II
Political Economy

The essays in this section should be read in conjunction with the Introduction to the volume, especially the discussion on political economy. The focus in this section is on the political determinants of growth and distributional patterns in India. The essay entitled 'India's Fragmented-Multiclass State and Protected Industrialization' is drawn from my book *State-Directed Development* (2004). It provides an overview of the state's role in promoting and hindering industrial growth in India. Unlike neo-liberal accounts of Indian political economy, I argue that growth patterns in India have been influenced, not so much by more or less state intervention, as by the type and quality of state intervention.

This emphasis on state capacity as a determinant of economic outcomes runs through the other essays in this section as well. In the essay, 'Politics of Economic Liberalization in India' I analyse various political obstacles that stymied Rajiv Gandhi's efforts to liberalize India's economy in the second half of the 1980s. Since similar efforts succeeded in the early 1990s, the changing role of business groups in economic policy making in India is especially worthy of serious study. This theme is analysed in much greater detail in the two part essay on the 'Politics of Economic Growth in India'. The focus in these essays is on how best to understand the growth upsurge in India since about 1980. I argue that this is best understood by focusing on the growing alliance between the state and private capital in India.

The focus in the final essay 'Regime Types and Poverty Reform in India' shifts from growth to redistributive issue. This essay was written earlier than all the essays on politics of economic growth; it provides a summary of my 1987 book, *The State and Poverty in India*. As with the other essays in this volume, it is reproduced here in its original form, without any updating. In

India reflects the organizational cohesion and the class basis of ruling regimes. Better organized regimes with a broader social base are thus more effective at reducing poverty. I demonstrate this argument by comparing political efforts at poverty alleviation in West Bengal, Karnataka, and Uttar Pradesh. I have recently updated this earlier study and the related argument has been summarized in the Introduction to this volume.

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India's Fragmented-Multiclass State and Protected Industrialization*

Sovereign India's experiment with state-led economic growth has produced mixed results. Between 1950 and 1980 the Indian economy grew at a sluggish per annum rate of 3–3.5 per cent, but accelerated to nearly 6 per cent per annum thereafter (see Table 5.1). Nonetheless, this performance of the sovereign state was a considerable improvement over the nearly stagnant colonial economy, especially the pre-1930 period. At the same time, this growth compares unfavourably, especially with that of South Korea but also Brazil, suggesting the need to scrutinize the role of the state in the Indian economy. As for industrial growth, it fluctuated from over 7 per cent in the first fifteen years, to below 4 per cent during 1965–80 and then back again to nearly 6 per cent per annum between 1980 and 2000. There was also considerable structural transformation over the five decades: while agriculture contributed more than half and industry less than 10 per cent of the national product at independence in 1947, towards the end of the century a diversified industrial sector contributed nearly one-quarter and the service sector nearly one-half of the whole.

This chapter focuses on the political determinants of economic performance in India, especially rates and patterns of industrialization, raising questions about the design and the capacity of India's highly interventionist state. Given the mixed outcome, the puzzles for analysis are both why the Indian economy has done as well as it has and why it has not done better. In keeping with the central themes of the study, the main concern is with the state's role, specifically, how the dynamics of a fragmented-multiclass state influenced economic choices and performance.

*Originally published as 'India's Fragmented-Multiclass State and Protected Industrialization', in Atul Kohli, *State-Directed Development, Political Power and Industrialization in the Global Periphery*, New York: Cambridge University Press, 2004, pp. 257–90.

TABLE 5.1: Some Basic Growth Data, 1950–2000
(all figures in percentage per annum)

	1950–64	1965–79	1980–2000
GDP growth	3.7	2.9	5.8
Industrial growth	7.4	3.8	6.2
Agricultural growth	3.1	2.3[a]	3.0
Gross investment/GDP	13	18	23

Source: Government of India, *Economic Survey* (various issues). Due to numerous statistical complications, these figures should be viewed as broadly indicative rather than as exact or definitive.
Note: [a]Figures are for 1967–80. Inclusion of the two drought years 1964–5 and 1965–6 would make this average figure even lower.

The scholarly scope of this chapter is broad and sweeping in quality, necessarily leading to neglect of nuances and of controversies relevant for a country specialist. I note at the outset that India's political economy can be interpreted from at least two distinct standpoints, only one of which is emphasized below. A more neo-liberal interpretation would suggest that India's lackluster performance results from the sluggish economic growth that followed from the closed and statist model of development adopted by India's misguided nationalist and socialist leaders. According to this line of thinking, the last two liberalizing decades have led to some improvement—higher rates of economic growth and a lower rate of poverty in India.[1] While there are valuable insights in such a perspective, it is not wholly consistent with the facts and it reflects a worldview that this study does not share.

I argue instead that the Achilles' heel of Indian political economy is not so much its statist model of development as the mismatch between that statist model and the limited capacity of the state to guide social and economic change. There have been statist models in other parts of the world that achieved important gains, but they were generally directed by more efficacious states. The cohesive-capitalist cases of South Korea and Brazil both represent models of the Right; the cohesive-lower-class model of communist China is a case on the Left. Trying to reconcile political preferences of both Left and Right in the context of a fragmented state, the Indians failed both at radical redistribution and at ruthless capitalism-led economic growth. The socialist commitment of Indian leaders, for example, was rather shallow. While socialist rhetoric was used to try to build political capital, policies in favour of the poor were seldom pursued vigorously. Such socialist commitments as were pursued, albeit ineffectively, also alienated private

[1]One recent collection that broadly reflects this standpoint is Isher Judge Ahluwalia and I.M.D. Little (eds), *India's Economic Reforms and Development: Essays for Manmohan Singh*, New Delhi: Oxford University Press, 1998.

investors. The associated difficulties in state-business relations also hurt economic growth. The change in India over the last two decades is not so much that it became more liberal as that Indian politics shifted towards the Right, allowing for more harmonious state-business relations and a positive impact on growth. But at the same time the politicized political exclusion of the poor made governance more difficult and fed neo-fascist tendencies, including the mobilization of nationalism against minorities.

I have divided the discussion of modern India's political economy into three chronological phases: the Nehru era (approximately 1950–64), the era of Indira Gandhi (approximately 1965 to the early 1980s), and the last two decades of the twentieth century, during which numerous governments have come and gone. This division reflects a trend whereby political changes seem to have influenced rates and patterns of industrialization. Thus, I suggest that the state's considerable legitimacy and relatively clear economic priorities in the Nehru period facilitated some economic gains. By contrast, Indira Gandhi's populism hurt investment and growth. And finally, the political drift towards the Right in the third phase has been accompanied by a growing role of the private sector in the economy and improved economic performance.

THE NEHRU ERA

If the 1940s in India are best thought of as the decade in which India marked the transition from colonialism to a sovereign democratic republic, the Nehru era that followed is usefully viewed as the crucible of modern India. It was during this era that a stable democracy took root and the hegemony of a statist model of economic development was established.

Indians by now take their democracy for granted, as if it were the most obvious way of organizing state power in a poor, multiethnic, continent-sized country. Viewed comparatively, however, as well as against the most popular theories that treat democracy as a function of economic advancement, India's democracy is a puzzle.[2] At a minimum the survival of democracy in India suggests that, under specific conditions, a country's political structures enjoy some autonomy from the underlying society and economy. The roots of Indian democracy and of its fragmented-multiclass state thus need to be understood in terms of institutional continuities, including the British political inheritance and, in particular, a relatively centralized and coherent state,[3] with its well-developed civil bureaucracy, its limited but real experience of

[2]For a fuller discussion of this puzzle, see Atul Kohli (ed.), *The Success of India's Democracy*, Cambridge: Cambridge University Press, 2001, especially the introduction.

[3]Those who do not see a ready connection between centralized authority and democracy may consider Samuel Huntington's important argument that 'order' nearly always precedes 'democracy'. See Samuel Huntington, *Political Order in Changing Societies*, New Haven: Yale University Press, 1968.

elections and of constitutional, parliamentary government, and its traditions of independent media and freedom of such associations as labour unions.

Since inheritance is seldom destiny, India, like many other post-colonial countries, could readily have squandered these valuable political resources. Yet it did not. Besides colonial inheritance, therefore, one must underline the constructive political role of India's nationalist movement/party, the Indian National Congress, and of India's leaders in the evolution of the democratic state. In its quest for freedom from British rule, the Congress not only brought together a variety of Indian elites but also established numerous links between elites and the masses, which defined the framework within which India's democracy advanced. India's leaders adopted mass suffrage, committed themselves to a parliamentary democracy, permitted the emergence of a variety of political voices and organizations, and conducted the internal affairs of their hegemonic party in a democratic and inclusive manner.[4]

This combination of a protodemocratic colonial inheritance and a democratically inclined mass nationalist movement provided the institutional preconditions for the emergence of democracy in India. But the political preconditions also helped to lay the foundation for the emergence of a fragmented-multiclass state. The Indian case thus raises the important question: Does democracy in a developing country necessarily lead to fragmented state power with a multiclass social base? The Indian case indeed suggests a strong association between democracy and a fragmented-multiclass state. But as no single case tells us that much about a general relationship, one must be wary of confusing association with causation. For every India, for example, there is also a Malaysia, with less fragmented state authority. And even if democratization in a developing country tends to encourage fragmented-multiclass states, the reverse is certainly not the case: state power in many authoritarian situations can also be fragmented and rest on a plural class base. Most important for the immediate discussion, certain specific political developments during the Nehru period helped consolidate India's democracy while also reinforcing the state's fragmented-multiclass nature.

