industry – manufacturing – should increase over this period.
- The increase in manufacturing employment should absorb at least a major part of the population released from agriculture.
- Within manufacturing, we may expect a shift from household activities to non-household activities as the latter may be expected to be larger, and to use better technology.
- There may be an increase in the percentage of population dependent on services. But, for a country in the early stages of industrialisation, this increase should be less than the increase in manufacturing. At a later stage of development, faster increase in the services sector may be expected.

The reasons for such a change are two-fold:

With rise in incomes, the demand for agricultural goods does not rise proportionately. On the other hand, rise in incomes brings about a large increase in demand for industrial goods and services, resulting in increasing demand for labour in the manufacturing and services sector.

With economic development more capital and better techniques become available with agriculture, so that the productivity of land and labour goes up fast. As a result, there is less need for labour in agriculture. On the contrary, in the industrial sector, although increase in capital and modern techniques makes it possible to bring about large increase in production per head, demand increases at a faster rate than the rise in per head productivity resulting in increasing demand for labour in the industrial and the services sectors.

1.8.1 Occupational Structure in India

Table 1.2 below presents data relating to India's occupational structure since the beginning of the twentieth century.

Table 1.2: Occupational distribution of working population.

(Percentage)

Sector	1901	1921	1951	1971	1981	1991	99-00	04-05	09-10
Primary	71.7	76.0	72.1	72.1	68.7	65.0	60.4	58.4	53.5
Secondary	12.6	10.5	10.7	11.2	13.5	15.0	15.8	18.2	20.9
Tertiary	15.7	13.5	17.2	16.7	17.8	20.0	23.8	23.4	25.6

Source: Census of India and NSSO

Extrapolating on the basis of the Census and the NSSO data 2009-10, a recent study estimates that the share of agriculture sector in total work force may fall to less than 50 per cent in another decade.

The following observations can be made from this table:

- 1) The occupational structure of the Indian economy is lopsided. There is a heavy dependence on agriculture, about one-half of the working population derives its subsistence from agriculture, non-agriculture sector absorbing less than one half of the total working population.

- 2) The whole period beginning with 1901 can be divided in two sub-periods. During the first sub-period, lasting till as late as 1971, the occupational structure of India did not change a bit. The second sub-period covers the period since 1971. Over the last four decades, some definite changes as evidenced on the celebrated Kuznets-Clark-Kaldorian path and as already experienced in other developed countries, have taken place.

Alongwith the changes noticed in the aggregate, a few other important changes in the economy need also be noted.

- 1) Some significant developments in certain segments of the economy can be seen. For example, the number of workers in modern industries is on the increase. The country is producing new products and using new and modern techniques. Furthermore, there is an impressive expansion of job opportunities in services like education, health, science, railways, communications, etc. These changes are indicative that the proceed of modernisation of the economy is under way. But the pace of modernisation is so slow that it does not leave a significant mark on the occupational structure.
- 2) The share of cultivators has come down while that of agricultural labourers has gone up. For the period 1901 to 1961, cultivators accounted for about 53 per cent of the total work force, while agricultural labourers hovered between 14 and 17 per cent. There has been a drastic change in this pattern since then. The share of cultivators came down to 29.7 per cent in 2004-05, while that of agricultural labourers has increased to 19.8 per cent in 1991. Such change is indicative of a major institutional shift in the economy. The movement is away from workers depending substantially on their own resources for making a living towards workers depending, or being obliged to depend, on other people to utilise their labour power.
- 3) The occupational structure in some of the States has undergone a marked change. The all-India trends, however, conceal the different types of changes taking place in the industrial distribution of workers in different States. In Kerala, Tamil Nadu, Maharashtra and Bengal, the proportion of working population engaged in agriculture has declined and that engaged in industries and services has gone up. In Rajasthan and Orissa, however, there has been an opposite development, the proportion in agriculture having increased and that in industries and services having decreased. About other States no definite trend has emerged.
- 4) The level of per capita incomes of different States too seems to tell a familiar story about the occupational structure. In States where the per capita income is about the same as the all-India level (e.g., Punjab, Kerala, Maharashtra, Gujrat, Tamil Nadu), the share of agriculture in the working population is low and that of industries and services high. On the other hand, in States where the per capita income is less than all-India level (e.g., Madhya Pradesh, Bihar, U.P., Rajasthan), the share of agriculture in the working population is high and that of non-agricultural sector low. In short, although the overall picture does not show any change, yet some perceptible changes in the occupational structure in some regions of the country have been marked.
- 5) The composition of the NDP has shown a marked change since 1950-51. There has been a marked fall in the share of the primary sector in the NDP, whereas the share of the secondary and the tertiary sectors has increased. The share of the tertiary sector has increased at a faster rate than that of the secondary sector. These trends are indicative of the structural changes being

experienced by the Indian economy. But these trends are not brought out by the data relating to the occupational structure of the economy.

