

Tried, then Abandoned: Economic Liberalisation in India

James Manor

In the heady days after Rajiv Gandhi's December 1984 election landslide, the *Wall Street Journal* got wind of plans for economic liberalisation in the first budget and promptly dubbed him 'Rajiv Reagan'. For understandable reasons, the Prime Minister did not relish the name, but at the time it did not seem wholly misplaced. He, like his mother, had long since lost confidence in the state as an agency for creative action in society. Unlike his mother, he came to power free of prior ties to the 'socialist' lobby in the Congress Party. He had a vast, four-fifths majority in Parliament and was surrounded by youngish technocrats who had emerged from private sector corporations in India. He had cordial relations with representatives of several multinationals, and he was keen to spur growth and change in India by removing barriers to the import of microtechnology from Japan and the West. Within a few weeks, his government's first budget took cautious but significant steps to trim the vast thicket of licences, permits and controls which attend the industrial sector in India, and much more in that vein was promised for the future.

At the time of writing a little over two years later, very little has actually come of all this. We have again been reminded that there is great inertia in the Indian polity which can withstand enormous pressure for change, and that its political economy is massive enough to give Indians the confidence to stand apart from the international trend towards liberalisation. We have seen a broad, heterogeneous and hugely formidable array of interests arise to oppose liberalisation. And we have come to realise that this Prime Minister is too irresolute, maladroit and dismissive to meet so daunting a challenge as this. Thus, our problem in dealing with the Indian case is not to assess the political implications of liberalisation, but to explain why this particular dog failed to bark.

Rajiv Gandhi succeeded to the premiership on 31 October 1984 with profound discontents about the condition of India's economy and polity. Whatever confidence he had once had in the capacity of the state to act as a creative force in society and the economy — and it may be that he had never had much in the first place — had evaporated by 1984. He was also deeply frustrated by India's slow industrial growth rate and by the poor quality of industrial products. And he was exasperated with the ubiquity of what he called 'power brokers' — a term that he uttered with intense distaste,

which meant wheelers and dealers, arrangers of bargains — in India's political economy. The term referred not only to those who secured electoral support from the rural masses by carefully distributing resources, but also to politicians and bureaucrats who mingled and forged transactions with every major interest in the industrial sector, including trade unions and the people who managed both public sector and private sector enterprises.

Indira Gandhi had, rather vaguely, shared nearly all of these views during her last premiership between 1980 and 1984, but she had taken no significant action as a consequence. Her last term in office was marked by an extraordinary degree of inaction on these fronts for a woman who was supposedly a forceful leader. The period between 1980 and 1984 'was virtually devoid of major economic initiatives' [Rubin 1985] and of major initiatives for the betterment of society as well [Manor 1987].

The son was not inclined to drift along in the manner of his mother, however. He had spent his entire adult life in an India which, after 1965-66 when growth rate in real value in manufacturing began to fall off dramatically, faced stagnation in the industrial sector [Rubin 1985:2]¹. This was made all the more difficult to bear by the take-off in the same period of several once-backward economies further east in capitalist Asia. India's troubles with industrial development are generally attributed to three main causes: inefficiencies which have resulted from policies that insulate both public and private sector industries from the market, inadequate demand for industrial products and insufficient investment in the public sector. In early 1985, Rajiv Gandhi's government set forth a strategy that was intended to deal with the first two (but not the third) of these problems and to obtain for India the advances in microtechnology in which the premier placed great faith as a further spur to economic development.

The new economic policy offered prosperous urban interests significant concessions that were intended to generate enthusiasm for the new strategy before these groups began to feel the bite of some of its less advantageous elements. Tax rates on personal income were cut and the maximum allowable bonus to

¹ This section of my article owes a heavy debt to Rubin [1985], to Bardhan [1984] and to conversations with Ashutosh Varshney.

employees of industrial firms was raised. Corporate tax rates were also lowered and the level of assets at which anti-'monopoly' regulations began to apply to firms was raised. Import duties were slashed or eliminated on an array of intermediate and capital goods. (These tax cuts were compensated for by *ad hoc* increases in indirect taxation on goods such as cement, steel and petroleum). The lending rate of public sector banks (that is, nearly all banks) was lowered and half of income from exports was exempted from corporate taxation. Twenty-five industries were freed of the need to obtain licences [Rubin 1985:3-8]. All of these measures were heartily welcomed by Indian corporations and their white-collar employees who had long had far greater difficulty dodging taxes than had self-employed people.