The colonial bureaucracy that India's leaders inherited was a fine professional force, especially the elite ICS officers, but it was mainly a law and order bureaucracy, not well suited to implement the leaders' ambitious developmental goals. A major overhaul of the bureaucracy, though contemplated, was never really pursued, mainly because the well-trained elite civil servants were indispensable for governing the new state.[5] The size

[4]For a good study of how and why the Indian National Congress—even though a single, hegemonic party—facilitated Indian democracy, see Rajni Kothari, *Politics of India*, Boston: Little, Brown, 1970.

[5]For a good study of continuity in the nature and the structure of the pre- and post-

of the civil service, including the officer ranks, also grew substantially during the Nehru years. Though renamed the Indian Administrative Services (IAS), the new service reflected the structure of the ICS and still relied for staffing on a highly competitive exam that mainly tested general rather than specialist knowledge. The small fraction of candidates who passed the exam were then trained in more or less the same way as ICS officers had been—first in an institute and then on the job, apprenticing under more senior officers. To keep up the old esprit de corps, many of the ICS traditions were maintained, including the idea that elite civil servants constituted the steel frame that anchored India's political stability. Internal promotions were made on the basis of merit and seniority, and an independent supervisory body helped to maintain the level of professionalism, essentially until the late 1960s, when the IAS became more politicized. The IAS also adopted the core structure of the old ICS, namely, district officers who were responsible for revenue and law and order; new development functions were merely add-ons.

Upon independence, India's leaders faced a cruel choice: advancing the state either as an effective agent of political order or as a successful facilitator of economic development. They opted for the former, which would become a longer-term trend, prioritizing political needs over economic ones and thus initiating what would eventually become a substantial gap between the state's capacities and its developmental ambitions. A similar mismatch came to characterize the Congress party as it sought to be simultaneously a popular ruling party and an agent of socialist development.[6] The majority of Indians lived in the countryside, and most of them operated within a variety of patron–client relationships. One ready way to build political support in such a social setting was to cultivate the support of the patrons—generally the highest, landowning elite castes—who, in turn, could sway the political behaviour of their dependent clients, generally poor peasants. And this is precisely what the party did, building long chains of patronage that extended from the centre to the periphery. This ensured a popular base—at least for a decade or two—but eventually also led to the capture of the party by society's powerful. In this way, more egalitarian ambitions, such as land redistribution and the capacity to tax the agrarian sector, were diluted.

From ICS to IAS, New Delhi: Oxford University Press, 1996. I draw on this study in the next paragraph, especially chapters 3 and 4.

[6]For a fuller discussion of some such issues, see Francine Frankel, *India's Political Economy, 1947–1977: The Gradual Revolution*, Princeton, N.J.: Princeton University Press, 1978, especially chapters 5 and 6. A much more detailed treatment of how the early Congress party 'succeeded' is Myron Weiner, *Party Building in a New Nation*, Chicago: University of Chicago

Another significant political development concerned the evolution of Indian federalism.[7] Soon after India won its sovereignty, each of its numerous ethnic groups began demanding a greater share of power. These struggles came to a head in the late 1950s, when a reluctant Nehru agreed to a linguistic reorganization of Indian federalism. Although this decision accommodated ethnic demands and created a more stable political unit, it also fragmented state power. To the extent that developmental ambitions of India's leaders found institutional expressions—such as the Planning Commission—these were nearly all at the centre. By contrast, lower-level governments were mainly 'machines' with significant powers and resources. While India's central state continued to be quite powerful in relation to its federal units, a federal reorganization of functions also diluted the state's overall capacity to pursue a coherent developmental agenda.

The ruling ideology of the Congress party provides a final example of the mismatch between capacity and ambitions. Congress committed itself to 'nationalism' and 'socialism'—Nehru's creed, which won substantial popularity and legitimacy for him and the party. At the same time, however, these ideological commitments made it difficult to pursue vigorous economic growth, a goal that Congress and the state elites also espoused. In spite of the socialist rhetoric, India was mainly a private-enterprise economy. Vigorous economic growth would be feasible only if there were a vigorous private sector. But the Indian version of multiclass statism found itself at odds with its espoused goals: Nationalism discouraged foreign enterprise in India, and the socialist inclination created difficult relations with Indian entrepreneurs.

Taken together, these political developments during the Nehru era suggest two conclusions. First, there was significant continuity between the colonial state and the sovereign Indian state, even as there were many obvious discontinuities—that the new state was sovereign, democratic and interventionist. The areas of continuity include, most strikingly, the design of the new civil service but also the organization of the legal system and of the armed forces. The latter was especially consequential for helping to ensure civilian control of the relatively apolitical military, a complex story beyond the scope of this study.[8] A more subtle area of continuity was the pattern of the state's alliances with the property-owning elites. The colonial state had rested its

[7]A ready and useful overview is Bipan Chandra, Mridula Mukherjee, and Aditya Mukherjee, *India after Independence, 1974–2000*, New Delhi: Penguin, 2000, chapters 8–10. For Nehru's views on this and a host of other related issues, the indispensable source remains S. Gopal, *Jawaharlal Nehru: A Biography*, vols 2 and 3, New Delhi: Oxford University Press, 1984.

[8]This is a surprisingly under-studied area of scholarship on Indian politics. Perhaps 'dogs that do not bark' attract less attention than the ones that do, but probably not justifiably. One study that does address this issue explicitly is Stephen P. Cohen, *The Indian Army: Its Contribution to the Development of a Nation*, Berkeley: University of California Press, 1971.

power with landowning traditional elites and generally had a good working relationship with Indian business groups. While Nehru clearly had a broader social base, the power alliances of India's new rulers with propertied groups also demonstrated remarkable continuities. While it is true that the mega-traditional elites such as the maharajas and the zamindars were eliminated, the Congress rulers still based their rural power on landowning elites, albeit smaller landowners, a 'lower' gentry of sorts.

Second, Nehru and his colleagues placed a high priority on consolidating Indian democracy. They thus incorporated society's powerful and conceded some power to demanding regional elites, but they also encouraged the hopes of the masses by promising egalitarian development to the poor. Although these strategies helped to institutionalize India's fragile democracy, at the same time, the resulting political developments also institutionalized the fragmented and multiclass political tendencies of the Indian state and undermined its capacity to pursue developmental goals vigorously. Was this outcome inevitable?

This is a difficult question to answer unambiguously. Certainly, the power to undertake some basic changes existed, as there was nothing inevitable in the degree of state fragmentation and in the lack of focus in the state's developmental priorities. At the same time, however, the nationalist movement was already straining and losing its way as it sought to create unity in diversity prior to independence. Nehru's specific decisions aimed at maintaining a stable and legitimate democracy in a heterogeneous society further weakened this potential in the post-independence period. Maintaining a 'law and order' bureaucracy hurt the state's capacity to undertake economic tasks directly; a commitment to nationalism and socialism made it difficult to mobilize private capital; and the Congress party's dependence on regional and rural elites fragmented state power, making it difficult to penetrate the rural society directly.

The economic model adopted during the Nehru era was, of course, the well-known model of state-led, import-substituting industrialization (ISI). Once adopted, it endured, even in the face of significant efforts in recent years towards a different model. At the end of the twentieth century, India still exhibited some of the core characteristics of its statist model of development—thus underlining the political nature of India's early economic choices.[9]

Nehru's political preferences, expressed through the Congress party, became India's dominant ideas and stressed the following: maintaining

[9]Good studies of this topic include A.H. Hanson, *The Process of Planning*, London: Oxford University Press, 1966; Jagdish N. Bhagwati and Padma Desai, *India: Planning for Industrialization*, London: Oxford University Press, 1970; and Baldev Raj Nayar, *India's Mixed Economy*, Bombay: Popular Prakashan, 1989.

national sovereignty, the superiority of the state in steering progressive capitalist development, and the need for India's poor to share in the fruits of development. The nationalist commitments of India's leaders translated into a suspicion of an open economy and a preference for heavy industry. In spite of low domestic savings, foreign investors were by and large discouraged, mainly because they might have threatened hard-won national sovereignty. A variety of interests, including Indian business groups, benefited from these ideological choices over time and helped to sustain them. A suspicion of an open trading regime is more difficult to understand in terms of underlying nationalism. Protectionism was justified mainly in terms of prevailing economic ideas of 'export pessimism' and 'infant industry'.[10] In the Indian case, however, there was also something deeply experiential and political about these choices. We have seen that openness during the colonial era had been interpreted by nationalists, not only as killing nascent industries, but also as inhibiting the emergence of indigenous industrial capitalism. Indian businessmen and industrialists, who stood to benefit from a relatively closed economy in which competition would be limited, expressed these preferences openly. Protectionism, as well as an emphasis on heavy industry, was thus seen as serving the interests of nation building. How else, according to India's leaders, could such an enormous country, with its ancient civilization, re-emerge as a powerhouse that was not easily subject to manipulation by external powers?