1.9 GROWTH AND COMPOSITION OF EXPORTS

Composition of Trade is indicative of the structure and level of development of an economy. For instance, most of the UDCs depend for their export earnings on a few Primary Commodities (PCs); these countries export raw materials of agricultural origin and import manufactured industrial products, thus denying themselves the benefits of value added. As an economy develops, its trade gets diversified; it no more remains dependent on a few PCs. It begins to export more of manufactured industrial goods and import industrial raw materials, capital equipment and technical know-how.

Manufactured exports create greater value addition than PCs as they go through more stages of processing. The manufacturing sector has greater linkages with the rest of the economy and hence the downstream effect on exports from these sectors are likely to be greater than primary exports.

The commodities entering trade could also be classified by various other criteria such as value added per unit of output, productivity of labour, capital intensity in production, the strength of backward and forward linkages, etc. The shifts in the commodity composition of trade in these categories would bring out the nature of structural changes in regard to income generation, employment effect and overall industrialisation through linkages effects, etc.

1.9.1 Composition of India's Foreign Trade

Exports

We can classify the various exports in three groups:

- 1) Export-oriented manufactures, viz., exports through industries which are significantly export-dependent.
- 2) Domestic-oriented manufactures, viz., exports through industries which largely cater to domestic needs.
- 3) Non-manufactures, viz., products which are of a natural or agricultural sector.

The relative share of the three groups in total exports has been 64 per cent, 19 per cent and 17 per cent respectively. Apparently, manufactures, and therein too the export-oriented manufactures, have come to dominate our export basket, i.e., our export basket is now less vulnerable to vicissitudes in quantum and unit value of exports. For a country aspiring to industrialise, a shift in favour of manufactured exports is good.

There are two riders, however, to this otherwise happy situation. *One*, high technology exports constitute only 5 per cent of total manufactured exports (corresponding percentage for some other countries are: China 27, Japan 24, Korea 32, Malaysia 58, Netherlands 31, Philippines 74, Singapore 59, Thailand 30, US 31 etc.). *Two*, our manufactured exports have increasingly got concentrated in a few items. From about a half in 1984-85 close to 40 per cent of all manufactured export in 2011-12 were accounted for by just two product categories, viz., textiles and garments, and gems and jewellery. This can be interpreted both a positive and a negative manner.

On the positive side, the potential of these items, undoubtedly, has by no means been exhausted. In fact, given low wage rates, the country will continue to enjoy

its natural competitive advantage in these labour-intensive manufactures and we should promote their exports with vigour.

The negative consequences of concentration are:

- i) Lack of diversification has adversely affected the competitiveness of India's exports.
- ii) There has emerged a mismatch in structures of world trade and India's exports.

In order to benefit from growing world trade, India's export basket has to diversify, change towards higher-valued products and more importantly, to products which have higher technology content.

1.10 GROWTH AND POPULATION CHANGE

Theory of Demographic Transition as formulated by Frank Notestein and based upon the actual experience of the developing countries explains the growth of population through three different stages of economic development. Over time, it follows in the shape of an inverted u, as shown in Figure 1.4.