These initiatives were part of a more general attempt to de-politicize India's public life. 'Power brokers' and political bargaining were supposed to decline radically in importance in the industrialised sector of the economy, even as the young Prime Minister and his cohort of technocrats applied their supposedly non-political managerial 'science' to the problems of running the ruling party and the Indian polity. (This writer received an early exposure to this mentality when he was introduced to Rajiv Gandhi in 1982 as a 'political scientist from Britain'. This prompted the budding politician to ask that the main principles of this 'science' be explained, so that this technology could be applied to the governance of India. The responses to this appeal were seen to be highly unsatisfactory). The 'rationality' of the market in the industrial sector was to be reinforced by the 'rationality' of modern management in the party and the state.

Certain other elements of the depoliticisation of the industrial sector were decidedly unappealing to industrialists and their managerial employees, however. India's Finance Minister announced in a characteristically prim manner that 'I am determined to end all lobbies' [*India Today*, 15 April 1985], by which he meant that he and his principal lieutenants would no longer meet with leading businessmen. Nor would they entertain appeals or messages from such people that were conveyed through Congress politicians who were close to industrialists. To do so might seem to some readers to be both proper and inevitable in a representative political system, and Indian politicians had excelled at just this for nearly four decades, but to give such interests a hearing would be to engage in 'politics' and the new regime was above that sort of thing. Upper middle class folk were further dismayed to see the government begin aggressive investigation into tax evasion which has long been something of an art among prosperous Indians. These were attended by police raids on the homes of certain well-known industrialists and entertainers, some of which led to arrests. These

actions, like tax cuts, were intended to discourage the use of black money and the evasion of civic responsibilities, but they were nothing short of alarming to well-heeled urbanites. Some simplifications in the tax code such as the abolition of investment allowances were also disconcerting.

None of this was quite so threatening to industrialists, however, as the first tentative signs that the government meant to cut away at the system of licences and permits which were an almighty inconvenience for industrialists to obtain but which — once they were secured — offered private firms valuable protection from competition, foreign and domestic. A splendid recent study by Stanley Kochanek [1985:189-211] has demonstrated just how expensive and excruciatingly complex the process of obtaining permits to import, manufacture, improve and export commodities actually is. Indian industrialists spend years securing such documents, and most of them have painstakingly assembled teams of professionals who specialise in obtaining them. Kochanek likens such captains of industry to people who have struggled at length to shoehorn themselves onto an overcrowded Indian bus and who, once aboard, stoutly resist others' attempts to climb on as well, lest in so doing they squeeze out those who have places already.

These unwelcome elements of the new economic policy were not adequately compensated for by the tax cuts and other concessions which were intended to sweeten the overall package. And in any case, those concessions were already in hand, so that prosperous urbanites and industrialists now began to seek ways to hang onto them without giving up the protection of what is often called 'permit raj'. They cast about for allies who also had an interest in thwarting thoroughgoing liberalisation, and they found plenty.

Opposition from one group, Congress politicians with a genuine philosophical commitment to Nehruvian socialism, was entirely predictable. There has always been a rather limited number of such people, and they have tended to be slightly more cerebral, westernised types who occupy positions in the upper echelons of the central government or the party's national-level organisation and who thus lack solid political bases in the regions. They have therefore been unable, in their own right, to exercise great power over events on the ground and in any case their numbers and influence have declined markedly since the mid-1970s as unbridled opportunists and criminals have come into the party in large numbers. But some old line Fabians are still there, and they are capable of mounting elegant, high-minded arguments that lend credence and respectability to the opposition of other groups who are driven by more mundane motives. The Congress socialists' protests are echoed by voices in leftist opposition parties, including the two main

Communist parties and the rumps and splinters of India's various Socialist parties.

