



World Development Report 2024

For Prelims: [World Bank](#), [European Union](#), [Digitalization](#), [Gross Domestic Product](#), [Gini index](#), [Inflation](#), [Digital Public Infrastructure](#), [Green hydrogen](#), [Renewable Energy](#), [Production Linked Incentive Scheme](#), [International Monetary Fund](#)

For Mains: World Development Report 2024, Global Economic Impact, Indian Economy and Middle Income Trap

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Why in News?

A recent [World Bank](#) report titled "**World Development Report 2024: The Middle Income Trap**" has highlighted significant challenges faced by over 100 countries, including India, in achieving high-income status in the coming decades.

What are the Key Highlights of the World Development Report 2024?

▪ Middle Income Trap:

- India is among 100 countries, including China, at risk of falling into the "**middle income trap**," where countries struggle to transition from **middle-income to high-income status**.
 - India is at a crucial juncture, benefiting from favorable demographics and advancements in [digitalization](#), but faces a tougher external environment compared to the past.
 - [India's aim to become a developed nation by 2047](#) requires a comprehensive approach that enhances overall economic performance, rather than focusing on isolated sectors.
- The report notes that only **34 middle-income economies have transitioned to high-income status since 1990**, often due to special circumstances like [European Union](#) integration or [oil reserves](#).
- Middle-income countries face challenges in **sustaining economic growth due to diminishing returns** on physical capital.
 - While low-income countries benefit from building physical capital and improving basic education like India in the 1980s, where capital deepening was crucial, middle-income countries encounter **diminishing returns as they invest further**.
 - Simply increasing **saving and investment rates to meet growth targets isn't sufficient**; these countries also need to address factors beyond physical capital.
 - Despite having relatively high capital endowments, **middle-income economies struggle with productivity issues**, highlighting that physical capital alone isn't the main barrier to further growth.
- The World Bank criticizes many middle-income countries for using outdated economic strategies focused mainly on expanding investment.

▪ Global Economic Impact:

- Middle-income countries are home to six billion people, **representing 75% of the global population, and generate over 40% of global Gross Domestic Product (GDP).**
 - The success or failure of these countries in achieving high-income status will significantly impact global economic prosperity.
- **Per Capita Income Disparity:**
 - India is identified as the fastest growing major economy, but it would take **75 years for its per capita income to reach a quarter of the US** income levels if current trends continue.
 - China would take over 10 years, Indonesia nearly 70 years, and India 75 years to reach a quarter of US income per capita.
- **Challenges and Risks:**
 - Middle-income countries face significant obstacles, including **ageing populations, rising debt, geopolitical and trade frictions, and environmental concerns.**
 - These countries are at risk of not achieving reasonably prosperous societies by the middle of the century if they continue with current trends.
- **Strategic Recommendations:**
 - **3i Strategy:** Report recommended a three-phase approach for countries to reach high-income status:
 - **1i Phase:** Focus on investment for low-income countries.
 - **2i Phase:** Investment and infusion of foreign technologies for lower-middle-income countries.
 - **3i Phase:** Investment, infusion, and innovation for upper-middle-income countries.
 - The report highlighted **South Korea** as an example, starting with a per capita income of **USD 1,200 in 1960, South Korea reached USD 33,000 by 2023 by sequentially adopting the 3i strategy.**
- **Policy Recommendations:**
 - India's aim to become a developed nation requires a comprehensive approach that enhances overall economic performance, **rather than focusing on isolated sectors.**
 - Focus on horizontal policies rather than vertical debates (e.g., manufacturing vs. services).
 - Emphasize **improving education and skills** to enable better absorption of technology and innovation.
 - Strengthen connections between **universities and industries to enhance knowledge transfer.**
 - India shows potential in technology preparedness, with a good track record in digitalization. However, there is a need for greater dynamism in firms to **absorb and utilize these technologies effectively.**
 - The report highlights the prevalence of **microenterprises in India**, suggesting that barriers exist for **productive firms to grow due to policies favoring smaller firms.**

What is the Middle Income Trap?

- The middle-income trap refers to a **situation where a country, after reaching a middle-income status, struggles to transition to high-income status.**
 - This typically happens when **economic growth slows down after an initial period of rapid progress**, and the country remains stuck at a middle-income level without advancing further to high-income levels.
- According to the World Bank, the Middle Income Trap refers to the economic stagnation that countries encounter when their GDP per capita reaches about 10% of the United States level, or around USD 8,000 currently.
- Low-income countries often experience rapid growth when transitioning to middle-income levels due to factors such as low wages, cheap labor, and basic technology catch-up.
 - At the middle-income stage, countries **may face stagnation due to exhaustion of initial growth drivers**, institutional weaknesses, income inequality, and lack of innovation.
- **Current Status:** By the end of 2023, 108 countries were classified as middle-income, with GDP per capita between USD 1,136 and USD 13,845.
 - These countries house 75% of the global population and generate over 40% of global GDP, contributing to more than 60% of carbon emissions.
 - Until 2006, the **World Bank categorised India as a low-income nation.** In 2007,

India **transitioned to the lower-middle income group** and has remained in that classification since then.

