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Why no applause for 138 million exiting poverty?

By SA Aiyar – July 28th, 2013

When China reduced people in poverty by 220 million between 1978 and 2004, the world applauded this as the greatest poverty reduction in history. Amartya Sen, Joseph Stiglitz and all other poverty specialists cheered.

India has just reduced its number of poor from 407 million to 269 million, a fall of 138 million in seven years between 2004-05 and 2011-12. This is faster than China's poverty reduction rate at a comparable stage of development, though for a much shorter period. Are the China-cheerers hailing India for doing even better?

No, many who hailed China are today rubbishing the Indian achievement as meaningless or statistically fudged. This includes the left, many NGOs and some TV anchors. The double standard is startling.

The Tendulkar Committee determined India's poverty definition. The Tendulkar poverty line in 2011-12 came to Rs 4,000 per rural and Rs 5,000 per urban family of five. Critics say this is ridiculously low. But it is roughly equal to the World Bank's well-established poverty line of $1.25 per day in Purchasing Power Parity terms (which translates into around 50 cents/day in current dollars). This is used by over 100 countries, by the United Nations and many other international agencies. When the whole world uses this standard, why call it statistical fudge?

When China claimed to have lifted 220 million people out of poverty, guess what its poverty line was? Just $85 per year, or $0.24 per day! Whatever statistical adjustments you make for comparability, it was far lower than today's Tendulkar line. Did today's critics of the Tendulkar line castigate China for fudging? No, they sang China's praises.

The World Bank actually has two lines — $1.25 denoting extreme poverty, and $2 denoting moderate poverty. India can also adopt two lines, the Tendulkar line for extreme poverty and a new Rangarajan line for moderate poverty, at around $2/day.

But this will in no way diminish the great achievement of slashing the number of those historically called poor — we can call them the "extreme poor"— by 138 million in seven years. Allowing for rising population in this period, the number saved from extreme poverty is even higher at 180 million.

Given our rising GDP and expectations, we can rename the Tendulkar line as our extreme poverty line. But to condemn it as statistical fudge is ridiculous. The $1.25 line is a world standard, even if it is below the Arnab Goswami line or Sitaram Yechhury line. Indian critics may not accept it, but the world will.

There is, of course, the separate issue of who should be entitled to various government subsidies, including food subsidies. Economists talk of targeting subsidies at those below the Tendulkar line. But for politicians, the aim of subsidies is to win votes. And clearly you win more votes by extending subsidies to two-thirds of the population, rather than the poorest one-third.

This spread of subsidies to those above the extreme poverty line was once called “leakages to the non-poor.” But it is considered good politics even if it is bad economics. This explains why the government chose to cover 67% of the population in the Food Security Bill, even though the poverty ratio at the time was 30%.

However, critics quickly exposed this as a double standard. They asked, if your Food Security Bill views two-thirds of the people as needy, how could you have a poverty line saying only one third are poor? The government found it difficult to say this was good politics even if it was bad economics. Instead, it appointed the Rangarajan Committee to devise a higher poverty line. This line will almost certainly be around the moderate poverty line ($ 2/day in PPP terms) of the World Bank.

Many critics and TV anchors will cheer at the prospect of freebies to two-thirds of the population. Yet here lie the seeds of fiscal disaster. India is poor because it has spent too much on ill-targeted subsidies, leaving too little for infrastructure and effective education that will raise incomes permanently. Total subsidies (mostly non-merit subsidies) exploded in the 1980s, reaching 14.5 % of GDP, almost as much as all central and state tax revenue. This ended in a fiscal and balance of payments crisis in 1991.

The risk of a new poverty line of $2/day is that it will create political demands for more freebies to two thirds of the population. That will further erode limited funds for productive spending.

In theory we can limit subsidies to the poorest and cut out unworthy subsidies. In practice, the combined pressure of vote banks and TV anchors threatens to raise subsidies beyond all prudent limits. There lie the seeds of another 1991-style disaster.