At the level of ideas, 'socialism' counts for far less than economic nationalism as an impediment to liberalisation. Many Indian nationalists regarded capitalism as one of the unsavoury weapons of European imperialism against which, in the years after independence in 1947, India had somehow to be protected if it was to remain truly free [see for example Toye 1981:22-48]. This notion lay behind the successful efforts of Nehru and company to develop a broad array of state-funded industries which, taken together, outweigh India's numerous private industries quite considerably. Indeed, after France, India has the largest number of Fortune 500 public sector companies of any nation outside the United States. Nehru and company also managed to erect extensive state controls on imports, exports, foreign investment, foreign ownership and domestic capitalist enterprise. One of the reasons that dependency theory has had so little impact among students of India² is that in the 1950s, the Indian authorities so effectively anticipated the warnings of dependency theorists and devised protective structures and strategies such as systematic import substitution which — together with India's sheer size and diversity of resources — eased many of the difficulties which assailed some other less developed nations. Today many influential Indians — politicians, bureaucrats, intellectuals, journalists, industrialists, etc. — after hearing extravagant warnings from the likes of Indira and Rajiv Gandhi that the outside world consists largely of those who would destroy India, cling to existing protectionist barriers and the economic nationalism that underpins them. And the failure of state-owned industries to flourish generates an insecurity about their capacity to compete with foreign corporations in a liberalised environment.

The most formidable obstacle to liberalisation is posed by Congress politicians who are 'socialists' by convenience rather than by conviction. To them, 'socialism' has generally meant the enlargement of the pool of state-controlled resources which they could distribute to build up networks of supporters. Congress legislators in the 1950s were happy to promote the development of state-owned bus lines since it gave them the chance to extend bus service to remote sections of their constituencies. They were glad to see the state move into the pricing of agricultural produce and a whole host of other roles and services since this gave them influence to wield among both producers and consumers. They continue to favour state control over the production and distribution of steel, cement, fertiliser, cables, pumps and a vast array of other scarce and useful commodities since this gives

them more resources to allocate, more opportunities to cultivate their political bases. In other words, Congress has tended to operate as an impressive political machine, using its dominant position in the party system and its control of public resources to distribute goods and services in a highly partisan manner, to cement transactional relationships with powerful interests.

The machine suffered serious decay under Indira Gandhi's leadership because she curtailed the flow of political spoils to it, but enough of the old patronage politics remains today to cause large numbers of Congress operatives to bristle at the thought of economic liberalisation. To them, the rolling back of the state means a reduction of resources on which they depend to sustain themselves in power and material comfort. And since many of those resources flow into the hands of prosperous urban and rural groups, these politicians have hugely formidable allies in their opposition to liberalisation. Changes in recent years which have enabled less prosperous groups to gain access to significant political spoils (and which are briefly discussed at the conclusion of this paper) also mean that poorer groups are unenthusiastic about economic liberalisation. Leaders of disadvantaged castes also worry that if private firms are to replace state agencies as employers in various spheres, they will lose the quotas of jobs reserved for them in public enterprises. (The still more serious if slightly less immediate concern that liberalisation might eventually increase disparities between rich and poor has not fully dawned on leaders of disadvantaged groups.)

Another important source of resistance is the bureaucracy. Civil servants are unable to express their views overtly, but they have been reasonably effective at sabotaging the implementation of new policies from within the machinery of state. Their foot-dragging has seriously impeded the advance of liberal policies in international trade and in domestic licencing. This enables other groups that openly oppose liberalisation to argue that slow implementation and the confusion and economic damage that it causes demonstrate that the system simply cannot function in any way other than that which has long existed. This in turn suits the bureaucrats who favour state controls partly because it gives them influence which some of them peddle for profit and, more crucially, because it gives them power that they enjoy exercising. Some, in unguarded moments, will say that the various frustrations of the job are eased by their ability to keep industrialists and their minions waiting outside their offices. There are also many bureaucrats who have invested years of well-meaning effort working within or in close cooperation with public sector industries, and who believe that state ownership ensures that they are managed in socially responsible ways. Many others continue to cleave to the Nehruvian view that the system of licences and permits curtails the excesses of

² For a particularly misguided example, see Frank [1977] which is discussed in Manor (forthcoming).

unfettered capitalism.

India's Soviet allies are also uncomfortable with the idea of liberalisation, since a major advance down that road might result in extensive transactional ties between Western capitalists and powerful Indian elites. That could eventually lead to closer links between India and the Western powers at a diplomatic level. The Soviets place great value on their special relationship with India since India is the one major nation outside the Soviet block that offers reasonably consistent support for the USSR in the international arena. Soviet suspicion of liberalisation has played a relatively minor role, since the number of politicians in the Congress Party who are full-blooded friends of the Soviets is rather limited, but it has had some impact. This also stems in part from India's dependence upon Soviet military equipment and technology in certain important sectors — a dependence which the Janata Party in the late 1970s found impossible to escape, despite considerable effort.

