



Opinion | Why economic freedom is important in India

September 26, 2018

The release of the Cato Institute and Fraser Institute's annual *Economic Freedom of the World* (EFW) report this week is a touch ironic. It comes days after a great deal of ink has been spilt on the tenth anniversary of Lehman Brothers' collapse. The global financial crisis that followed turned capitalism and free markets into four-letter words for many. The report is a timely reminder of their continued importance in a country like India.

There is a strong correlation between economic freedom and well-being. The EFW report finds that "Nations in the top quartile of economic freedom had an average per capita GDP [gross domestic product] of \$40,376 in 2016, compared to \$5,649 for bottom quartile nations" in terms of purchasing power parity in constant 2011 US dollar terms. Here's the important bit: In the top quartile, the average income of the poorest 10% was almost seven times the average income of the poorest 10% in the bottom quartile. Besides, there is a gulf of almost two decades in life expectancy of the nations in the top and bottom quartiles. Political and civil liberties and gender equality levels show similar divergence.

At its core, such freedom is about an individual's ability to act as a free economic agent making voluntary decisions and choices. The greatest enemy to this is poverty. Economic agency for the poor is a shabby thing. Their choices are too constrained for it to have much substance. India has made more progress against this kind of grinding poverty in the quarter century and change since liberalization started widening the scope of citizens' economic choices than in all the prior decades. By 2022, the number of Indians living in extreme poverty is expected to drop to 20 million, according to the Brookings Institution. This is startling progress seeing where India stood at the turn of the century.

Unsurprisingly, the EFW index reflects this, with the caveat that rankings and scores are crude means of pinning down such changes. India's overall ranking has dropped from 83 in 1990, when it stood on the cusp of liberalization, to 96 in 2016. This is due to expansion in the number of countries the index looks at, as well as the progress made by them. In terms of summary scores, though, India has made appreciable progress on some fronts—from the government vacating space for the private sector in various industries to monetary policy with the Reserve Bank of India adopting an inflation-targeting regime in 2015.

On too many fronts, however, it has stagnated. The EFW's conception of small government reflects a hard-nosed approach that can be reductive here, particularly in the context of a country

like India. An efficient government—one that draws down its intervention where it is distortionary and goes big where it needs to—is a better goal. The Indian state has made the wrong call too often. Judicial and law and order capacity, for instance, continue to lag. So do labour market regulations.

The index's transfer and subsidies category is particularly illustrative. India's score has barely budged between 1990 and 2016. Little wonder; while a trend towards direct benefits transfers is making subsidy regimes more efficient, the logic of the underlying policy decisions remains ruinous. The RBI, for instance, has noted on multiple instances that farm loan waivers don't work. They don't improve farm productivity, they reduce formal farm credit and they cause fiscal slippage. Yet, multiple state governments have gone big on this over the past couple of years. Meanwhile, they—and the Centre—refuse to step back when it comes to everything from stocking limits to export restrictions and monopoly procurement, although doing so would make their waiver munificence unnecessary.

On property rights, likewise—the backbone of a market economy—the scores indicate insufficient progress. That said, the United Progressive Alliance government's National Land Records Modernization Programme, which the National Democratic Alliance government has folded into its Digital India push, is a move in the right direction. Indeed, state governments are doing some of the most interesting work here from Karnataka's Bhoomi Project to Rajasthan's Urban Land (Certification of Titles) Act, 2016. And the Andhra Pradesh government's push to use blockchain technology for preventing property fraud has perhaps the most potential of the lot.

The EFW report notes that support for free markets has been dipping across the world from well before the financial crisis—since their late 20th century heyday, in fact. This is not particularly surprising. When the benefits of an economic system become baked into it, they can be hard to see. The missteps, meanwhile—from declining labour shares of income to the threat of increasing monopoly power—have come increasingly into prominence. They should be addressed, certainly. But the Indian experience shows how foolish it would be to underestimate the importance of free markets and the economic freedoms they underwrite.