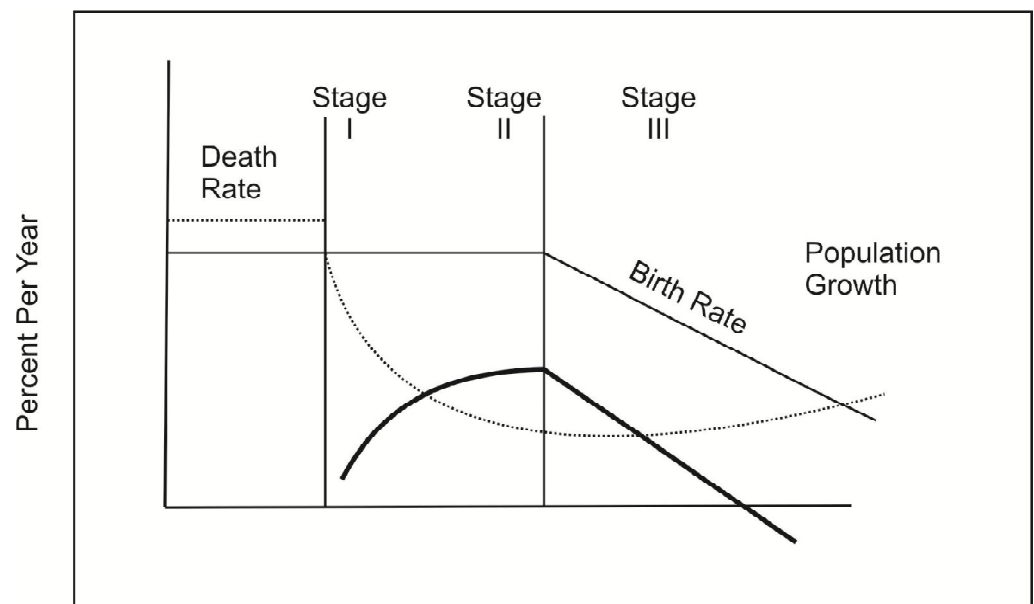


Figure 1.4

The first stage relates to the most backward stage of a country. It is primarily applicable to an agrarian economy with no sign of industrial development. Birth rate and death rate are high in this stage. The birth rate is high as a consequence of widespread illiteracy, early marriages, absence of knowledge of family planning methods, and above all the conventional belief about the big size of a family. The death rate is also high during this stage on account of poverty, poor diet, primitive sanitation and absence of medical facilities. Epidemics take a heavy toll of human life. Many people die for want of food, shelter and clothing. High birth and death rates keep the growth of population either stagnant or very slow.

The second stage relates to a developing country when resources are utilised and industrial development also sets in. The birth rate continues to be high because social customs do not change overnight. Mass illiteracy still exists and the people are not rich enough to practise family planning measures. On the other hand, the death rate falls considerably on account of spread of health technology that brings in improved medical and health facilities, fall in the infant mortality rate and assured

food supply, a better standard of living, and so on. A high birth rate matched with a sharp decline in the death rate causes a rapid increase in population. This stage is better known as the stage of 'population explosion'. The consequences of this stage are very dangerous. The population outpaces production. Whatever little development takes place in the country is eaten away by the excessive population. Sooner the country gets out of this stage, more favourable the conditions for economic growth would emerge.

The third stage relates to a developed country. Economic development advances further. The character of the country changes from the agrarian to the industrial status. The birth rate falls sharply on account of universal literacy, an extensive use of family planning devices, and a high standard of living. Instead of homes, women prefer jobs outside. The large size of a family obstructs free mobility, hence a general preference for a small family prevails. The death rate also falls, sometimes to unusually low levels because of the superfluity of young people in the population. Eventually death rates rise somewhat as the age distribution becomes more normal. The population of a country grows at a slow rate, if at all it rises.

In short, the theory of demographic transition views economic growth as a sufficient condition for a decline in fertility.

1.10.1 Trends in Population

India is the second largest populated country in the world with the total population enumerated in the 2011 census at about 121.02 crore. This forms about 17.5 per cent of the total population of the world. In other words, every sixth person on the earth is an Indian. India, on the other hand, has got only 2.4 per cent of the total land area in the world. China with about 20 per cent of the world's population has about 7 per cent of the land area, the U.S.A. maintains only 6 per cent of the total area; Russia has 5 per cent of the population and 12 per cent of the land area. It would thus be seen that India has been seriously handicapped in that a large proportion of the world population is found jam-packed in a small area.

India's population has grown over the years as can be seen from Table 1.3.

Table 1.3: Trends in Population in India.

(Crore)

Year	Population	Year	Population
1901	23.80	1971	54.81
1911	25.20	1981	68.33
1921	25.10	1991	84.63
1931	27.90	2001	102.70
1941	31.87	2011*	121.02
1951	36.10	2016*	126.89
1961	43.92	2026*	139.98

Source: Census of India.

As brought out in Table 1.3, the history of population growth in India divides itself into four natural phases.

1901-1921: Stagnant population

1921-1951: Steady growth

1951-1981: Rapid high growth

1981-2011: High growth with definite signs of slowing down.

