Indian Economy · GS - III

Define potential GDP and explain its determinants.

What are the factors that have been inhibiting India from realizing its potential GDP?

EXAM YEAR	PAPER	SUBJECT
2020	GS - III	Indian Economy

MARKS	WORD LIMIT
10	~150 words

Answer Hint

Potential GDP; productive capacity; labour productivity; capital formation; human capital; technology; infrastructure; investment constraints; structural bottlenecks; economic reforms

Model Answer

Introduction

Potential GDP is the level of output an economy can sustainably produce when its labour, capital and technology are utilised at normal, sustainable rates, without generating persistent inflationary pressure.

Determinants of potential GDP

- **Labour force:** Population structure, labour-force participation and workforce skills determine productive capacity.
- **Capital formation:** Investment in machinery, factories, infrastructure and equipment expands output capacity.
- **Human capital:** Education, healthcare and vocational training improve worker productivity.
- **Technology:** Innovation, research and digital adoption raise efficiency and total factor productivity.
- **Institutions:** Regulatory certainty, contract enforcement and effective governance encourage investment.
- **Infrastructure:** Reliable electricity, transport, logistics and communication reduce production costs.

Factors inhibiting India

- **Low labour productivity:** Skill gaps and limited access to quality education constrain workforce efficiency.
- **Insufficient private investment:** Policy uncertainty, weak demand and financial constraints can discourage capital expenditure.
- **Infrastructure bottlenecks:** Logistics costs, congestion and unreliable services raise business expenses.
- **Employment challenges:** Informality, underemployment and low female labour-force participation limit productive capacity.
- **Agricultural dependence:** Low farm productivity and disguised unemployment constrain structural transformation.
- **Research and innovation gaps:** Limited research intensity and uneven technology adoption slow productivity growth.
- **Credit constraints:** Financial stress and restricted access to finance affect small enterprises.

Conclusion

India can raise potential GDP through productive investment, employment-intensive growth, better skills, infrastructure development, innovation and predictable regulation. Sustainable productivity improvements are more important than temporary increases in demand alone.

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