Widespread was the belief in the state's ability to guide social and economic change efficaciously at the middle of the twentieth century. We have seen this in the Korean and Brazilian cases. This view had a left-leaning tilt in India, reinforced by an admiration of the Soviet Union's developmental 'successes' and by an affinity to the British Labour Party's type of socialism. These ideological proclivities were also consistent with the concrete interests of the Indian political elite, which could channel some of the fruits of development to themselves and their offspring. The statist model translated into both a direct economic role for the state—as, for example, in the widespread creation of public enterprises—and into a more indirect role in guiding the activities of private capital via the 'license-permit raj [or regime]'.[11] What is surprising in retrospect is not so much India's affinity for statism but how little open discussion took place concerning the type of state that could successfully undertake such ambitious economic tasks. While market imperfections were discussed ad nauseam, there was no parallel discussion

[10]A good discussion of the belief systems that supported India's economic choices can be found in Sukhamoy Chakravarty, *Development Planning: The Indian Experience*, New Delhi: Oxford University Press, 1988, chapters 1 and 2.

[11]For a highly critical but excellent description of how this policy 'regime' operated, see

of state imperfections from the standpoint of developmental capacity. One wonders whether the discussion was avoided because it would have focused attention on the shortcomings of the rulers.[12]

Finally, a vague commitment to the poor and the downtrodden permeated much of the nationalist political discourse. Gandhi and Nehru in their own ways shared this commitment. It found expression in socialist rhetoric and in policy areas such as land redistribution and the laws governing employment of urban labour. Unlike the commitment to nationalism and statism, however, the commitment to the poor was relatively shallow. India's upper-caste rulers may have meant well, but they were no revolutionaries. Barrington Moore's apt description of Nehru as 'the gentle betrayer of masses'[13] probably applies as well to a fairly broad spectrum of India's political class, though not all of them were always as 'gentle'. How else would one explain the limited political energy devoted to land reform or, for that matter, to promoting widespread access to primary education?[14]

What was the impact of Nehru's economic approach, which was statist in intent and emphasized public investment in heavy industry? The modest economic success of the period brings us back to the twin questions: why, in spite of India's fragmented-multiclass state, was a statist model able to achieve some success and why was the performance not better?

We begin by situating India's initial conditions in a comparative perspective. India's socio-economic conditions at mid-century were probably somewhere between the much more favourable starting point of Korea, or even Brazil, and the considerably worse conditions of, say, Nigeria. On the positive side, India had undergone some industrialization; a small but significant group of indigenous entrepreneurs was in place; banking and other financial institutions existed; and technically trained manpower, though not abundant, was not as scarce as it was in many African and Middle-Eastern countries. The agrarian economy, by contrast, had not grown much over the previous several decades; internal demand was limited; savings were low; experience with managing complex modern production was relatively scarce; and the health and educational conditions of the working population were abysmal. Given these conditions, how well designed was the developmental approach of sovereign India's leaders?

[12]To be fair, Nehru did on occasion blame developmental failures on the bureaucracy, though this also conveniently exonerated him and his Congress colleagues for the state's shortcomings. See, for example, Potter, *India's Political Administrators*, p. 2. A number of government reports also analysed administrative weaknesses of the Indian state, though without much impact. See Bhagwati and Desai, *India*, chapter 8.

[13]Barrington Moore, Jr., *Social Origins of Dictatorship and Democracy: Lord and Peasant in the Making of the Modern World*, Boston: Beacon Press, 1966.

[14]See, for example, Myron Weiner, *The Child and the State in India*, Princeton, NJ:

First, the agricultural sector: Nehru's approach to this sector was mainly 'institutional' in the sense that he and India's economic planners hoped that by tinkering with agrarian relations (via land reforms, for example) and by educating the peasantry (via extension programmes, for example), India's agricultural production would improve.[15] After some significant initial public investments, especially in irrigation, the agricultural sector was therefore more or less ignored at the expense of industry. The results reflected this neglect. Agricultural growth was barely able to stay ahead of population growth. More serious was that much of this growth was extensive and not intensive; that is, it was the result of bringing more land under cultivation, not of improving productivity.

The modest increases in agricultural production thus reflected increasing labour input—growing population—and the use of additional land facilitated in part by new public investments in irrigation. Beyond this, the repeal of a variety of colonial-era taxes on agriculture may have created some incentives for agrarian producers that contributed somewhat to higher rates of production. Conversely, the state's downward penetration was minimal and, hence, so was its capacity to alter agrarian relations.[16] The relative neglect of public investments in better irrigation and higher use of such other agricultural inputs as fertilizers further undermined the prospects of rapid increases in food production. By the mid-1960s, then, India's agricultural sector was on the verge of crisis.

Heavy industry, by contrast, was emphasized by Nehru, who used the tremendous legitimacy he enjoyed to pursue his priorities and translate goals into outcomes. In truth, constructing heavy industry was more readily influenced from the political apex than, say, agriculture or land redistribution. The imposition of substantial tariffs and quotas provided a protected environment in which industry could take root. The bulk of this growth, facilitated by rapidly growing public savings and investment, was in the public sector: further development of electricity, railways, and communication, and in such areas as machineries and steel.

The main source of growing public revenues was indirect taxation, especially of consumer goods. There were, consistent with India's socialist leanings, progressive income tax laws in place, but the government's capacity to collect them was limited—a problem that, over time, would become quite consequential. Indirect taxation sufficed in this early period because the government's non-developmental expenditures were minimal: Nehru's

[15]For a good discussion, see Gunnar Myrdal, *Asian Drama*, New York: Pantheon, 1968.

[16]I have analysed this issue of the state's limited downward reach in detail elsewhere. See Atul Kohli, *The State and Poverty in India: The Politics of Reform*, Cambridge: Cambridge University Press, 1987.

government spent little on health and primary education, underlining the superficial quality of India's socialism. Moreover, his considerable legitimacy minimized the need to throw money at one group or another to buy political support. The levels of political mobilization in India were also relatively low at this early stage, with much of the lower-class population deeply enmeshed in traditional patron-client relationships. Hence, public expenditures could stay focused on Nehru's priorities, especially the development of heavy industry, which generated substantial production growth.[17]

Critics of this strategy have documented that this growth was quite expensive, in the sense of being relatively inefficient.[18] Some of the underlying causes are inherent to the nature of public sectors—for example, investment in industries that are not immediately profitable or below-market social pricing of output. But others were specific to India: the role of generalist bureaucrats, ill equipped to manage public sector industries, and/or the growing political interference by lower-level political elites who treated public sector industries as one more resource in their patronage networks. The highly protected environment within which these industries operated also contributed to the accumulating inefficiencies.

The Indian state's attempts to guide the private sector have also been roundly criticized.[19] These criticisms, however, need to be kept in perspective. As the role of private capital in industry at this early stage was not all that significant, the prominent role assigned to the public sector is better understood as providing a substitute for a laggard private sector. After all, India's private sector had hardly flourished in the pre-independence period under nearly free-market conditions. That said, however, the socialistic Nehruvian state—unlike the South Korean state—sought more to tame than to encourage private sector development. State intervention had a decidedly regulatory cast. Instead of asking business what it could do and how the state could help, the state itemized what private business could not do and then raised numerous barriers to what it could do. Implementation, too, was haphazard and inefficient: for example, priority industries were not always the ones that enjoyed maximum protection, and overbearing bureaucrats in charge of licensing often deterred private investors. The growing maze of bureaucratic obstacles to private sector development led over time to corruption and to inefficient allocation of private sector resources.

[17]For a good review, see K.N. Raj, *Indian Economic Growth: Performance and Prospects*, Delhi: Allied Publishers, 1966.

[18]See Bhagwati and Desai, *India*. See also Jagdish N. Bhagwati and T.N. Srinivasan, *India*, New York: National Bureau of Economic Research, distributed by Columbia University Press, 1975.

[19]See Bhagwati and Desai, *India*, esp. pt 6.

The examples of the steel and textile industries help to fill out this broad account of the Nehruvian state's role in promoting public and private sector industries, respectively. The indigenous steel industry was initiated in the first half of the twentieth century by the Tatas.[20] To advance their nation-building goals, Nehru and his political colleagues prioritized the development of steel in the 1950s.[21] But, as in South Korea and Brazil, state elites found the private sector not forthcoming. It is true that in India some private steel industries, such as that of the Tatas, continued to flourish, but given the size, complexity, and risk involved, other private sector start-ups were not on the horizon.[22] Steel, therefore, emerged as the leading candidate for public sector development.

But in India, unlike in South Korea and Brazil, the steel industry grew up relatively inefficient, not very competitive internationally. A blanket condemnation of public sector ownership clearly will not do, as steel in all three cases was developed in the public sector. Rather, the culprit was the differing nature of states and patterns of state intervention. Moreover, the problems in India developed only over time. Under Nehru, substantial public investments were devoted to steel and foreign collaboration was sought to help to establish and manage the steel plants. Competent senior bureaucrats at the Planning Commission were responsible for steel policy, and there were good management practices at the plant level. The overall protected environment generated by the import-substitution policy regime ensured a ready market in an economy in which industrialization had begun in earnest. The result was that steel production in India between 1950–64 grew rapidly at a rate of nearly 11 per cent per annum.

The real problems of the steel industry date to the Indira Gandhi period, when it was starved of new investments and thus of new technology and modernization. It was then that the fragmented-multiclass nature of India's developmental state came to the fore to cause problems for the steel industry. First, locational issues that were politicized by India's federal structure were exacerbated during Indira Gandhi's period. Second, policy making was in

[20]I am indebted to my research assistant, Rina Agarwala, for collecting this information on the steel industry.