Before 1921 the growth of population was very slow: as a matter of fact, India's population had declined during the decade 1911-21. The decline was caused by famines and epidemics. The year 1921, therefore, is also known as the 'Year of Great Divide'.

The next census of 1931 and the following census of 1941 recorded an increase of the magnitude of about 2.76 crore and 3.97 crore respectively. The increase after the country's Independence was more rapid. Thus, whereas during the first fifty years of the present century, i.e., during 1901-51, India's population had increased by about 12 crore, it increased by about 32.5 crore during the three-decade period of 1951 to 1981.

The upward trend in population growth rate maintained since 1951 got reversed during the decades 1981-2011. It means that although India continues to grow in size, its pace of net addition is on the decrease.

1.11 GROWTH AND DISTRIBUTION OF INCOME

The pattern of income distribution in the UDCs shows wide inequalities: a large proportion of income generated in the economy accrues to a smaller section of the society, whereas a larger proportion of population is left to thrive on a smaller slice of income. For instance, evidence from 44 UDCs suggests that, on an average, only about six per cent of the population, whereas 30 to 56 per cent of national income is obtained by the highest 5-20 per cent of the population.

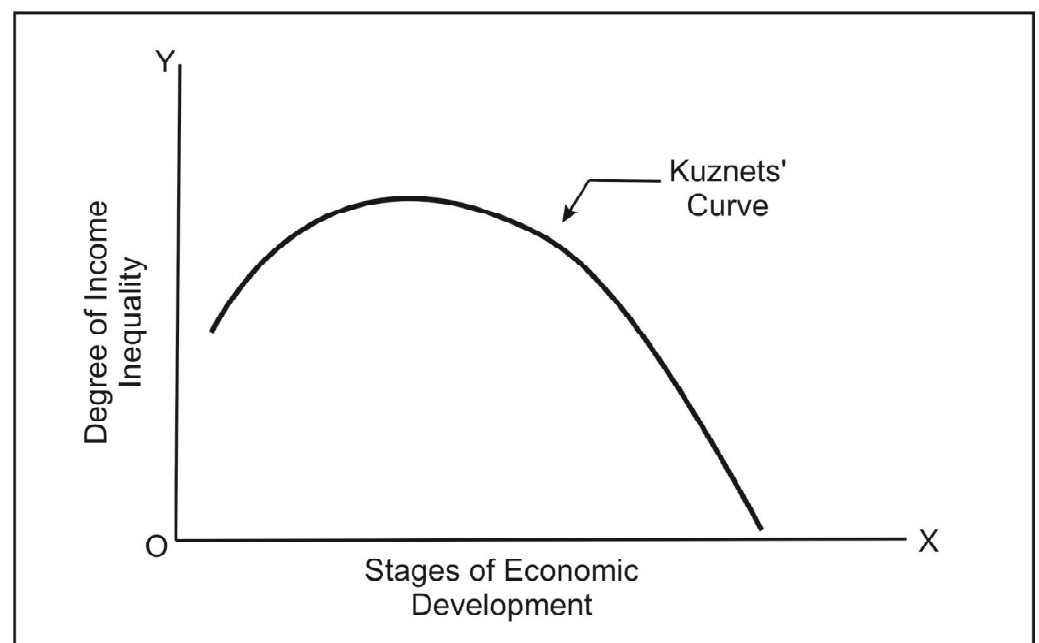


Figure 1.5

Economists generally agree on an asymmetrically U-shaped relationship between income distribution and economic growth as shown with the help of Kuznets' curve in Figure 1.5. The inequality widens during the early phase of economic growth, relatively stabilises at a given level, and then narrows in the advanced stages of growth.

1.11.1 Inequalities in Distribution of Income in India

The extent and magnitude of inequalities of income in India can be studied on the basis of available data relating to: (1) income distribution, (2) wealth distribution, (3) consumption expenditure, and (4) distribution of savings in the country.

- 1) The data relevant to income distribution is contained in a number of studies carried out to measure the extent of inequalities. A conclusion common to all the studies is: the gross inequalities of income exist in India.

For example, according to UNDP's Human Development Report 2009, the top 10 per cent of the population had 31.1 per cent of total income while the bottom 10 per cent has to do with only 3.6 per cent of income. The Ginni coefficient worked out to be 0.368.

