

How does Caste Affect Entrepreneurship?

Birth vs Worth

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Introduction

- Huge **TFP differences** across countries, Hall & Jones (1999).
- **Misallocation** seems to be an important factor. Banerjee et al. (2005) & HK (2009)
 - Financial frictions, Government policies - eg: size dependent policies, Informational frictions & Adjustment costs
- No Systematic evidence on the role of informal institutions.
 - This paper evaluates the effects of the **caste system in India**

Caste & Misallocation

- **Extensive margin**: low caste, can not enter the market.
 - **Intensive margin**: those who enter, can not access capital.
 - High caste controls much of the Capital & Wealth.
 - Top 30 traded firms (sensex) owned or run by high caste (OTH). 2012-46 Billionaires in India but none is low caste (LC).
- "Dalits (LC) are second to none as far as intelligence and entrepreneurship is concerned. We only have to give them an opportunity,"
- (J J Irani, Director, Tata Sons)

Main Results: Stylized Facts

- **Fact 1**: low caste are **less likely to enter** entrepreneurship but **more productive**(TFPR, profit) on average.
- **Fact 2**: low caste have **lower K/L** ratio but higher returns to capital than high caste.
 - These differences converge over age and size.
- **Fact 3**: caste-dependent component represents 1-25% of the total misallocation.
 - Caste-dependent misallocation **higher** " in regions with "**stronger** caste system.

Main Results: Model

- Dynamic stochastic GE model:
- Each period agents make their occupation decision.
 - Caste dependent fixed costs and financial constraints.
- Calibration:
- Match entrepreneurship rates => fixed-costs
 - Credit-gdp ratios => degree of financial friction
- Outcomes:
- LC face higher fixed costs (80%) and lower borrowing limits (22%).
 - Such asymmetries implies a 2.54% & 6% lower TFP & GDP.
 - Intensive margin => 40% & Extensive margin => 60%.

Table: Share of Population and Non-agricultural Enterprises across castes

Caste	Population	Enterprises	Enterprises with		
			One employee	Outside labor	Employment
LC	24%	13%	14%	10%	11%
MC	43%	43%	44%	10%	39%
OTH	33%	44%	42%	50%	50%

Notes: The enterprise ownership rates are computed with non-agricultural enterprises in the Economic census 2005. The population statistics for low caste and middle caste are drawn from Census 2001 and National Sample Survey 66th Round 2009-10. Outside labor means labor outside the household.

