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South Asian Economies: Growth Experience

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South Asia has witnessed a growth miracle in the past five years. This paper tries to examine the growth experience and examine the performance of the South Asian economies since 1980s. The current global crisis may potentially change globalization itself. It appears that the three aspects of globalization - capital flows, trade flows, and economic management - may not be the same in the future. Trade flows will be diminished and exports may not be a powerful engine of growth as developed countries try to correct the imbalance by consuming less and saving more. Thus, the chances of external demand for traded goods picking up anytime soon are bleak. Improved education and health are, thus, essential means of increasing GDP. South Asia has transformed itself from a region of primary products to a region of services virtually skipping the manufacturing stage. Quality of service exports from the region resemble that of developed countries. This unique trade and growth pattern of South Asia has important implications for the recovery of the region. Despite a shift towards market liberalization, South Asia continues to be overregulated. As a result, it is not fully realizing its growth potential and there is a need for better targeting of investments and in particular, for improvements in sector policies, governance, and institutional environment.

Keyword(s): Globalisation, Structural change, Economic Growth, Value Added

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Introduction

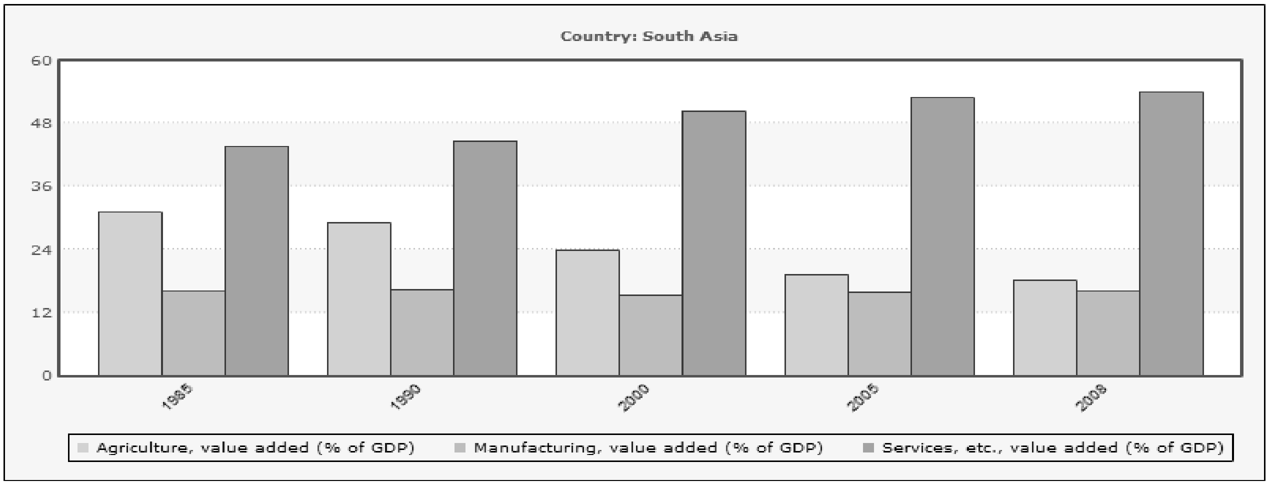
According to the UN division, 8 countries make South Asia namely Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, Sri Lanka. The study discusses the growth experience of South Asia, South Asian economies in particular as well as its comparison with other economies of the world. The South Asia in general and some countries in the region (especially India), in particular, have experienced unprecedented growth since 1990s. It has helped in poverty reduction and raised the human development index, though there is hardly any improvement in the relative HDI ranking. Similar improvements have taken place in the macroeconomic fundamentals (lower inflation, smaller current account deficit, and declining fiscal deficit in the last 5 years), in the saving and investment rates, and in the integration with the global economy.

While developments in India are clearly the predominant factor in the improved economic performance of South Asia, most other countries in the region have been on a similar trend—although their improvements generally are more modest. Despite the high growth rate, the total number of people in poverty has not gone down and health and education are still areas of serious concern.

How Is The Growth Experience Of South Asia Different From Other Economies?

South Asia, in general, and countries in the region (especially India), in particular, have experienced unprecedented growth since 1990s. It helped in poverty reduction and raised the human development index. However, though there is hardly any improvement in the relative HDI ranking. Despite the high growth rate, the absolute number of people in poverty has not gone down, and health and education are still areas of serious concern.