[21]A useful recent account of the state's role in India's steel industry is Vibha Pingle, *Rethinking the Developmental State: India's Industry in Comparative Perspective*, New Delhi: Oxford University Press, 1999, chapter 3. Earlier accounts include W.A. Johnson, *The Steel Industry of India*, Cambridge: Harvard University Press, 1966; Padma Desai, *The Bokaro Steel Plant: A Study of Soviet Economic Assistance*, Amsterdam: North-Holland, 1972; and Gilbert Etienne, *Asian Crucible: The Steel Industry in China and India*, New Delhi: Sage, 1992.

[22]Vibha Pingle thus notes that T.T. Krishnamachari, a successful industrialist, Nehru's confidant, and subsequently minister of steel, approached Indian industrialists but in vain. It was only then that he and Nehru were persuaded that the state would have to undertake

the hands of generalists, the IAS bureaucrats, whose relations with plant-level management were at best remote and at worst condescending and demoralizing for the technocrats. Third, pricing and distributional policies were politicized, with especially damaging consequences. Steel prices were kept below market price and became a public subsidy to a variety of industries, including private sector industries. Although justified in terms of the needs of rapid industrialization, the policy could be sustained only as long as ample public resources to support such subsidies were available. A critical constraint was the state's limited capacity to undertake direct taxation, especially in the countryside, where formal political penetration was minimal. Controlled prices were also a constraint on steel industry profits, reducing its capacity for self-sustaining investments. As long as steel was a priority sector during the Nehru period, with continuous infusion of new resources, these problems remained manageable, and fairly impressive growth continued.

By contrast, large-scale textile production performed rather poorly in Nehru's India, even though at the time of independence, the textile industry, concentrated in private hands in western India, was not insubstantial. It is possible that with pro-business state intervention and subsidies for exports, India's textile production could have become internationally competitive. This was not to be so, however, and the state's legitimacy-driven policy choices were the root cause.[23] We have seen that Nehru was not especially supportive of private enterprise. And within this framework, textiles faced special obstacles.

Recall that the issue of the destruction of small-scale, household-based textile production at the hands of modern textiles played a central role in India's nationalist imagination. Gandhi successfully exploited *khadi*, or hand-spun cotton, as a tool of political mobilization, as witnessed in the symbolism of the Congress elite donning khadi uniforms and caps. With this political inheritance it would have been very difficult to unleash modern textile manufacturing against small-scale production. Mahatma Gandhi's populist commitment to 'love of the small people' cast a long political shadow on India's textile policy. (While championing khadi, however, Gandhi was simultaneously collecting large dues for the Congress from his close friend, textile manufacturer G.D. Birla.) Add to this Nehru's socialist proclivities,

[23]See, for example, S.R.B. Leadbeater, *The Politics of Textiles: The Indian Cotton Mill Industry and the Legacy of Swadeshi (1900–85)*, New Delhi: Sage Publications, 1993; and Sanjib Misra, 'India's Textile Policy and the Informal Sector', in Stuart Nagel (ed.), *India's Development and Public Polity*, Aldershot Ashgate: Policy Studies Organization, 2000. For analysis of related economic issues, see Howard Pack, *Productivity, Technology and Industrial Development: A Case Study in Textiles*, New York: Oxford University Press, 1987; and Keijiro Otsuka, Gustav Ranis, and Gary Saxonhouse, *Comparative Technology Choice in Development*, Basingstoke, Hampshire:

which inclined him to argue in favour of producing cheap cloth for mass consumption, and the political factors moulding policy choices start to become comprehensible.

Nehru and his colleagues restricted production of textile mills, taxed them highly, and even priced a part of their output below market prices so as to provide cheap cloth for poor consumers. Contrast this pattern of intervention with the one encountered in Korea and Brazil, where state intervention was often supportive of producers, though the political framework necessary for that support was also much narrower and more repressive. This contrast also underlines a central argument of this study, namely, that variations in patterns of state intervention are what matters most when trying to understand varying roles that states play in late-late-development. Thus, Nehru's textile policies undermined private and large-scale textile manufacturing in India but encouraged small-scale textile manufacturing, first with hand looms and then with power looms. Support, that is, went for anything that was less than a modern textile mill, with commensurate consequences: output of large mills nearly stagnated, while that of smaller producers grew sharply. The latter were suitable for the low-end market consumption but not for competitive exports.

The story of industrialization in Nehru's India is thus mixed, characterized by notable achievements but also stupendous follies. As demonstrated with examples of steel and textiles, both these successes and limitations are explicable in terms of the underlying patterns of state intervention. Thus, India's 7 per cent industrial growth rate per annum in this period was respectable. But Brazil in the same period—one of the fastest growers in the world and also a democracy with a strict import-substitution policy regime—industrialized at a rate of nearly 10 per cent per annum. This somewhat superior performance also reflected underlying political and policy differences. The rate of investment in Brazil and India in this phase was more or less comparable. The real difference thus was in capital-output ratios, or in the relative efficiency with which capital was invested in the two countries. The roots of this difference, in turn, can be traced back to the fact that Brazilian democracy was considerably less nationalist and mass-based than that of India. Brazilian leaders thus worried less than India's leaders about legitimacy issues of nationalism or redistribution. The clearest manifestations of this greater political room for manoeuvre in Brazil were the closer cooperation between the state and business and the heavy dependence on foreign investment to facilitate import-substitution industrialization. While this strategy was not without its own problems, the advanced technology and management that foreign investors brought to Brazil was an important reason for Brazil's more rapid industrial growth in this early phase.

THE INDIRA GANDHI ERA

If democracy and a nationalist-statist model of economic development took root in India during the Nehru era, the political economy of the Indira Gandhi era that followed is best viewed as one in which India's democracy became more populist and deinstitutionalized, economic rhetoric moved further to the Left, and the gap between the state's developmental capacities and economic goals widened even further, to the detriment of industrial development. Nehru's death in 1964 marked the slow but steady departure of the first generation of nationalist leaders from the political scene. As nationalist legitimacy declined, numerous movements and parties opposing Congress's hegemony emerged. The party's old ruling formula—a mantle of inclusive nationalism and long chains of patronage fed by statism—was increasingly incapable of generating electoral majorities. Either Congress had to come up with a new winning formula or it would give way to other parties. It was Indira Gandhi who stepped in and provided the winning strategy that revived Congress's sagging fortunes. But her populism and top-down deinstitutionalization of the polity further accentuated its fragmented and multiclass character, with significant developmental consequences.

Under Nehru, India had undergone steady industrialization and experienced modest economic growth, but the poor had not benefited very much. Indeed, the spread of commerce and democracy had eroded patron-client ties, making the poor ripe for new forms of political mobilization. A savvy Indira Gandhi understood these changes and capitalized on them,[24] turning 'poverty alleviation' into her central political slogan. This shift to the Left in India's political discourse yielded handsome short-term political dividends. Indira Gandhi became a darling of India's downtrodden, but her popularity, unlike her father's, was not institutionalized. Whereas he had presided over a nationalist party, the daughter found herself opposed by the old, entrenched Congress elite. Her solution: label the old elite enemies of the poor, exploit her popularity to undermine their power, and appoint loyal minions to positions of responsibility. As India's political system thus became increasingly personalistic, well-established patterns of authority within the party were undermined, and the broader process of institutional development in India's democracy was derailed.[25]

[24] Good biographical studies of Indira Gandhi include Mary Carras, *Indira Gandhi: In the Crucible of Leadership: A Political Biography*, Boston: Beacon, 1979; and Pupul Jayakar, *Indira Gandhi: An Intimate Biography*, New York: Pantheon, 1992.

[25] This theme of deinstitutionalization of the Indian polity under Indira Gandhi is emphasized and developed in Atul Kohli, *Democracy and Discontent: India's Growing Crisis of Governability*, Cambridge: Cambridge University Press, 1991. See also Atul Kohli (ed.), *India's Democracy: An Analysis of Changing State–Society Relations*, Princeton, N.J.: Princeton University

The logic of this process of personalization of power was inexorably deinstitutionalizing. Challenged in an increasingly contentious polity, Indira Gandhi not only eliminated her challengers but also weakened the institutions that enabled such challengers to emerge: she tampered with appointments in the civil service and the courts, dismissed 'troublesome' chief ministers, and demanded absolute loyalty from supporters. As a result, the professionalism of the bureaucracy, the independence of the legal system, the functioning of the national parliament and the autonomy of the regional units within the national federation were all adversely affected.

The changing nature of the bureaucracy is especially noteworthy. Though slow and not dramatic, the changes were nevertheless significant, mainly in the direction of undermining the professionalism of the civil service that India inherited from the British. The size of the IAS continued to grow throughout this period, quadrupling between 1950 and 1983.[26] This reflected the overall growth of the public sector, in which employment grew from some four million in 1953 to ten million in 1983. By the end of this period, the IAS employed some 4,000 officers, about 15 per cent of whom served in New Delhi, 25 per cent in the districts, some 10 per cent in public sector enterprises, and the remaining 50 per cent in various state capitals. The basic structure of the IAS in terms of its size within the overall public service or in terms of its distribution across various types of jobs (with the significant exception of public sector enterprises, of course) did not undergo any dramatic changes from earlier times. What changed instead was the diminishing degree to which the IAS was insulated from the broader society, the erosion of professional criteria for internal promotion, and a greater premium placed on connections and loyalty to politicians for securing desirable positions. To some extent these changes reflected the expected indigenization of a colonial state, but they also reflected the priorities of the political elite, as holding on to power became an end in itself.

