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<https://escholarship.org/uc/item/1dp7s36h>

Journal

Economic and Political Weekly, 50(18)

ISSN

0012-9976

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Publication Date

2015-05-02

Peer reviewed

Reflections on Indian Political Economy

The economic growth fundamentals for India are potentially quite strong (stronger than it seemed in 1984).

- Domestic saving and investment rates are relatively high for a poor country
- After the opening of the Indian economy the alacrity with which part of hitherto protected Indian business adapted to the demands of global competition and thrived suggests a remarkable resilience
- Vigorous entrepreneurial spirit in all corners of the economy, rejuvenated by the infusion of business entries from hitherto subordinate castes and regional capitalists
- The majority of the population is quite young, with thus the potential of a large and productive young work force
- With better transport and communication (particularly with the remarkably fast spread of mobile phones), connectivity is increasing in a way that is likely to speed up enhancement of productivity

But there are major structural and institutional problems blocking the full realization of these strong growth fundamentals:

- **Weak physical infrastructure (roads, electricity, ports, railways, etc.)**
 - ✓ **Public budgets laden with heavy subsidies and salaries and bad loans in public banks keep very little for infrastructure investment**
 - ✓ **Public-private partnerships on infrastructure have been saddled with problems of opportunism, corruption, non-transparent regulations and mismanagement**
 - ✓ **Caught in the cross-fire between corporate lobbies on the one hand and social activists and judiciary on the other, official land and environmental clearances for infrastructure projects had become extremely slow, non-transparent or erratic**

- **Secondary education is a minimum qualification for many good non-farm jobs, and yet the children from poor families drop out in large numbers before entering or completing secondary schools, on account of economic and, particularly in the case of girls, also social compulsions.**

- The quality of school and college education is not sufficient for employable skills for many, even manual, jobs. The provisions for vocational training and skill formation along with connections with potential employers, particularly for rural youths, are extremely deficient. In a so-called 'labour-surplus' country there is now a serious shortage of employable labour in factories and other enterprises.
- Despite all the economic growth of recent years, a major social and organizational failure, almost at a disastrous level, over many decades has been in matters of public health and sanitation, where India lags behind even several African countries. Poor public health and sanitation continue to keep the Indian disease burden high and productivity of workers low.
- Environmental degradation has been a major drag on net economic growth. It has been reported in the latest UNDP Human Development Report that the annual depletion in natural resources (depreciation of 'natural' capital) in India is nearing 5 per cent per year (wiping out much of the current growth in national income conventionally measured). A recent book, *Greening India's Growth* by M. Mani (2014) estimates that in 2009 the cost of environmental degradation in India came to 5.7% of GDP. It has been assessed by WHO that of the 20

most air-polluted cities in the world, 13 are in India. (Indoor and outdoor) air pollution kills an estimated 1.6 million people every year.

- All of the above--infrastructure, education, public health and sanitation, environment-- involve the governance effectiveness issue with respect to delivery of key public goods and services, which is rather low in India, and, of course, varies a great deal between different states in India. A recent ranking, by Mundle et al (2012), of 17 major Indian states in terms of a composite score for quality of governance (taking into account delivery of infrastructure, social and judicial services, fiscal performance, law and order and quality of legislators) suggests, unsurprisingly, that the six states that occupy the top ranks, across alternative rules of weighting the different indices, are: Andhra Pradesh, Gujarat, Haryana, Kerala, Punjab, and Tamil Nadu; the bottom ranks are largely occupied by seven states: Assam, Bihar, Jharkhand, Madhya Pradesh, Uttar Pradesh, and West Bengal.
- Governance ineffectiveness is often regarded as a lack of state capacity, many point to this as India's major failing. State capacity is weak not necessarily because of a dearth of capable people but because of a systemic impasse.

Extraordinary state capacity in some episodic matters, for example, in organizing the complex logistics of:

- **The world's largest election**
- **The world's second largest Census**
- **Some of the world's largest religious festivals**

But extraordinarily poor capacity displayed in, for example, some regular essential activities like cost-effective pricing and distribution of electricity—the key input for the economy. Under-recovery of costs, erratic supply and anemic investment in electricity, caused not so much by an inherent lack of administrative capacity, but more by factors relating to complicity in an occasionally sinister political nexus, populist pressures and outright theft.

Similarly, much of the police and bureaucracy are highly politicized and often deliberately incapacitated.

Corruption in India is often more dysfunctional, than say in the more politically centralized countries of East Asia, primarily because it is fragmented, with no encompassing centralizing entity, internalizing the distortions (negative externalities) of each act of corruption.

- The apparent lack of state capacity is more often a *symptom* of the underlying difficulty of organizing collective action (or collectively working out a 'social pact') in India, a problem exacerbated by its

- ✓ Large heterogeneous population
- ✓ Fragmented polity
- ✓ Extreme social and economic inequality

In such a context commitments on the part of the state are often not credible, and anticipating that different interest and identity groups settle for short-run patronage and subsidies.

This brings me back to the main theme of the 1984 book.

Since 1984

- the population has increased considerably both in size and the diversity of now-assertive groups,
- the polity is more fragmented (even in the most recent, unusually aggregative and presidential, national election signs of high political fragmentation remain --36 political parties with at least one seat in Parliament; the vote share of regional parties still remaining almost half)
- (while social inequality may be on a slow decline) economic inequality has almost certainly increased.

By and large the consequent problems for collective action may have become more severe, in spite of centralization of power under the new regime.