- 2) Inequalities are more wider in distribution of wealth, as brought out in a 2009-end study. It highlights that the top 10 per cent of the population had 52.9 per cent of the country's wealth, while the top 1 per cent had 15.7 per cent. In contrast, the bottom 1 per cent of the population own a meagre 0.2 per cent of the country's wealth and the bottom 20 per cent own just 1 per cent. The Ginni coefficient for wealth in China is 0.550 and in US it is 0.801).
- 3) Information on the distribution of the household consumption is available from the data collected by the National Sample Survey Organisation (NSSO). What is more, inequality of wealth has been consistently higher than even income inequality. The Ginni Coefficient of wealth distribution has been around 0.65.
- 4) Similarly, distribution of savings originating in the household sector also brings out the fact of inequalities in income distribution. According to NCAER, the bottom 70 per cent save 6 per cent of that total while the top 10 per cent save 68 per cent and the top 5 per cent save 50 per cent. In particular, the lowest 45 per cent of the urban people saved 4 per cent, while the top 10 per cent saved 56 per cent.

Ginni Index

Ginni index for India has been estimated as 32.5 (index value of 0 implies perfect equality and 100 implies an extreme of inequality). Among a group of 106 countries, India ranks at 51, way above countries like Ethiopia, Pakistan, Bangladesh, Sweden, Norway and Germany. (Surprisingly, the value of Ginni coefficient is higher in countries like China and Russia.)

Another evidence of inequality in income distribution is brought out by a recent World Bank publication (*Equity in a Globalising World*, 2010). There is no middle class in India. Middle class includes people with an income above \$10 a day, but excluding the top 5 per cent of that country, in India, everyone at over \$10 a day is in the top 5 per cent of the country.

Check Your Progress 4

- 1) How does economic growth affect the occupational structure of an economy?

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- 2) How does the composition of exports change with economic growth?

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- 3) Highlight the important demographic changes which result from economic growth.

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- 4) Examine the effects of economic growth on the distribution of national income in an economy.

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1.12 LET US SUM UP

Indian economy as a mixed economy is on the path of transition — transition from underdevelopment to development, from poverty to prosperity, from scarcity to abundance. Along-with economic transition we are also seeking two other fundamental transitions, big political decentralisation (i.e., devolution of power from the Centre to the States and from the States to local self-government bodies) and social empowerment (for traditionally disadvantaged and discriminated groups). How soon India can traverse this long path will depend upon a multiplicity of factors like the availability of resources, the economic policy pursued by the State, etc. But, for India to set out boldly for a new pattern of interaction between the State and the market what is more important is to disavow what Keynes called “the tyranny of the status quo”.

1.13 EXERCISES

- 1) Distinguish between ‘economic growth’ and ‘economic development’. How is economic development a better measure of economic welfare?

- 2) Highlight the importance of the composition of GDP of an economy? What important changes in the composition of GDP have taken place over the last six decades?
- 3) What changes have taken place in the composition of GDP over the last decades?

1.14 KEY WORDS

Economic Growth	: An increase in the quantity of goods and services produced in an economy during a year.
Economic Development	: A process of economic changes which brings in an improvement in the general standard of living in an economy.
Composition of GDP	: Industry wide classification of GDP among three sectors of the economy, viz., primary, secondary and tertiary.
Composition of Exports	: A commodity-wide distribution of exports by a country during a year.
Demographic Dividend	: Changing age composition of population that results in increasing number of labour force.

1.15 SOME USEFUL BOOKS

- 1) Dhingra Ishwar C. (2012): *The Indian Economy: Environment and Policy*, 27th Ed.
- 2) Basu Kaushik (ed.) (2010): *The Oxford Companion to Economics in India*, Oxford.
- 3) Srinivasan, T.N. (2004): *Eight Lectures an Indian Economy*, Oxford.

1.16 ANSWERS OR HINTS TO CHECK YOUR PROGRESS EXERCISE

Check Your Progress 1

- 1) See Sub-section 1.2.1
- 2) See Sub-section 1.2.1
- 3) See Sub-section 1.2.3

Check Your Progress 2

- 1) See Sub-section 1.3.1
- 2) See Sub-section 1.3.2
- 3) See Sub-section 1.3.3

Check Your Progress 3

- 1) See Section 1.4

**Indian Economic
Development: An Overview**

2) See Section 1.6

3) See Section 1.7

Check Your Progress 4

1) See Section 1.8

2) See Section 1.9

3) See Section 1.10

4) See Section 1.11