So, too, Indira Gandhi focused less on matters economic and more on maintaining power. Nehru's statist model of economic development thus essentially continued without major change. Within the framework of continuity, economic policy changes during this era were mainly of two types: a major shift in agricultural policy that had a benign long-term impact on food production and a variety of left-leaning changes that reflected Indira Gandhi's political calculus but helped neither economic growth nor redistribution.

Press, 1988. For a somewhat different interpretation, see Lloyd Rudolph and Susanne Rudolph, *In Pursuit of Lakshmi*, Chicago: University of Chicago Press, 1987.

[26]The factual information here is drawn from David Potter, *India's Political Administrators*, chapter 4.

Looked at broadly, this was an era of missed economic opportunities in India at a time when other countries exploited such opportunities. From the mid-1960s on, the global economy became more open to manufactured exports from developing countries,[27] and countries as diverse as South Korea and Brazil sought to take advantage of such global shifts. These countries, of course, came to be ruled by military dictators who prioritized economic growth and sought export promotion as an additional strategy. By contrast, India, after a brief flirtation with devaluation in 1966, moved in nearly the opposite direction, becoming more and more obsessed with 'politics'.[28] Indira Gandhi's personalistic governance led India down a path on which democracy was maintained, though tenuously, but on which economic policies became further politicized. And the gap between the state's economic rhetoric and its capacity to implement grew only wider.

A set of agricultural policies adopted in the mid-1960s eventually produced India's 'green revolution'. Insofar as these policies sought to concentrate production inputs in the hands of landowning classes in some regions of India, they did not readily fit in with Indira Gandhi's populist designs. Why and how were these policies adopted?[29] First, they were adopted in the mid-1960s, just before Indira Gandhi's full embrace of 'poverty alleviation' in the late 1960s. More important, India faced severe food shortages in 1965 and 1966, which made the country more open to seeking ways to boost food production and temporarily more dependent on food aid, especially from the United States. The United States favoured green revolution policies and pressured India to adopt them in exchange for aid. But the adoption of these policies was such a politically sensitive matter, in terms of both external dependence and possible distributional consequences, that policies were essentially adopted by a handful of the political elite as executive decisions rather than through any open political discussion.

Various other social and economic policies adopted by Indira Gandhi in the 1970s were aimed at legitimizing populist politics. While the significance of some of these was more symbolic, others turned out to be quite economically consequential. Among the more symbolic—and thus politically consequential—were the removal of privileges that Indian government

[27]See, for example, W. Arthur Lewis, *The Evolution of the International Economic Order*, Princeton, NJ: Princeton University Press, 1977, chapter 6. See also W. Arthur Lewis, *Dynamic Factors in Economic Growth*, Bombay: Orient Longman for the Dorab Tata Memorial Lecture Series, 1974.

[28]For a discussion of the brief experiment with devaluation, see Bhagwati and Srinivasan, *India*.

[29]For a good account, see John P. Lewis, *India's Political Economy: Governance and Reform*, New Delhi: Oxford University Press, 1995, chapter 4. See also Frankel, *India's Political Economy*, chapter 7.

hitherto provided to Indian princes. More economically consequential, Indira Gandhi intensified the rhetoric but also to some extent the efforts to implement land reforms. Land redistribution was a fairly central component of the new 'poverty alleviation' strategy, though the actual impact was quite limited.[30] Similarly, the nationalization of the banks was supposed to 'democratize' lending and so was popular among Indira Gandhi's constituents.

Among the economically most consequential policy developments, the following had an adverse impact on economic growth. First, Indira Gandhi held her populist coalition together by channelling public resources to numerous interest groups—a case of largess that cut into public investment and hurt economic growth.[31] Second, the radical political rhetoric, some seemingly radical policies, and a new level of labour activism alienated private investors, both domestic and foreign. These policies included restricting the growth of private business and industry, nationalization of banks and threats to nationalize other industries. And third, India's closer political links with the Soviet Union and a parallel distancing from the West made it difficult for the Indian economy to derive benefits that might come from further integration with more dynamic economies.

With Indira Gandhi's addition of populism to the statist model of development, the gap between the state's ambitions and capacities that had already existed in Nehru's India grew even wider, and India's fragmented-multiclass developmental state became even less developmental. For example, Indira Gandhi raised the expectations that her policies would help to alleviate poverty—a demanding task that would have required high rates of economic growth, some effective redistribution, and the capacity to penetrate and reorganize the rural society. This demanding task, in turn, would have required a cohesive political party and bureaucracy. Indira Gandhi, however, achieved the opposite, by further deinstitutionalizing the Congress party, further fragmenting the state's authority structure and undermining the professionalism of the bureaucracy. And instead of enhanced public investment in agriculture, infrastructure, public sector industries, and education and health, the state's resources were increasingly directed at buying political support. With growing politicization, the bureaucracy and public enterprises simply deteriorated. And finally, the state simply did not support the private sector and became increasingly anti-capital, with predictable negative results for investment and growth.

As is evident in the figures in Table 5.1, India's economy did not perform very well between 1965 and 1979. As we have seen, Indira Gandhi's populism

[30]For an analysis of related failures, see Kohli, *State and Poverty in India*.

[31]See Pranab Bardhan, *The Political Economy of Development in India*, New Delhi: Oxford University Press, 1998.

especially hurt industrial growth. The intervening links need to be clarified, but first a few comments on the agricultural sector. Indira Gandhi's agricultural strategy, adopted under conditions of crisis and external pressure, concentrated agricultural investment in providing better seeds and fertilizer to regions with assured irrigation, such as the Punjab. Price supports were also provided for food producers, thus shifting the terms of trade somewhat in favour of the countryside.[32] While the distributional consequences were decidedly mixed, the new policies did help to improve agricultural production.

On the face of it, the aggregate figures in Table 5.1 do not support this view: agricultural growth between 1965 and 1979 was lower than in the earlier period. However, much of this new growth was based on higher yields. With the possibility of bringing more land under cultivation more or less exhausted—certainly without major public investments in irrigation—productivity-based food growth was essential to feed the growing population. Dramatic increases in wheat production undergirded this new growth, pulling India back from the brink of famine and mass starvation. The state intervened massively to support those property-owning elites who were most likely to generate economic growth, with benign consequences for production. While state intervention was a result of a crisis and though the intervention was concentrated in the agrarian rather than the industrial sector, this alliance of the state and the propertied class is reminiscent of the East Asian cohesive-capitalist state. Over time even the industrial sector moved in this direction but not before a significant populist interregnum and not without being pressed by yet other economic crises.

Industrial growth in India decelerated sharply during 1965–79, leading some observers to dub this an era of 'stagnation'.[33] The underlying cause was mainly declining investment, but there were also accumulating inefficiencies, and both of these, in turn, can be traced back to growing populism. While the rate of investment for this period (see Table 5.1) was higher than in the earlier period, a more disaggregated picture clarifies the apparent contradiction. The higher aggregate rate mostly reflected savings (and thus assumed investment) in the household sector, where the majority of non-consumed resources were maintained in the form of physical assets and were therefore not readily translated into investments with high rates of return. More

[32]For a useful discussion of the politics of agricultural policy, especially of issues surrounding debates on terms of trade within India, see Ashutosh Varshney, *Democracy, Development, and the Countryside: Urban-Rural Struggles in India*, New York: Cambridge University Press, 1995.

[33]See, for example, Isher Judge Ahluwalia, *Industrial Growth in India: Stagnation since the Mid-Sixties*, New Delhi: Oxford University Press, 1985.

significant was thus the behaviour of public and corporate savings in this period, both of which decelerated.

The decline in public investments reflected both a failure to add to the revenue base (for example, by taxing new agricultural incomes or by generating surpluses in public enterprises) and growing public expenditures in such 'non-developmental' areas as 'subsidies' aimed at securing political support.[34] This pattern was a direct function of Indira Gandhi's growing populism: she essentially threw public resources at numerous social classes she sought to mobilize. As public investments declined, industrial growth was hurt on both the supply and the demand side.[35] Infrastructure development suffered, for example, creating serious supply bottlenecks for industrial production. And in the steel industry, reduced public investment hurt production directly. On the demand side also, given the weight of the public sector in India's industrial economy, reduced investment shrank the demand for a variety of industrial outputs, thereby discouraging production.

Since public investments in India have not grown in recent years but industrial growth has, it is also important to consider the role of corporate investments in industrial deceleration during the Indira Gandhi era. Corporate investments also slowed down in this period, especially in fixed capital formation. The underlying causes are difficult to discern but can be traced back to declining profitability. Decline in demand in the overall economy was probably partly responsible. Also at play, however, were more directly political factors. Populist and multiclass politics led to steeper corporate taxes and to labour activism, industrial unrest, and higher wages, probably cutting into profitability. There is also the more diffuse impact of a seemingly left-ward turn in national politics on investor behaviour. While difficult to document decisively, investors may have been discouraged by the growing talk of nationalizing business (and the reality of nationalizing some banks), by new policies that sought to limit their growth and areas of investment, and by the adoption of a general anti-business rhetoric.