Organised labour in India has also been deeply suspicious of liberalisation. This includes both the comparatively powerless unions that are associated with opposition parties and — more to the point — the Congress Party's own trade unions. Their anxiety is that public sector industries, and to no small extent India's heavily protected private sector, may wither in the face of challenges from multinational and indigenous competition. That could destroy jobs and it could mean that Indian industries have to 'rationalise' their labour forces in order to hold their own alongside new competitors. The unions also fear that if liberalisation were to succeed famously, it might open the way for a substantial abandonment of public sector industries, with catastrophic results for the workforce.

With so many powerful interests that seldom make common cause arrayed against economic liberalisation, we might well ask who is actually *for* it. The answer is unimpressive. Rajiv Gandhi and a few of his technocratic associates favour it, as do representatives of foreign governments and corporations, and a modest number of Indian entrepreneurs who stand poised to strike deals with such corporations. But the constituency for liberalisation is very modest indeed when considered alongside the broad coalition of opponents. Despite this, the Prime Minister did not feel compelled to invest time and effort cultivating support for liberalisation. He simply unveiled it, suddenly and unexpectedly, soon after obtaining an electoral landslide in the last week of 1984. The logical thing would of course have been to generate popular backing for the idea during the General Election campaign, but no mention was made of it on the hustings. Indeed, virtually nothing was said about economic policy at all in a campaign that consisted of little more than slanders about the sinister nature of

certain minorities, of the opposition parties and of shadowy foreign hands that sought to destroy India [Manor 1985]. Rajiv Gandhi presumed, with surprising naïvete, that there was no need to build support for this major change in policy. He shared his mother's central misperception that India could be governed by mere assertion from the apex of the political system.

Individual personalities usually count for relatively little in the success or failure of grand policy, but enough in India today depends on Rajiv Gandhi to justify a moment's further discussion of his behaviour. He owes his pivotal position to many years of assiduous effort by his mother to erode the substance and autonomy of political institutions, both formal and informal, in the interests of personal and dynastic rule. The result is a political order which is inadequate for governing India satisfactorily, but which greatly inflates the importance of whichever Gandhi stands at the helm. Since Rajiv Gandhi gained the premiership, despite a near-total lack of political experience, it is not surprising that he should have made some elementary mistakes in this first phase of on-the-job training.

Consider just two: his inconstancy and his dismissiveness. His abrupt unveiling of economic liberalisation was only one of several sudden changes of course that he sprang on the electorate. During the election campaign, he was a passionate Hindu chauvinist, sowing suspicion of religious minorities. After the election, he instantly became a magnanimous cosmopolitan, making remarkably generous concessions to the minorities. He seemed not to realise that by whipping up antipathy towards the minorities in the first place, he had helped to create a constituency for such views and to generate expectations of chauvinistic action. By reversing himself so abruptly, he dismayed militant Hindus who had responded to his election rhetoric and yet failed to persuade the minorities of his good intentions, ending up without solid backing from either. Such tergiversations on a great many issues — including the place of 'socialism' in India and the need for economic liberalisation — have alienated many interests who, rather to his surprise, take his statements seriously. His presumption that, as Indira Gandhi's son, he can get away with anything has lost him so much support that he now has great difficulty imposing his will on any front. And yet the potency of interests opposing economic liberalisation ensures that it can only succeed if he has the clout and the inclination to impose it.

His naïvete, born of inexperience, has also led him into frequent fits of dismissiveness which are so sweeping as to leave observers wondering whether the Prime Minister sees value in anything. One such outburst bears directly on the attempt at economic liberalisation.

In September 1985, Rajiv Gandhi addressed a gathering of Indian (private) industrialists. The first half of his speech was a withering denunciation of the nation's public sector industries which he said were losing gargantuan sums and draining the exchequer while producing little other than rubbish. This tirade, which went on for 15 minutes or so, was sweet music to the assembled magnates who waited keenly for the second half of the speech which, they expected, would be a hymn to capitalism as a creative force. When the Prime Minister turned to the private sector, however, the ranting continued. India's capitalist enterprises were useless, they produced third-rate goods and they offered no hope for the nation's future — end of speech. He appeared to see no way forward at all.