Let me end by pointing briefly to at least four types of structural issues, not considered in the 1984 book, where there are significant unresolved tensions that the Indian political economy will have to grapple with in the coming years.

- (a) There is a brewing 'legitimisation crisis' of capitalism in India among many sections of the people on account of**
- Rising inequality of wealth**
 - The flourishing of 'crony' capitalism**
 - The displacements and dispossession of common people from their land and degradation of their environment**
 - Deterioration in the supply of basic public services (water, safety, etc.) in the burgeoning cities and towns, while the rich arrange for private access to these services**

In reaction, quite often politicians try to placate with short-run populist measures.

But the legitimisation issue has also induced over the last couple of decades vigorous social movements and pressures for the recognition of

various kinds of citizen rights and accountability institutions. (The Left, or whatever is left of the Left in party politics, has so far given mostly rhetorical support to these movements, without putting its organisational muscle into them.)

On the other hand, these movements have occasionally ended up stalling industrial progress—in collaboration with judicial activism they have made mining, infrastructural and environment clearances sometimes very difficult, slowing industrial growth.

The debates all around have become polarized on this matter, and political decisions seem to lurch from one end to the other—under UPA in the early years the rights movement flourished, but in the last two years, under UPA as well as NDA governments, the pendulum has swung again in favour of corporate lobbies.

Since the social movements have not yet taken the form of mass political organisations, it has been relatively easy for business-friendly governments to bypass or dilute earlier welfarist legislative actions in actual implementation. To negotiate some kind of political balance in this tug of war between competing interests will be complex and time-consuming, and the Indian polity will go on vacillating on these issues. And following usual political practice, parties in Opposition will agitate against policies they themselves supported while in power.

The mainly elite-led but thriving NGOs act often as strident single-interest lobbies, making compromise difficult. In this respect they are poor substitutes for large multifarious political parties. But with the decay of inner-party democracy in all the parties, political parties no longer act as a forum for deliberation and transactional negotiations between contending interest groups within the party on

controversial policy issues, where there are always trade-offs which could be negotiated.

(b) More than citizen rights and welfare, the young people who are the majority of 'aspirational' India seem to be demanding jobs. Over the next decade or so this can be a major source of political turmoil, particularly because over many decades job growth in India has been very sluggish. Every month there is about a million new entries into the non-farm labour force, but outside the construction sector growth elasticity of job creation so far has been extremely low. Most recent economic success stories in India have been in relatively skill-intensive or capital-intensive industries (software, pharmaceuticals, vehicles, auto parts, etc.).

There are several constraints on large-scale labour-intensive industrialization in India— infrastructure, skill formation, credit, regulatory environment, contract enforcement problems, red tape, etc.

Partly on account of forces of technology, and more capital mobility both across countries and across states in India, trade unions are now much weaker than before.

Even in the organised sector more than one-third of workers are 'contract labourers' without security or benefits, sometimes working side by side with regular workers.

We do not yet have good statistical decomposition exercises on the net impact of these various factors on job creation or lack of it.

- (c) Even when jobs are created, there is a major regional discrepancy between job demand and supply, which may turn the so-called demographic dividend into a ticking time bomb in parts of the country. For demographic reasons the young people are more in the large populous states of north India (where poor governance and infrastructural deficiency limit**

job growth as well as delivery of welfare services); jobs when created are more in states in west and south India. Inter-state migration can be a partial relief but, given the staggering numbers, cannot be a solution if one wants to avoid large costs of dislocation and nativist unrest. The current government and the Finance Commission seem to be encouraging more devolution of finance and responsibility to the states. With large initial differences in state capacity and infrastructural deficit, this is likely to accentuate regional inequality. With capital being much more mobile across states than unskilled labour, many states are likely to compete in giving concessions to capital while indulging in populist measures for the poor.

(d) Tension between rentier and entrepreneurial capitalism

Three major sources of rent:

- Traded natural resource intensive goods (like minerals)—with global recession and slowing down of the Chinese economy this source is a bit weaker now

- **Non-traded natural resource intensive goods and services (like land and real estate)**
- **Political rent in other activities (following from collusion between politicians/bureaucrats and connected sets of favoured businessmen). Even after liberalization capital crucially depends on various kinds of regulatory discretion of officials as well as loans from public banks—large corporate defaulters on the latter have recently been described by the RBI Governor as ‘free loaders’.**

There is hardly any major state or political party in India which has not been corrupted by land and real estate interests. As the economy grows and land prices in a densely populated country gallop, this is unlikely to diminish in importance. (There is some evidence that land price rise in India in recent years has been one of the highest in the world).

On political rent there are, of course, built-in checks in economic competition (if scale economies are not large barriers to entry), particularly from abroad, and the political competition of democracy. Though the domestic non-traded part is large, the Indian economy is now sufficiently globally integrated for the economic check to be quite significant in many sectors. On political competition, however, the barriers to political entry are getting stiffer, as elections become inordinately expensive and all campaigning politicians are increasingly dependent on scarce financial and organisational resources.

The impact of rentier capitalism on politics is to encourage oligarchic forces. In US history the 'robber barons' of the 19th century were partially checked by the institutions created by the politics of the 'progressive era'. Much will depend on if or how a sufficient number of accountability institutions develop in India. Our elections are vigorous but our democracy is enormously flawed in terms of various kinds of accountability failures, particularly at the local level. It is this uphill democratic

struggle that will shape the future of Indian political economy.