Finally, whatever investment was taking place was not always efficient. Since there is little evidence that productivity growth in this period was worse than during the Nehru period,[36] much of the industrial deceleration under discussion cannot be attributed to issues of efficiency. Rather, the main culprit was reduced investment, both public and private. Nevertheless, continuing inefficiencies were certainly at least a part of the overall economic scene. A poorly managed and inefficient public sector repeatedly failed to

[34]For such an argument, see Bardhan, *Political Economy of Development in India.*

[35]For details, see Ahluwalia, *Industrial Growth in India.*

[36]Ibid., especially p. 146, for data; Ahluwalia notes that 'productivity growth estimates do not show a worsening of the situation after the mid-sixties.'

generate investable surpluses and thus contributed to a slowing down of industrial growth. A policy framework that did not encourage domestic competition led to misallocation of resources, hurting growth. Capital-output ratios, a rough indicator of efficiency, increased during this period, especially in manufacturing, underlining that, besides the slowdown in investment, investment was simply not being utilized efficiently.

The evolution of the steel and textile industries can further clarify the changes under Indira Gandhi. After considerable growth in the earlier period, steel production in the public sector stagnated during her tenure, especially between 1964 and 1971.[37] Levels of efficiency in the steel industry also remained relatively low. Again, the roots of many of these problems grew out of the new populist politics. For example, in addition to suffering from a war with Pakistan and droughts in the mid-1960s, public investment declined as well because of Indira Gandhi's new political priorities. The results included declining investment in established steel plants. In the words of one analyst, the steel industry suffered in this period because of 'the state's lack of investment in technological upgrading and plant maintenance and poor plant management.'[38] The problems of an investment-starved industry were exacerbated by low, government-imposed steel prices—again justified in terms of 'socialism'—that deprived firms of internal savings for investment and modernization. And finally, among the political roots of the problems of steel industry was the power of politicized labour. Well-organized unions affiliated with and empowered by the ruling party essentially squeezed the managers of public sector firms, leading to numerous rigidities and inefficiencies.

The problems in textile production, dominated by the private sector, also continued in this period and were probably exacerbated.[39] Controls on the growth of the organized mill sector persisted and were made even more restrictive in the name of protecting handlooms and small producers. The same logic was extended to power looms, a hitherto growing segment of the industry, that had started filling the production space between mills and handlooms. Large mills, moreover, were obliged to provide a significant portion of their output to poor consumers at controlled prices. When less-efficient producers faltered, Indira Gandhi nationalized them. These mills did not perform better in the public sector, at least in part because they were burdened with producing regulated cloth for the low end of the market. Import of new technology was also restricted in order to deal with balance-

[37]See the references in note 21.

[38]See Vibha Pingle, *Rethinking the Developmental State*, p. 61.

[39]See, for example, D.U. Sastry, *The Cotton Mill Industry in India*, New Delhi: Oxford University Press, 1984. See also the references in note 23.

of-payment problems. The political context for private textile manufacturers was thus discouraging and contributed to limited growth in both productivity and production.

Finally, a comment ought to be made about the continuing 'closed' nature of the Indian economy. Irrespective of whether arguments about 'export pessimism' or about the need to protect 'infant industries' were ever technically supportable or not, such attitudes were understandable during the Nehru period, given the prevailing political values and popular economic doctrines of the time. By the 1970s, however, many of these assumptions were being globally challenged. Countries such as South Korea and Brazil were aggressively turning towards export promotion and trying to attract foreign investors. Indira Gandhi's legitimacy-driven politics led her instead to adopt a sharply anti-Western and nationalist political rhetoric, pushing India's economic policies in nearly the opposite direction. As a result, India continued to embrace its import-substitution regime fiercely, as well as to resist foreign investment, again hurting growth in multiple ways. Limited exports, for example, remained a key vulnerability, creating periodic balance-of-payment crises. Moreover, by not pushing exports India was not taking advantage of its key resource, cheap labour; it also limited imports of new technology and discouraged economies of scale. Enhanced foreign investment might also have facilitated growth, not only via additional investments, but also and more importantly by contributing to better technology, management, and export promotion.

Populism may be politically expedient and, on occasion, even a political necessity to balance conflicting interests under conditions of weak political institutions, but its economic impact on growth is seldom benign. The Indian case fits this broader pattern. A more genuine social democratic tilt in India, one that would have reconciled better growth and modest redistribution, would have required a well-organized social democratic party and a durable ruling coalition at the helm of a more effective state. In other words, it would have required a cohesive-multiclass state rather than a fragmented-multiclass state. Short of that unlikely outcome, a charismatic and popular leader, promising radical redistribution within the context of a fragmented-multiclass state and a largely private-enterprise economy, was a recipe for failure. Populism doubly harmed economic growth by hurting public and private investments and by further politicizing the statist and closed economic policy regime.

THE PRO-BUSINESS DRIFT

Following Indira Gandhi's return to power in 1980 and later following her assassination in 1984, Indian democracy entered a new phase, marked by a

to find workable alternatives, culminating in the emergence of a right-wing, religious nationalist party at the helm.[40] While the 1980s and the 1990s were characterized by a fair amount of governmental instability and even political instability, especially by ethnic and communal violence, India's economic policies took on a more consistent character, generally tending in a more pro-business direction—a process dubbed by some observers as economic liberalization. During this phase the gap between governmental economic ambitions and capacities narrowed somewhat, not so much due to enhanced state capacities as to the scaling back of ambitions, both in the productive and the redistributive spheres. Over the last two decades of the twentieth century, in other words, India's fragmented-multiclass state became not so much more cohesive as markedly less multiclass.

Indira Gandhi's departure from the political scene left India without a charismatic leader capable of holding together an increasingly mobilized and heterogeneous political society. Her failure to make a dent in India's poverty also clarified to her successors (and even to her in the early 1980s) the limits of class politics in India; without a well-organized social democratic party, appeals to the lower classes in India quickly devolved into irresponsible populism that simultaneously hurt economic growth and failed to achieve effective economic redistribution. Subsequent attempts to discover new formulas for ruling have moved in one of three directions, none totally successful: maintaining the Nehru–Gandhi family rule, forging new caste coalitions, and encouraging ethnic politics, especially mobilizing Hindu nationalism. The Congress party pursued the first strategy, and a variety of opposition parties followed the second and the third. Since none of these strategies readily translated into enduring national electoral victories, India's regions also gained national political significance by joining coalition governments at the centre.

The most significant political development over the last two decades has been the emergence of the Bharatiya Janata Party (BJP), a right-leaning religious nationalist party, as a major alternative to the Congress. The BJP emerged as India's ruling party towards the end of the 1990s and remains in power at the time of writing (2003). The rise of the BJP needs to be understood in terms of its ability to fill a growing political vacuum. The assassination of Indira Gandhi's son, Rajiv Gandhi, an heir apparent of sorts, deprived Congress of the opportunity to continue to capitalize on 'dynastic popularity'. With the aim of finding an alternative to the Congress, a series of opposition

[40] I have analysed these changes in more detail elsewhere. See Atul Kohli, 'Indian Democracy: Stress and Resilience', *Journal of Democracy*, 3 January 1992, pp. 58–65; Atul Kohli, 'Can the Periphery Control the Center? Indian Politics at the Crossroads', *Washington Quarterly*, 19(4), Autumn 1996, pp. 115–87; and Atul Kohli, 'India Defies the Odds: Enduring Another

parties sought to mobilize hitherto unincorporated middle-caste groups but failed due to factionalism and leadership rivalries, not to mention the absence of any clear political programme.

As a better-organized party, the BJP stepped into this vacuum and sought to unite India's Hindu religious majority into a nationalist political bloc. In a programme reminiscent of European fascist movements, this party sought politically convenient enemies, both within India—India's religious minorities, especially Muslims—and beyond India's borders. The reformulation of Indian nationalism along religious lines paid off handsomely for the BJP, but not enough to win a national electoral majority. The party's appeal remained concentrated in those central areas of India where memories and symbols of rule by Muslims remain mobilizable. Coalition alignments, as well as experience with democratic governance, softened the more extreme elements of the BJP, enabling it to provide a viable alternative to the old Congress, at least over the short term. How the BJP will evolve in the future, however, remains an open question.

From the standpoint of this discussion, it is important to note that shifting governments and coalitions of the last two decades have not translated into sharp economic policy instability. While there have been fluctuations, economic policies over the last two decades have generally moved in a liberalizing or, more precisely, pro-business direction, both dismantling some of the inherited state controls on private economic activities and distancing the state from the rhetoric of redistribution and populism. How can one explain this shift, as well as its consistency, in the face of governmental instability? A few comments will help to round out the story.[41]

Neither state-led economic growth nor political efforts at redistribution and poverty alleviation have proved to be especially successful in India. State capacity to push either the Korean type of high economic growth or the Chinese type of radical poverty alleviation has simply been missing. The more this understanding of past failures seeped into the gestalt of India's political class, however, the more it embraced pro-business solutions to its development problems. Even Indira Gandhi in her later years quietly de-emphasized poverty alleviation as a slogan and courted the business class she had alienated earlier on. Her son, Rajiv Gandhi, embraced the rhetoric of economic liberalization, though in practice his attempts to dismantle India's statism ran into numerous obstacles.[42] Subsequent national governments have more or less maintained a rhetorical commitment to liberalize the

[41]One recent book on politics of India's economic liberalization is Rob Jenkins, *Democratic Politics and Economic Reform in India*, New York: Cambridge University Press, 1999.