Figure 1: Value Added (% OF GDP), South Asia



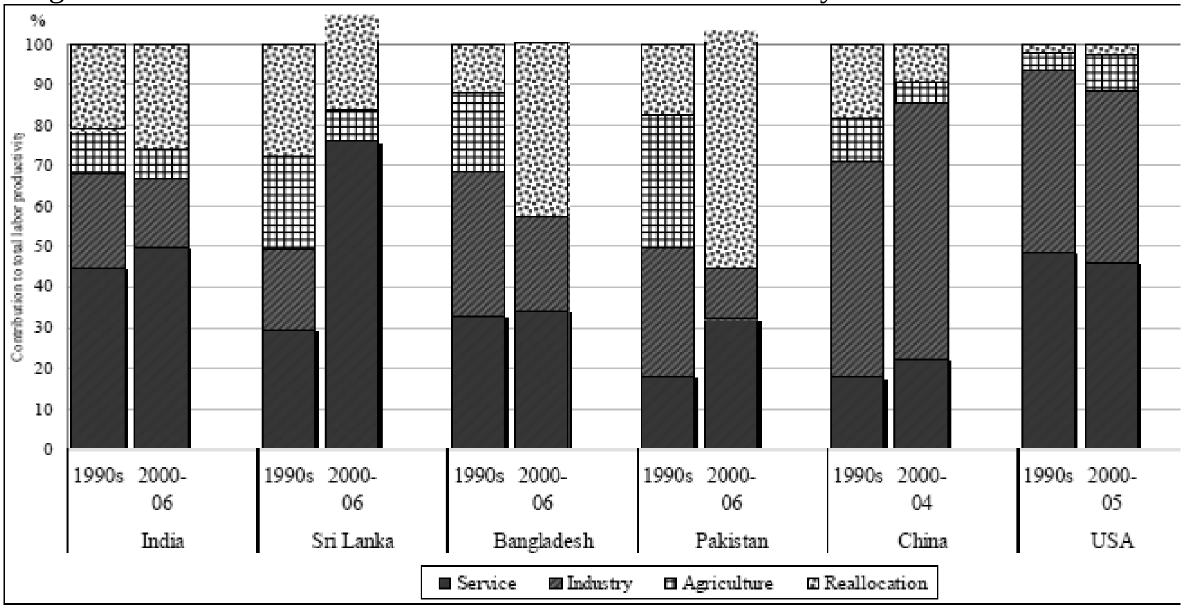
Source: World Bank

Looking at the sectoral contribution to GDP (Figure 1), Growth miracle of South Asian is service led unlike East Asia which is a story of manufacturing led growth miracle. Services are the major contributor to GDP in South Asia, accounting for more than 50% of GDP in all South Asian countries—India, Pakistan, Bangladesh, Sri Lanka and Nepal.

South Asian GDP composition resembles that of developed economies like Ireland and Norway, rather than that of China and Malaysia. Despite being a low income region, South Asian countries have adopted the growth patterns of middle/high income countries. Contribution of service sector to GDP growth in South Asia is nearly double than the contribution of industry to GDP growth.

Growth in South Asia is driven by structural changes. Now what this means, unlike other economies, the miraculous growth story of South Asia is scripted by the service sector growth. South Asia, it seems has consciously skipped the manufacturing sector, and has leaped straight from agriculture into services. This massive structural transformation from primary good producer region into the region of services has been a key driver of growth in the region. (David, Canning and Rosenberg, 2011)

Figure 2: Sectoral Contribution To National Labor Productivity And Reallocation Effects



Source: World Bank 2008a.

Services in South Asia have much higher productivity as compared to agriculture and industry and growth in service productivity has contributed the most to the overall growth in labor productivity in the region. South Asia differs significantly on these dimensions from East Asia. In East Asia, industrial sector has the highest productivity growth and has contributed the most to the growth of national productivity (Figure 2). Even in USA the contribution of industrial and service productivity growth are nearly equal.

Table 1: Agriculture, Value Added (% of GDP)

	1980	1990	2000	2005	2010
World	7	5	4	3	..
High income	4	3	2	2	..
South Asia	35	29	24	19	17
India	36	29	23	19	16
Source: World Development Indicators and Global Development Finance					

Table 2: Manufacturing, Value Added (% of GDP)

	1980	1990	2000	2005	2010
World	25.1	22.3	19.2	17.4	..
High income	25.0	22.1	18.8	16.7	..
South Asia	16.3	16.3	15.4	15.9	16.2
India	16.7	16.7	15.6	15.4	16.0
Source: World Development Indicators and Global Development Finance 2011					

Table 3: Services, Value Added (% of GDP)

	1980	1990	2000	2005	2010
World	56.36	61.42	67.52	68.92	..
High income	59.12	64.56	70.49	72.33	..
Euro area	58.38	63.84	69.66	71.74	..
South Asia	40.91	44.74	50.34	52.80	55.18
India	39.61	43.84	50.46	53.04	55.36
Source: World Development Indicators and Global Development Finance 2011					

This structural transformation of the region has led to the reallocation of resources from traditional low productivity activities (agriculture) to modern high productivity activities (services). Reallocation of resources has resulted in an increase in the overall productivity and high growth (Figure 2).