One logical next step was of course to open India up to high technology and multinational firms. But here his impatience surfaced once again when the first budget encountered resistance and failed to produce the rapid and tidy transformation of the economy that he seemed to expect. Experience would have taught him that such quick turnabouts seldom occur and that one must have patience with minor reverses and persist. But his tendency in such circumstances is to switch off, to dismiss the whole problem from his mind and to rush headlong into another sphere. That is what happened to his plans for liberalisation. After a few months of serious effort and modest innovations in the first budget, at the first sign of serious opposition he turned his back on the entire scheme. Since then little has changed. Liberalisation is where it was, launched but dead in the water, and no coherent alternative in which the state sector might play a more creative role has emerged to replace it.

This is not, of course, a discussion merely of economic liberalisation, but on the retreat of the developmental state more generally. To address that set of broader concerns, two further comments about India are necessary. It should first of all not be presumed that the thwarting of Rajiv Gandhi's scheme for liberalising the industrial sector means that the developmental state will now resume a robust forward march. The authorities in New Delhi have, at least since 1980 and arguably well before that, abandoned the idea of using the public sector as an engine for change. They no longer believe that it can have a creative impact within society, nor do they think that it can carry India through to an economic breakthrough to developed-nation status. So although India's national leaders have found it impossible to roll back the state, since too many potent interests oppose that, they see no developmental purpose for it and therefore leave it in place — disparaged, disregarded and underfunded.

That does not mean, however, that the developmental state has been utterly abandoned in India. Note the references in the previous paragraph to the *New Delhi*

authorities and to *national* leaders. India is a federal polity and in several of its states, governments continue to play, and even find new ways to play developmental roles. Not all state government's fit this description. It is at the state level that we find, paradoxically, both the most corrupt and parasitic governments in India and the most creative. Several states are run by governments which routinely brutalise their critics, while others are systematically looted by politicians. But such governments eventually have to face what has been a remarkably mature and assertive electorate. And since incumbent governments get re-elected less than half the time — and only when they have governed well enough to earn popular support — there are clear incentives to find ways for the state to promote development. This is true both of 'development' defined as the promotion of economic growth and of 'development' which serves redistributive purposes.

State and local governments in India control more than half of the country's public sector industrial productive capital (which is another reason why Rajiv Gandhi, who overseas only the *central* government's industries, cannot mount a thoroughgoing roll-back of state sector industries). The main contribution of state governments' industries to economic growth has not been through profitable production in their own right, but through the provision of crucial inputs to profit-making agrarian enterprises. By providing machinery, power, fertilisers, materials to facilitate irrigation and the processing, storage and transport of crops such as sugar and wheat, state-level industries have helped to produce booms in states like Maharashtra in the west, Karnataka in the south and (until ethnic conflict engulfed such doings) in Punjab in the north. State-level agencies also provide vital credit facilities, agricultural extension services and a host of other aids to growth. In such places, the developmental state is not entirely in retreat.

And since the late 1970s, several state governments have mounted an impressive array of programmes that are at least modestly redistributive in their impact. Most have done so because they realise that poorer people whose votes were often controlled by powerful landowning groups during the 1950s and 1960s have tended increasingly to make up their own minds at election time, and to support parties and leaders that have delivered real substance to them. Since poorer voters outnumber the prosperous, state governments have been compelled out of self-interest to respond. Thus we see a Congress government in Karnataka and a Janata government in Rajasthan in the 1970s channelling resources to poorer groups through pension schemes, scholarships to poorer students, reservations in government employment, modest land reforms, the provision of housing sites and materials to the rural poor, etc., etc. In so doing, they have broken the traditional hold of locally

dominant landowning groups over state-level politics. A Communist government in West Bengal has entrenched itself in rural areas — an historic achievement — by providing land reform, major efforts in literacy and public health, and an impressive de-centralisation of power that gives disadvantaged groups in small arenas some control over their own destiny. The newly elected Communist regime in Kerala can be expected to follow suit, and perhaps to achieve the unassailable position with the electorate that their Bengali comrades now enjoy. Even in certain states where landowning groups still exercise substantial control of state-level politics such as Maharashtra, they are canny enough to see that it is in their interests to draw the leaders of numerically powerful poorer groups into their ruling coalition by giving them substantial patronage to distribute among their caste and class fellows. None of this amounts to *radically* redistributive politics, but these initiatives have genuine substance and they are likely to provide the basis for at least a modest revival of the developmental state once Rajiv Gandhi's government passes from the scene.

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