[42]For a full discussion, see Atul Kohli, 'Politics of Economic Liberalization in India', *World Development*, 17(3), March 1989, pp. 305–28.

economy, moving in fits and starts to produce an incremental progress that suits a large, complex democracy. When questioned as to why, in spite of its nationalist orientation, the BJP sought to liberalize and open India's economy, India's current prime minister, Atal Bihari Vajpayee, replied: 'Nehru Ji's approach was not all that successful. Indira Ji was never sincere. What else can we do now?'[43]

The growing sense among leaders that past strategies were not enormously successful and that there is no alternative but to liberalize is probably the driving force behind the shift in India's development strategy. A moment of reflection, however, suggests that past failures could have been interpreted differently, with different implications for policy. For example, India's leaders could have embraced more fully the model of East Asian 'developmental states', or, less likely but not totally out of question, they could have embraced a more genuine social democratic model based on what has been tried in such Indian states as West Bengal and Kerala. The fact that they did not, in turn, points to another key factor that has pushed India's new economic choices: the liberalizing trend is consistent with dominant interests and ideas, both within India and abroad.

In spite of its socialist flourish, India's statism provided a framework for the emergence of a largely capitalist economy in India. The more Indian capitalism has matured over the last few decades, the more difficult it has become for India's leaders to maintain anti-capitalist political positions. Even India's communist parties now accept market realities and seek to attract private investors. The shifting nature of the political economy has thus bounded the range of economic choices available to India's leaders. International pressures have further reinforced these boundaries. Just as at mid-century statism appeared to be a 'natural' path to adopt worldwide, towards the end of the century the virtues of markets appeared nearly hegemonic.[44] India's leaders could have resisted these national and international constraints, but that would have required considerable political cohesion around alternative values. Having not done so, however, nearly all of India's political parties have sought to work with powerful interests and ideas, especially anti-statist,

[43]This is a translation of a conversation in Hindi between Mr Vajpayee and Atul Kohli in Oxfordshire, England, 19–21 June 1992. Mr Vajpayee at the time was a leader of the opposition in the Indian parliament, and both he and the author were attending a conference on 'India: The Future', organized by the Ditchley Foundation.

[44]This sweeping gestalt shift, which has an ideological quality, should give thoughtful observers a pause. The earlier embrace of statism led to some successes and numerous failures. The new commitment to markets is also likely to lead to a similar, mixed record that will be evident only in the future. For one useful account of this shifting economic mind-set, see Paul Krugman, 'Cycles of Conventional Wisdom on Economic Development', *International Affairs*, 72(1), 1996, pp. 717–32.

pro-business ideas, thus narrowing the range of available options in the economic sphere.

Nonetheless, despite a commitment to economic liberalization, India's political economy still remains quite statist by global standards. Unlike South Korea or Brazil in the 1990s, there was no basic shift in India's development model in the 1990s. Thus, public enterprises remained very significant, tariffs came down but were far from negligible, the role of foreign investment in the economy was minimal, numerous laws governed capital movements in and out of the country, and a variety of labour laws made the economy anything but a model of flexibility. This is neither an endorsement nor a criticism of the state of affairs. The analytical point is that, during the last two decades of the twentieth century, India's leaders sought to liberalize the statist economy they had inherited. This liberalization, while real, was also limited—a mixed result consistent with powerful political forces in India, since a variety of interest groups, especially business, objected to some aspect or another of a radical policy shift. Weak governments, in any case, were reluctant to undertake major policy restructuring. The policy shift in India is thus better understood as a pro-business drift rather than as economic liberalization, but a policy drift that has nonetheless facilitated improved rates of economic growth.

India's rate of economic growth improved between 1980 and 2000 and averaged nearly 6 per cent per annum (Table 5.1). This higher rate was in part a statistical artifact insofar as it reflected the growing share in the national economy of the fast-growing industrial and service sectors. Nevertheless, agricultural growth over the last two decades must be judged satisfactory as both industry and services grew at some 6 to 7 per cent per annum, propelling India into a group of relatively fast growers in the world. How does one explain this improved performance, especially in light of our focus on the role of the state and of state policies? The discussion distinguishes between the higher growth rates in the 1980s and those in the 1990s: growth in the 1980s was debt-led, especially by a growing public debt, and growth in the 1990s was driven by higher rates of investment in the private corporate sector.

Other underlying factors that may have also contributed to this outcome ought to be noted. During the Nehru period India invested in heavy industry and in higher technological education to feed this industry. Returns on these investments typically take time, and India may now be benefiting from these earlier decisions. Consequently, entrepreneurial and managerial skills have been slowly but steadily accumulating in India and probably contributed to better economic performance. There is also some evidence that the structure of industry is steadily shifting towards consumer industries where capital-output ratios are generally lower. India may also have just been lucky over the last two decades, with a spate of good weather, growing

TABLE 5.2: Patterns of Capital Formation, 1980–98
(percentage of GDP)

Period	Total Gross Capital Formation	Private Corporate Sector	Public Sector
1980–5	21.9	4.3	10.2
1985–90	23.7	4.5	10.5
1990–5	23.7	6.0	9.1
1995–8	24.0	8.3	7.0

Source: Adapted from Rakesh Mohan, 'Fiscal Correction for Economic Growth', *Economic and Political Weekly*, 10 June 2000, p. 2028, table 4.

and trade. And finally, as in true for such other cases as Brazil as well, prior industrialization creates its own efficiencies for future industrialization by providing a trained workforce, dense supplier networks, demand for goods, and a supportive tax base.

In spite of the potential relevance of such non-policy variables, there is still something significant to explain. As is clear in Table 5.2, higher growth rates, over the last two decades were accompanied by higher rates of investment, increases that originated in the public sector in the 1980s and in the private corporate sector in the 1990s. What explains these higher rates of investment? Also, what role, if any, have attempts to liberalize the economy played in this improved economic performance? The Indira Gandhi who returned to power in 1980 was considerably less populist than the one in the 1970s. She thus initiated an era—especially marked by a more pro-business Industrial Policy Resolution in 1982—that increasingly came to be characterized by growing silence on issues of deliberate poverty alleviation and by greater public attention directed towards the promotion of economic growth. The appropriate strategy for promoting growth has been evolving. There was a lot of talk of liberalizing the economy in the second half of the 1980s, when Rajiv Gandhi was in power. While some pro-business policy measures—such as a reduction in corporate taxes—were indeed passed, overall liberalization was fairly limited; for example, the average rate of tariffs in India in 1990 was still over 100 per cent.

Following a balance-of-payment crisis in 1991, there was some significant liberalization, especially of the internal economy from state controls, but the pace of change, especially of 'opening' the economy to the world, slowed in the second half of the decade.[45] Tariff rates in India at the end of the century still averaged close to 40 per cent and foreign investment was minuscule compared to, say, China. What continued steadily throughout

[45]For a discussion of policy changes in the 1990s, see Shankar Acharya, 'Macroeconomic

the two decades, however, was a move away from populism and towards a focus on economic growth, and relatedly towards a warmer embrace between the state and national business. The argument I am proposing is that this shift in state priorities and alliances is an important ingredient in improved economic performance.

As discussed above, there was substantial evidence in India in the 1970s of a link between declining public investments and deceleration of industrial growth. With changed priorities, subsequent governments decided that one way to improve growth was to boost public sector investments. This is precisely what happened during the 1980s.[46] The government channelled new investments into promoting infrastructure and industries that provided key inputs for intermediate and final goods, which promoted higher rates of growth. While the direct contribution of an increase of some 2–3 percentage points in public investment to overall growth may be fairly small, given the significance of such bottlenecks as infrastructure, the indirect contribution of this new investment for growth was in all likelihood much more significant.

How was this new public investment financed? Recall that the economic capacities of the Indian state during the Indira Gandhi years had deteriorated, as politicization of the bureaucracy made it difficult to collect more taxes or to improve the performance of public sector enterprises. Some new public resources were found in further taxing international trade (hardly a route to improving economic performance!), but for the most part the role of new resources was limited. The government also did not cut back on the variety of its non-developmental expenditures, such as subsidies. Given weak political parties—essentially, personalistic groupings—it was increasingly difficult to hold together ruling coalitions. Public monies continued to play a key role in buying and maintaining political support. The government thus pursued the only option it thought it had, namely, borrowing—mainly internally but also externally. Given that this borrowed money was being invested in areas with low financial returns and often through inefficient public firms, the results included accumulating debt that created the twin crises of internal and external debt in 1991.

Meanwhile, the economy grew at a handsome rate of nearly 6 per cent throughout the 1980s. Increasing public sector investment was one component of this growth. Private investments also grew, though not by much. There is, however, evidence of improvements in the productivity of investments,

[46]See, for example, Rakesh Mohan, 'Fiscal Correction for Economic Growth: Data Analysis and Suggestions', *Economic and Political Weekly*, 10 June 2000. He concludes that 'what becomes clear from examination of the data is that the 1980s were characterized by a significant increase in public sector investment as well as other government expenditure' (p. 2028).

especially in private manufacturing.[47] The underlying causes are not readily evident. Joshi and Little conclude that 'the high level of demand in the 1980s' may be an important part of the explanation.[48] As noted, the roots of this were also the debt-led increase in public expenditure.