- Economists view that India's growth has been sluggish at lower-middle-income levels, with per capita income stuck between USD 1,000 and USD 3,800. Emphasized that India's growth has been driven primarily by the top 100 million people and warned that this model might not be sustainable.

What Challenges Must India Overcome to Improve the Income Status?

- **Income Inequality:** India continues to grapple with high levels of consumption inequality, with a **Gini index of around 35 over the past two decades**. This inequality limits broad-based economic growth and hinders inclusive development.
 - Although India made significant strides in reducing extreme poverty between 2011 and 2019, the **pace of poverty reduction has slowed**, especially post the Covid-19 pandemic. This indicates ongoing struggles to address deep-seated economic disparities.
- **Balancing Growth and Inflation:** **Higher interest rates**, aimed at controlling **inflation**, can temper demand and impact economic growth. India needs to manage monetary policy effectively to balance growth with inflationary pressures.
 - Strategic fiscal management is crucial to support growth without exacerbating inflation.
- **Income Per Capita:** **India's per-capita income** is significantly below the upper-middle-income threshold of USD 4,256. Achieving high-income status will require substantial growth in per-capita income over the coming years.
 - Although India is projected to approach the **USD 7 trillion economy milestone by FY31**, it must sustain a 6.7% average annual growth rate to reach this target and transition to an upper-middle-income status.
- **Labor Force Participation:** Despite improvements in employment indicators, concerns remain about the **quality of jobs, real wage growth, and the low participation of women in the labor force**.
 - These issues affect the overall economic productivity and inclusivity of growth.
 - The **Economic Survey 2023-24** notes that India needs to generate an average of nearly **78.5 lakh non-farm jobs annually until 2030** to cater to the rising workforce.
- **Economic Diversification:** While **mining, manufacturing, construction, and services are key growth drivers**, India must ensure continued diversification to avoid over-reliance on any single sector.
 - India aims for the manufacturing sector to contribute beyond 20% of GDP by FY31. Sustaining this growth will depend on **increasing global competitiveness, enhancing value chains, and supporting green transitions**.
- **Environmental and Climate Resilience:** India's aspiration to achieve high-income status by 2047 **must align with its goal of net-zero emissions by 2070**.
 - Balancing economic growth with climate resilience is a complex challenge, requiring significant investments in **green technologies and sustainable practices**.
 - The country must ensure that its growth path is resilient to climate impacts while delivering broad-based benefits to its population.

What are the Factors Supporting India's Improvement in Income Status?

- **Global Offshoring:** Increased outsourcing of services such as software development, customer service, and business process outsourcing to India.
 - Acceptance of work-from-home and work-from-India models, potentially **doubling employment in outsourced jobs to over 11 million by 2030** as global spending on outsourcing is expected to grow from USD 180 billion annually to around USD 500 billion by 2030.
- **Digitalization:** **India's Aadhaar program** and **IndiaStack (Digital Public Infrastructure)** are driving a digital transformation, enabling greater financial inclusion and credit access.
 - **India's credit-to-GDP ratio could rise from 57% to 100% in the next decade**, and consumer spending is expected to more than double from **USD 2 trillion to USD 4.9 trillion, with the greatest gains in non-grocery retail**.
- **Energy Transition:** Significant investment in **renewables** such as **biogas, ethanol, Green hydrogen, wind, solar, and hydroelectric power**.

- Daily energy consumption is expected to increase by 60%, **reducing reliance on imported energy and improving living conditions.**
- The energy transition creates new demand for **electric solutions, driving investment growth and a virtuous cycle of investment, jobs, and income.**
- **Manufacturing Sector:** Corporate tax cuts, investment incentives, and infrastructure spending are driving capital investments.
 - **Manufacturing's share of GDP** is projected to increase from 15.6% to 21% by 2031, potentially doubling India's export market share.
 - India continues to open its economy to global investors **by raising Foreign Direct Investment limits**, removing regulatory barriers, developing infrastructure and improving the business environment.
 - India's 14 **Production Linked Incentive Scheme** have the potential to significantly boost production, employment, increase manufacturing activities, and contribute to economic growth over the next five years, thereby having the potential to change the manufacturing ecosystem in the country.
- **Services Sector:** **Services sector** is expected to grow at 6.9% between fiscals 2025 and 2031. Services will continue to be the dominant driver of India's growth.
- **Economic Size:** Potential doubling of GDP from USD 3.5 trillion to over USD 7 trillion by 2031.
 - **Bombay Stock Exchange** expected to grow at 11% annually, reaching a market capitalization of USD 10 trillion by 2030.
 - Projections indicate that **India will become the world's third-largest economy by 2031.**
 - According to the International Monetary Fund (IMF), India's current GDP per capita is around USD 2,850, placing it in the lower-middle-income category. However, CRISIL's report projects India's GDP per capita to reach USD 4,500 by 2031.
- **Consumption and Income Distribution:**
 - Rising income levels can lead to a significant increase in overall consumption.
 - Increased per capita income and economic growth will boost domestic consumption.
 - Consumer Spending is expected to more than double from USD 2 trillion in 2022 to USD 4.9 trillion by the end of the decade, with notable gains in non-grocery retail, leisure, and household goods.