Thus growth in South Asia has been driven by structural changes and the benefits of reallocation therein. There is still a huge productivity gap between agriculture and services in the region. Also, the size of agricultural sector (a low productivity activity) is huge in South Asia. Thus there is an ample scope for sustaining a service-led growth in South Asia, as resources will continue to reallocate from low productivity to high productivity sectors even during the crisis. The reallocation effect can benefit the South Asian economies because Table 4 shows that it has larger labor force as compared to the High Income Economies. Also, India alone accounts for more than 80% of the South Asias Labor Force.

Even though the productivity of services is higher than other sectors in South Asia, there is an enormous scope of catching up with developed countries. The crisis has not diminished the stock of global knowledge and South Asian economies can still benefit from them to raise their skill levels and reap the benefits of structural change and reallocation effects.

Table 4: Labor force, total

	1980	1990	2000	2005	2010
World	1883151427.60	2342918459.98	2756754643.82	2987870963.18	..
High income	409568242.42	462031264.74	504827166.87	528990806.76	..
Euro area	125807305.79	135904822.15	144813314.09	153885250.71	..
South Asia	324587250.20	415333353.36	514341651.90	573660813.63	..
India	251645217.10	317295318.74	387377809.40	426557833.09	..
Source: World Development Indicators and Global Development Finance 2011					

Catching up will drive the growth and not the rate of growth of advanced countries. Slowing down of growth in advanced countries can only have indirect impact on the growth of South Asia through the channels of trade and capital flows. The lower growth rate in advanced countries does not imply an automatic slowing of growth in developing countries. What matters for growth in South Asia is not the growth rate of the advanced countries but the difference between the income levels of the rich and South Asian economies. It is this convergence gap, which matters for growth and hence recovery (Rodrik, 2009). South Asia still faces a huge convergence gap with high income countries and it is the catching up which is going to drive growth even during the crisis and thereafter.

There is an ample scope for catch up in productivity for South Asian economies. Overall labor productivity is still very low in South Asia. Even though services have been a major driver of growth, the productivity of this sector is still too low compared to advanced economies. South

Asian countries have started from a low technological base compared to international best practice in services. It is the catching up phenomenon which has resulted in the rapid productivity growth in services in South Asia in last couple of years. Services have huge potential for productivity gains from learning, networking, and knowledge spillovers. Even though the growth in advanced countries has become low or even negative the pool of technological knowhow has not gone down in these economies. Since important factors which can potentially improve productivity of services sector remain unaffected by the crisis South Asian economies can continue to improve their productivity and hence grow.

Since there is a huge convergence gap between South Asia and advanced economies, the present crisis which is going on right now is not likely to hurt the growth prospects of South Asia. With suitable policies in place this could be used to stage a recovery and sustain growth.(Ghani and Anand,2009)

Table 5: GDP Growth (Annual %)

	1980	1990	2000	2005	2010
World	1.86	2.98	4.27	3.56	4.22
High income	1.34	3.19	4.03	2.64	3.09
Euro area	2.26	3.51	3.83	1.66	1.81
South Asia	6.45	5.43	4.28	8.73	8.83
India	6.74	5.53	4.03	9.32	9.72
Source: World Development Indicators and Global Development Finance 2011					

Table 6: Population, total

	1980	1990	2000	2005	2010
World	4434035156.73	5272353133.90	6079752533.80	6458364363.80	6840507002.54
High income	911571691.98	978884198.00	1049546481.62	1086778569.66	1127002177.75
Euro area	296150940.00	304708869.00	315014558.80	324202166.00	331675464.43
South Asia	894467635.50	1122835469.00	1359978470.50	1471800361.21	1579469720.12
India	687332000.00	849515000.00	1015923000.00	1094583000.00	1170938000.00
Source: World Development Indicators and Global Development Finance 2011					

Growth in the South Asian region has been significantly influenced by the specific policy decisions taken by each government. In particular, these economies entered an import-substitution phase and were characterized by significant state intervention in both financial and labour markets. In addition, these nations relied heavily on State owned enterprises and favoured regulation. The entrenchment of some of these policy decisions over time have resulted in delayed or stagnant levels of growth, which have been difficult to amend due to various political pressures.

Governments generally struck an appropriate balance between private and public action. A common error in South Asia and elsewhere was trying to do too much, not only providing public goods, but also run bakeries, mines, steel mills, hotels, and banks".

Another significant impediment to growth in South Asia throughout its post independent years has been the failure of governments to effectively govern in terms of both politics and economics. In particular, state powers have been highly concentrated in centralized regimes and corruption both in public and private sectors.