The Indian economy continued to grow at nearly 6 per cent per annum during the 1990s as well. It will be a while before all the relevant data for the most recent period is analysed and the underlying determinants of the continuing high growth become clear.[49] Some trends are already evident, however. The crisis of 1991 and the related agreements that the Indian government reached with the IMF led to pressure on government deficits. It is difficult for India's fragmented-multiclass state to collect new taxes, to improve the performance of public enterprises, or to cut back on the various supports and services it provides. The main strategy for debt management is thus evident in Table 5.2, namely, in declining public sector investments. This trend may hurt growth and development in the future, especially because of the woeful state of India's infrastructure but also because of the pressing need to invest more in basic education and health.[50]

In spite of a decline in public sector investments, overall economic growth did not suffer, mainly because private sector investments grew and the share of corporate investments in the GDP actually surpassed the share of public sector investments (see Table 5.2). Private sector industrial investment in India was generally quite productive, though new investment was only partly in new industries. And the industrial sector, especially manufacturing, did not perform all that handsomely in the 1990s. The real locus of growth shifted instead to the less-regulated service sector, especially to exports of information technology, as India's accumulating manpower resources in this area found a niche in the global market.

The success of India's computer industry, including software exports, presents a good example of these broader, changing patterns of state-business relations.[51] The roots of this success are generally traced to policy changes

[47]See, for example, Vijay Joshi and I.M.O. Little, *India: Macroeconomics and Political Economy*. Washington, D.C.: World Bank, 1994, chapter 13. Joshi and Little argue that increased investments were too small to explain higher growth rates, which is surprising in light of their own evidence (see p. 327) that public sector investments averaged 7.7 per cent of the GDP between 1960–1 and 1975–6 and 9.9 per cent between 1976–7 and 1989–90. For a discussion of the 'multiplier effect' of public investments in India, see Ahluwalia, *Industrial Growth*.

[48]Joshi and Little, *India*, p. 328.

[49]One such preliminary attempt is Acharya, 'Macroeconomic Management in the Nineties'.

[50]See, for example, Mohan, 'Fiscal Correction'.

[51]See, for example, Peter Evans, *Embedded Autonomy: States and Industrial Transformation*, Princeton, N.J.: Princeton University Press, 1995; and Pingle, *Rethinking the Developmental State*, chapter 5.

in the late 1970s and then especially in 1984 under Rajiv Gandhi, who prioritized this sector for growth. Reminiscent of state-business cooperation in Korea, the Indian government during the 1980s and the 1990s reduced regulations and licensing requirements for this industry, reduced import duties and promoted exports with aggressive marketing in overseas markets. At home, the state helped to create industrial parks and software technology parks with a communications infrastructure, provided core computer facilities and engaged in a type of intervention generally more supportive than regulatory. This strategic state-business alliance was an essential component of the remarkable performance of the software industry, which grew at a rate of more than 50 per cent per annum during the 1990s.

Beyond the information-technology industry, the factors that help to explain growing private sector investments and pockets of dynamism more broadly are the state's increasingly pro-business policies. Over the last decade or so, India's various governments have cut corporate taxes, provided a variety of supports to business, especially for exports, sought to tame labour—evident in the substantial decline of man-days lost due to strikes[52]—and relaxed public controls on entry, exit, and expansion. Tax reforms have included across-the-board reductions in rates and simplification of procedures for paying direct and indirect taxes, lowering of import tariffs by almost one-third between 1990 and 1996, dispensing with industrial licensing agreements for most industries, allowing new entrants—private, semi-private, and foreign—into the banking system and capital markets, and opening up sectors such as power and telecommunications that had previously been limited to the public sector. While champions of liberalization may see all these measures as evidence of a growing free market in India, it remains the case that India's state is still heavily interventionist and that the Indian economy is still relatively closed to external goods, finance, and investors. The policy trend is thus better interpreted as a right-ward drift in which the embrace of state and business continues to grow warmer, leaving many others out in the cold.

CONCLUSION

India's quest for industrialization over the last half-century has produced mixed results. On the one hand, starting from very little, India now has a substantial and diversified industrial base, considerably more sophisticated than, say, that found in much of Africa, the Middle East, or even parts of Latin America. On the other hand, when compared with a South Korea or a Brazil, the progress of industrialization in India has not been all that rapid and levels of efficiency have generally been low. Industrial performance has also varied over time, moderately satisfactory in both the beginning and the ending periods and punctuated by a fairly lackluster interregnum during Indira Gandhi's rule. This chapter has sought to analyse the political underpinnings of this economic record. Economic outcomes in India, as elsewhere, are of course a product of numerous non-political factors. Nevertheless, the impact of the state's nature and role on the pattern of late-late industrialization is significant and varies systematically across cases and over time within a case.

The analysis has emphasized the impact of India's fragmented-multiclass state on rates and patterns of industrialization. The Indian state effectively controls the territory it governs, provides moderate political stability, is run at its apex by publicly oriented leaders and bureaucrats, and has always included among its multiple priorities promotion of industry and economic growth. Moreover, the state has intervened heavily in the economy to undertake production directly and to protect its indigenous entrepreneurs from global competition. The state took the lead during the Nehru period and increasingly supported the private sector in the last two decades of the twentieth century.

Conversely, however, the Indian state often lacked the political capacity to translate its enormous economic ambitions into outcomes. Central to this incapacity is its fragmented authority, characterized by both intra-elite and elite–mass schisms and ruling coalitions that are generally multiclass. Leaders in such a state worry perennially about their legitimacy, inclining them to adopt economic policies based on whether they can help to consolidate their political position rather than on whether they will necessarily produce rapid industrialization and growth. The impact of these legitimacy concerns was most obvious during the rule of Indira Gandhi.

In conclusion, the impact of India's fragmented-multiclass state on its middling industrial performance may be usefully compared with some other cases around the world. When juxtaposed against Nigeria, what stands out is the economic importance of a moderately effective state that provides order, protects private property, operates according to the rule of law and procedures, is run by an elite with a modicum of public commitment and competence, and thus focuses some of the state's energies and resources on promoting industry. Absent from such minimal capacities, the state in Nigeria has made a mockery of planned economic development, with dismal results. Indeed, Indian specialists have only to imagine all of India being governed in the manner of Bihar—the Africa within India—to understand the positive contribution of the central Indian state to India's industrialization.

Compared with Brazil or South Korea, however, India's economic

[52]If the yearly man-days lost due to strikes averaged some 37 million in the 1980s, this average in the 1990s was down to nearly 20 million. See *Yearbook of Labour Statistics*, Geneva:

mid-century was not as advanced as that of Korea and Brazil—the share of industry in the Indian economy at independence was closer to 10 per cent whereas it was nearly 20 per cent in both Korea and Brazil following the Second World War. This difference was consequential in two ways. First, to the extent that prior industrialization helps subsequent industrialization, India was disadvantaged. And second, India would have had to industrialize even more rapidly than Korea or Brazil to achieve the levels of prosperity that these countries now enjoy. As it was, however, the pace of India's industrialization was slower. The question, then, is what role the Indian state has played in the process.

Although I have studied the subject extensively, I confess that a firm, parsimonious, and confident answer eludes me. Rather, only fragments of long chains of causation suggest themselves. Taken together, these may constitute a complex answer. A comparison with Brazil is especially instructive. Both India and Brazil pursued import substitution in the 1950s within democratic regimes and yet Brazil's industry grew faster and more efficiently. Clearly, blaming import-substitution policies per se is not an adequate explanation. Instead, the role of different types of states in the two countries stands out as significant. The Brazilian state in this period was considerably less nationalist and mass-based than that of India, allowing Brazilian leaders to focus more on industrialization, to invite foreigners to lead the way, to cooperate closely with business groups, and to repress labour. All of these political differences were economically consequential, producing more rapid and more efficient import-substitution industrialization in Brazil.

After the mid-1960s Brazil and India of course took very different political paths, with striking economic consequences. Indira Gandhi sharply politicized economic policies in India, with a negative impact on industrialization. By contrast, the right-wing military regime in Brazil, much more cohesive-capitalist in its make-up and orientation, emphasized economic growth, repressed labour even further, worked closely with private investors, both domestic and foreign, and borrowed heavily, hoping to boost exports so as to pay off its growing debts. Brazil's strategy ultimately backfired, but not before first achieving 'miracle' growth rates in industry.[53] Industry in Indira Gandhi's India, by contrast, nearly stagnated. This economic situation in India changed somewhat in the 1980s and 1990s, but only when national politics also turned more pro-capitalist, with a greater emphasis on economic growth, closer cooperation with business, and further taming of labour.

[53]It may be worth noting that if Brazil's and India's economic growth are compared over the entire period of, say, 1950–2000, the economic performance of the two countries starts to converge more than diverge.

Finally, the comparison between India and South Korea is dramatic. South Korea's cohesive-capitalist state contrasted fairly sharply with India's fragmented-multiclass state. This was evident in how state authority in the two countries was organized—cohesive versus fragmented—as well as in the state's relations with various social classes—narrow and precapitalist in one, broad and multiclass in the other. The South Korean state under Park Chung Hee thus concentrated power at the apex, defined rapid industrialization as essential for national security, penetrated downward, instituted close relations with business, controlled and mobilized labour, and cooperated closely with Japan without creating debilitating dependencies. While Korean citizens paid a heavy price in terms of repression and lack of freedoms, Korea's cohesive-capitalist state intervened heavily in the economy to promote both import substitution and exports of manufactured goods and, judged at least by growth results, did so rather successfully. India's fragmented-multiclass state, by contrast, pursued several goals simultaneously, cooperated with business only sporadically, faced considerable labour activism, resisted integration into the global economy—either for capital, as the Brazilians did, or for trade, as the Koreans did—and has only lately moved in a more developmental direction, but not without a commensurate rise in communal nationalism as the new legitimacy formula. In broad terms, India's middling industrial performance has also reflected these underlying political patterns.