What Strategies Should India Adopt to Avoid the Middle-Income Trap?

- **Address Income Inequality:** Implement policies to **ensure a more equitable distribution of wealth.** This could include progressive taxation, increased social spending, and targeted subsidies for the lower-income segments.
 - **Strengthen social safety nets** and support systems to reduce the disparity between different income groups and regions.
- **Enhance Economic Diversification:** Focus on diversifying the economy beyond traditional sectors. Invest in **emerging industries such as technology, renewable energy, and advanced manufacturing.**
 - Encourage development in **economically lagging regions to prevent over-reliance on certain areas** and spread economic benefits more evenly.
- **Increase Productivity and Innovation:** Foster innovation through investments in research and development, and support tech-driven industries to enhance productivity.
 - Focus on improving education and skills to meet the demands of a modern economy. Emphasize vocational training and higher education.
- **Support Local Manufacturing and Production:** Encourage local manufacturing through policies such as the PLI schemes. This can help make essential goods more **affordable and competitive.**
 - Tap into local skills and resources by promoting manufacturing in states with potential but lower costs. This approach can also address regional disparities and unemployment.
- **Foster Inclusive Growth:** Ensure that the production and distribution of essential goods like food, **healthcare**, and education are prioritized, making them affordable for all segments of the population.
 - Implement policies that create job opportunities and improve living standards across different regions and communities.
- **Strengthen Economic Institutions and Governance:** Improve the efficiency and

transparency of economic institutions to reduce corruption and ensure that resources are used effectively.

- Undertake structural reforms to streamline regulations, ease the business environment, and attract investment.

▪ **Focus on Sustainable Development:** Align economic growth strategies with **environmental sustainability goals**. Invest in green technologies and ensure that development does not compromise environmental health.

- Develop strategies to **mitigate the impacts of climate change and build resilience in vulnerable sectors**.

▪ **Promote Financial Inclusion:** Enhance financial inclusion by improving access to credit and financial services for small businesses and individuals in underserved areas.

- Leverage digital platforms to increase financial inclusion and improve the efficiency of financial transactions.

World Bank

- The World Bank, created in 1944 was established at the **United Nations Monetary and Financial Conference in Bretton Woods**, New Hampshire in 1944 as the **International Bank for Reconstruction and Development (IBRD)**, along with the International Monetary Fund (IMF).
- The IBRD later became the World Bank. The World Bank Group is a global partnership of **five institutions working for sustainable solutions to reduce poverty and build shared prosperity in developing countries**.
- The World Bank is one of the [United Nations'](#) specialized agencies and has **189 member countries, including India**.
- **Five Development Institutions of World Bank:** International Bank for Reconstruction and Development (IBRD), International Development Association (IDA), International Finance Corporation (IFC), Multilateral Guarantee Agency (MIGA), International, and Centre for the Settlement of Investment Disputes (ICSID).
 - **India is not a member of ICSID** but has been accessing funds from the World Bank (mainly through IBRD and IDA) for various development projects. **India is one of the founding members of IBRD, IDA and IFC.**
- **Major Reports:** [Ease of Doing Business \(Stopped publishing\)](#), [Human Capital Index](#), [World Development Report](#), and [Global Economic Prospect \(GEP\) Report](#).

Drishti Mains Question:

Q. Evaluate the criticism by the World Bank on outdated economic strategies used by many middle-income countries. What alternative strategies should India adopt to avoid the middle-income trap?

UPSC Civil Services Examination, Previous Year Questions (PYQs)

Prelims

Q. With reference to 'IFC Masala Bonds', sometimes seen in the news, which of the statements given below is/ are correct? **(2016)**

1. The International Finance Corporation, which offers these bonds, is an arm of the World Bank.
2. They are the rupee-denominated bonds and are a source of debt financing for the public and private sector.

Select the correct answer using the code given below:

- (a) 1 only
- (b) 2 only
- (c) Both 1 and 2
- (d) Neither 1 nor 2

Ans: (c)

Q. India's ranking in the 'Ease of Doing Business Index' is sometimes seen in the news. Which of the following has declared that ranking? **(2016)**

- (a)** Organization for Economic Cooperation and Development (OECD)
- (b)** World Economic Forum
- (c)** World Bank
- (d)** World Trade Organization (WTO)

Ans: (c)

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