An ADB report says that improved governance, better quality of regulation and infrastructure can help South Asian economies emerge as the "New Tigers" of Asia. The banking sectors in South Asia have not only improved their performance over the recent past, but have also reduced the performance gap between themselves and other economies in Asia.

Analysis Country Wise

The GDP growth rate in South Asia registered an upward trend since 1970s through the first decade of the 21st century. The annual average growth rate increased to 8.8 per cent during 2009-10. However, all the countries have not experienced the same level and pattern of growth.

Table 7: GDP Growth Country wise (Annual %)

	1980	1990	2000	2005	2010
South Asia	6.4	5.4	4.3	8.7	8.8
Afghanistan	NA	NA	NA	14.5	NA
Bangladesh	0.8	5.9	5.9	6.0	5.8
Bhutan	NA	9.1	7.5	7.1	7.4
Maldives	NA	NA	4.8	-4.6	4.8
Nepal	-2.3	4.6	6.2	3.5	4.6
India	6.7	5.5	4.0	9.3	9.7
Pakistan	10.2	4.5	4.3	7.7	4.4
Sri Lanka	5.8	6.4	6.0	6.2	8.0

Source: World Development indicators and Global Development Finance 2011

It is interesting to note that some of the high growth countries (Pakistan) during 1960s and 1980s slipped down during 1970s and 1990s. Its growth rate varied between 6.3 per cent to 6.7 per cent during 1960s and 1980s. During 1970s and 2000-06, its growth rate was 4.7 per cent and 5.5 per cent, respectively.

Bangladesh, however, registered an upward trend since 1980s. Its growth rate rose from less than 4 per cent during 1970s and 1980s to nearly 5 per cent during 1990s. Its growth rate increased to 5.5 per cent during 2000-06.

India attained a remarkable success in its journey towards higher growth rate. Its growth rate during 1960s and 1970s was much lower than that of Pakistan. Even Bangladesh had an edge over India during this period. In fact, India's growth rate was almost around the average growth rate of South Asia.

Nevertheless, India started looking up during 1970s and achieved distinctively high growth rate (5.7 per cent annum) than that in the past. Its growth rate further rose to

5.9 per cent during 1990s and to 7.4 per cent during 2000-06. Its growth rate crossed 8 per cent and even touched 9 per cent during 2006-07 and 2007-08.

Thus, all the countries except Pakistan, displayed an upward trend in GDP growth rate during 1970s and through 1990s. Their growth rate during the first six years of the 21st century has also been quite high by South Asian and Global standards. Nepal experienced a lower growth rate during 2000-06. The global recession, since 2007, has certainly dampened the growth performance of these countries; though less severely than many other regions and countries of the world.(Ghuman and Bhullar, 2010)

Conclusion

South Asia has witnessed a growth miracle in the past five years. The growth rate has been exceptional by any standard. Globalization has accelerated growth in the region and contributed to poverty reduction. But the current global crisis may potentially change globalization itself, as developed countries adjust to global imbalances that contributed to the crisis. It appears that the three aspects of globalization - capital flows, trade flows, and economic management - may not be the same in the future. Trade flows will be diminished and exports may not be a powerful engine of growth as developed countries try to correct the imbalance by consuming less and saving more. Also, growth in the developed world is either negative or stagnant. Thus, the chances of external demand for traded goods picking up anytime soon are bleak. Capital flows are not likely to reach its pre-crisis levels in the short-term, and South Asia's rising public debt means there is less room for economic management, such as fiscal stimulus. In the words of Stiglitz "Improvements in education or health are not just means to an end of increased output, but are an ends in themselves" (Stiglitz, 1997, p. 19). "If a government reduces its fiscal deficit by cutting back vital investments in infrastructure or in human capital, growth may actually suffer" (Stiglitz, 1997, p. 29). Improved education and health are, thus, essential means of increasing GDP. South Asia has transformed itself from a region of primary products to a region of services virtually skipping the manufacturing stage. Quality of service exports from the region resemble that of developed countries. This unique trade and growth pattern of South Asia has important implications for the recovery of the region. Globalization of services is still at an early stage and they are likely to grow faster even during the crisis. Structural transformation and very high quality of service exports is likely to help the region sustain growth in the face of the present crisis.

Despite a shift towards market liberalization, South Asia continues to be overregulated. As a result, it is not fully realizing its growth potential. "Also In addition to increasing public and private spending on infrastructure, there is a need for better targeting of investments and in particular, for improvements in sector policies, governance, and institutional environment

South Asia stands at critical juncture today, where the potential for sustained high growth and poverty reduction is excellent. A unique opportunity exists to drastically reduce poverty over the next decade, provided the right choices are made.

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