Syllabus subtopic: Indian Economy and issues relating to planning, mobilization of resources, growth, development and employment.

Prelims and Mains focus: about Middle Income Trap; why is India facing it; about GNI

News: Many economists believe that countries that grow from low-income to middle-income levels tend to get stuck in a trap that prevents them from graduating to high-income status. **India runs the risk of getting caught in that trap.**

**What is the middle-income trap?**

World Bank defines a **middle-income country** as one with a gross national income (GNI) per capita of $1,000-12,000 in 2011 prices.

Those **below the $4,000 mark** are “**lower middle-income**” countries, and those **above it “upper middle-income”** ones. The **middle-income trap** refers to the phenomenon where rapidly growing economies graduate to the middle-income tier but then stagnate. They get squeezed from below by intense competition from lower-cost competitors while failing to transition to high-income levels for a **variety of reasons—especially a failure to build institutional, human and technological capital.**

**Which countries have escaped it?**

In the history of development, the **success stories of transformation** to high-income status include **Japan, South Korea, Portugal, Poland and Latvia.** Countries such as Brazil, South Africa, Egypt, Thailand and Turkey also tried to develop but could not transition to the high-income level. These countries failed to develop and remain stuck below their potential. Argentina, Mexico, and Russia, meanwhile, have been trapped in the upper middle-income category for a long time. China, with a GNI per capita of around $9,800, is most likely on its way out of the middle-income trap—unless it stumbles.
How has India moved up the development ranks?

In 1960, India had a per capita income of $1,033 (in 2011 purchasing power parity terms). This was equivalent to 6% of the per capita income of the US. India attained lower middle-income status in 2008. By 2017-18, the country’s per capita income was $6,538—or 12% of the per capita income of the US.

Is India caught in the middle income trap?

Rathin Roy, a former member of Prime Minister Narendra Modi’s economic advisory council, has cautioned that India runs the risk of getting caught in the middle-income trap. According to him, the country’s growth has mostly been driven by demand generated by the richest 100 million Indians. However, as this demand cannot keep growing infinitely, a failure to broaden the income base—and, therefore, the demand base or the market size—could act as a growth barrier, resulting in India slipping into a middle-income trap.

Is India’s market too small?

Inequality is a barrier to the broadening of the demand base in an economy. Even at $2.7 trillion, India’s GDP is relatively small—it’s about the size of California’s GDP. China’s is over 4 times as large. The 2017 Economic Survey warned that four factors could hurt India:

- hyper-globalization repudiation,
- thwarted/impeded structural transformation,
- human capital regression due to technological progress, and
- climate change-induced agricultural stress.

Following are the measures of National Income:

1. Gross Domestic Product (GDP):
   - GDP is the final value of the goods and services produced within the geographic boundaries of a country during a year.
   - GDP growth rate is an important indicator of the economic performance of a country.
   - The gross domestic product (GDP) is one of the primary indicators used to
gauge the health of a country’s economy

- In India, contributions to GDP are mainly divided into 3 broad sectors – agriculture and allied, industry and service sector.

2. **Net domestic product (NDP):**

- The net domestic product (NDP) equals the gross domestic product (GDP) minus depreciation on country capital goods.
- \[ \text{NDP} = \text{GDP} - \text{Depreciation} \]

3. **Gross national product (GNP):**

GNP is an estimate of the total value of all the final products and services produced in a given period by the means of production owned by a country’s residents.

4. **Gross National Income (GNI):**

- Gross national income is a measurement of a country’s income. It includes all the income earned by a country’s residents and businesses, including those earned abroad.
- GNI measures all income of a country’s residents and businesses, regardless of where it’s produced.
- Gross domestic product (GDP), on the other hand, measures the income of anyone within a country’s boundaries, regardless of who produces it.

**Difference between GNI and GNP**

- GNI measures income earned, including that from investments that flow back into the country. Gross National Product (GNP) includes the earnings from all assets owned by residents.
- It even includes those that don’t flow back into the country.
- It then omits the earnings of all foreigners living in the country, even if they spend it within the country.

**Calculation of GNI and NNI:**

**GNI (calculated from GDP) = GDP + (income from citizens and businesses earned abroad) – (income remitted by foreigners living in the country back to their home countries).**
GNI (calculated from GNP) = GNP + (income spent by foreigners within the country) – (foreign income not remitted by citizens).

Net National Income (NNI) = GNI - Depreciation = NDP + (income from citizens and businesses earned abroad) – (income remitted by foreigners living in the country back to their home countries).