# Why the Poor Have not Done as Well as the Rich in New India

*by Parth J. Shah*

"The rich are getting richer and poor are getting poorer!" is now a common refrain in India in any discussion on economic reforms. Since 1991, India has undergone a great deal of liberalization both internally through market reforms, and externally by opening up to competition from the outside world. Many feel that the gains of this liberalization and globalization have not accrued to the poor.

## Unequal distribution of economic freedom

One can dispute this charge by pointing out that according to World Bank data, the proportion of the population in India below the poverty line[1] has declined from 36 percent in 1994 to 28 percent in 2000, the latest year for which this data is available. Nonetheless, I agree that the poor have not gained as much as they could have in the new India. But it is not because the rich have taken from the poor, as commonly implied. The reason is simple: the areas in which the middle and upper classes make their living have seen the highest degree of liberalization, while the areas in which the poor earn their livelihood have seen the fewest reforms.

Economic freedom for the rich has increased but it has not for the poor. In The Fraser Institute's *Economic Freedom of the World: Annual Report 2006*, India's rank has improved from 80 in 1990 to 53 in 2004. This overall increase in economic freedom has not been the same across all classes (for details, see Shah, 2004).

The poor still live under the draconian "license-permit-quota raj," as the system of extensive government intervention in India is known. Today, setting up a factory or a call center requires no government license. But anyone wanting to run a tea stall, or to become a street hawker, or a cycle-rickshaw puller, or to work as a railway porter requires a license. For entry-level professions that need low skills and little capital, licenses are still mandatory.

*A rich man's capital can work 24 hours a day, but a poor man's capital cannot.*

The industrial entrepreneurs now have economic freedom, but the street entrepreneurs do not. A vast majority of street entrepreneurs operate without a license—illegally, informally. They are open to constant harassment and extortion by the police and municipal officers.

## The license raj on street entrepreneurs

Consider cycle-rickshaw pullers and street vendors in the cities and towns of India. Delhi has approximately 500,000 cycle-rickshaws providing an affordable and accessible transportation service to the poor. The Municipal Corporation of Delhi has mandated that rickshaws have to be licensed and only 99,000 licenses shall be given out. More than 80 percent of the cycle-rickshaws are illegal. Studies suggest that on average, a bribe of Rs 200 (Can $5) per month per cycle-rickshaw is paid. Even the licensed rickshaws have to pay up (see Shah and Mandava, eds., 2005). The government functionaries extort Rs 10 million a month from the cycle-rickshaw pullers! Similarly, Delhi's approximately 600,000 street vendors operate without the necessary license and pay up about Rs 12 million per month in bribes. This is the burden of the license-permit raj—of economic unfreedom—on the poorest of the poor in Delhi.

During municipal raids, which occur regularly on a weekly or monthly basis,

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all the goods, hand carts, weighing balances and other equipment, as well as rickshaws are impounded. Once the rickshaw is seized, it takes 5 to 15 days and more bribes to get it released. During these days, the puller loses his means of earning his livelihood. Because of the constant threat of raids, the street hawkers are unable to expand their business. If the hawkers expand by acquiring more goods to sell, they won't be able to grab them quickly and run when the police van arrives. The hawker can expand his business only and literally to within arm's reach. No wonder that India's urban poor are still earning a subsistence living. The areas in which they earn their living lack liberalization.

## Well-intentioned laws and the poor

In addition to the stifling licensing system, myriad rules and regulations create further hurdles. Many of these rules are well-intentioned, but the outcomes are perverse, just as the Law of Unintended Consequences predicts. Delhi has a law that the owner and the driver of a cycle rickshaw must be the same person. Renting rickshaws is illegal. The law's intention is to promote ownership and to limit exploitation of rickshaw pullers by people who would buy multiple rickshaws and rent them out. But what about a migrant who does not have enough money to buy a rickshaw and does not have any other skills? Many migrants are seasonal; they come to the city during the non-agricultural season, earn some cash, then go back to work on the farm. Obviously there is demand for rental rickshaws, and the suppliers are easy to find. The rental charge, however, includes a premium for the risk of running an illegal business. Supply of rental rickshaws is limited since honest people do not enter this business. Not surprisingly, then, a five-month rickshaw rental costs the same as a new rickshaw. Is this artificially higher rent good for the rickshaw puller?

Equally importantly, when a poor migrant somehow buys a rickshaw, what happens when he has to go back to his village for a few months? He cannot rent out his rickshaw. A person can ply a rickshaw for 10-12 hours a day. He cannot rent the vehicle out for the rest of the day. A rich man's capital—a call center—can work for 24 hours a day, but a poor man's capital—his rickshaw—cannot. If he falls sick, his rickshaw must lie idle. It is the only business he knows, yet he cannot grow it. His earnings are forever limited to what he can earn from one rickshaw with his own labour. Yet people wonder why he is poor!

## The rural poor with no agricultural reforms

The rural poor who earn their living in agriculture fare no better. Agriculture is the area that has seen the least reforms. Much agricultural produce cannot be transported across district lines, let alone across the state or the country. India does not even have a common market in agricultural produce. A law in the state of Maharashtra requires farmers to sell their sugar cane to a specified sugar mill in the district. In Kerala, the law mandates that once a farm is registered as producing one crop, it cannot change its crop without government permission! Recently, farmers who had planted sugar cane instead of rice saw their crop uprooted by unionized workers. Rice and sugar cane farm workers belong to different unions. The Essential Commodities Act considers agricultural produce so essential that it has condemned its producers to perpetual poverty through a multitude of inane restrictions.

The urban and rural poor of India are unenthusiastic about liberalization, not because it is making them poorer as some claim, but because they have not seen much liberalization in their means of livelihoods. We must do for them what we have done for the rich: give them freedom in their livelihoods.

## Lifting the poor: the livelihood freedom test

The Indian government's first step must be to remove all employment hurdles by applying the Livelihood Freedom Test. Assess all existing rules and regulations to determine their impact on people's freedom to earn an honest living. Does any law restrict opportunities for any person to earn a living, particularly in a profession that requires little capital or skills? If so, then review, revise, or remove those laws. When these restrictions are removed, economic growth will not only increase genuine employment, but will also be more balanced in offering opportunities to all classes in the society.

## Note

[1] In India, poverty is determined according to whether or not a person gets 2,400 calories per day (see National Sample Survey Organization).

## References

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