Figure: Capital intensity & MRPK across sectors: 2006

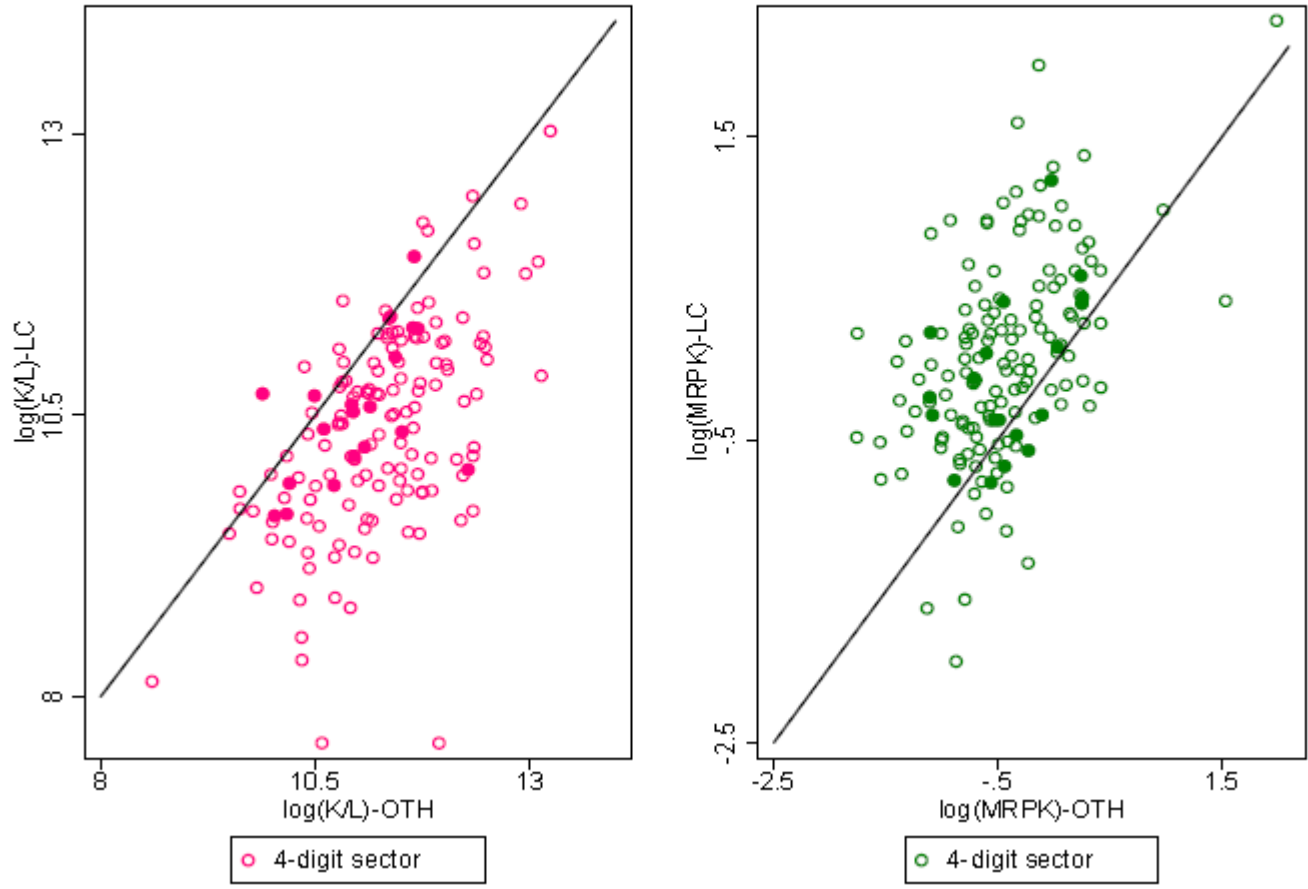
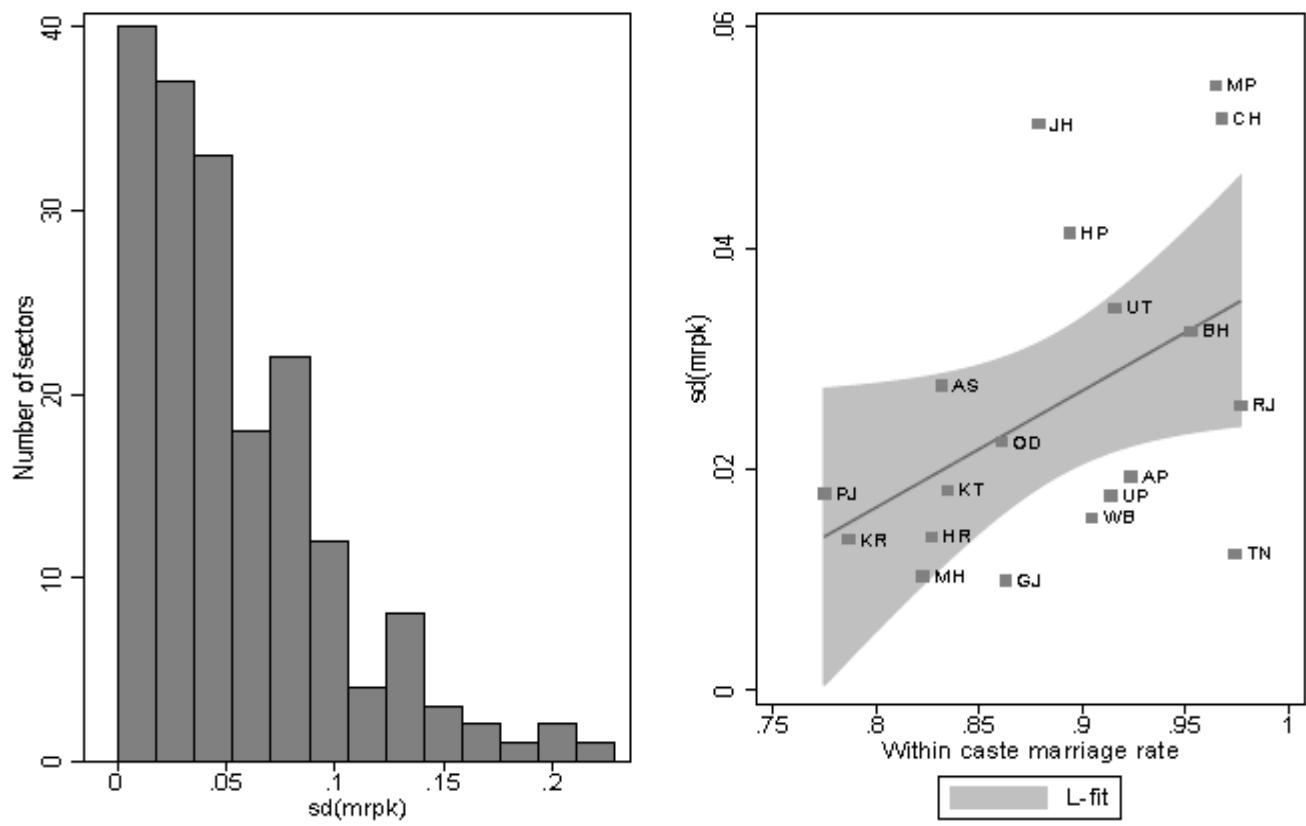


Figure: Caste-dependent misallocation of capital: 2006



Conclusion:

- Caste dependent misallocation is substantial and lowers **the Income per capita by 6%** in India.
- Such distortions widen the across caste **inequalities in consumption** and wealth.
- Also **lowers the scale** of operation of the average firm in the economy.