

INDIANOMICS

Can India Experience Economic Reform Without Political Revolution?

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III Year

Since independence, India has seen a few strokes of economic reforms, the 1991 reforms being the most prominent ones. However, today with a slow real gross domestic product (GDP) growth and a high inflation rate, the country seems to be operating at full capacity with a sense of saturation. There is a general discontentment with the political and economic system among the citizens of India, and an unwillingness to cooperate with the government. With a fickle federal government and the regional parties gaining more power, key economic reforms are stuck in messy politics. This is accompanied by innumerable corruption charges, low economic growth and investment, and high inflation. All these stress an urgent need for another round of economic reforms that must be backed by a political revolution.

The growth rate of the Indian economy has been dwindling, with 4.4% in the first quarter (Q1, April-June) of the current fiscal year 2013-14. Inflation rate has been on a rising trend (6.6%, September 2013), with food inflation between 15% and 25%. The

marginal efforts targeting industrial growth, monsoon-dependent agricultural growth, and the drop in private consumption are only worsening the situation. Although the situation is not as bad as that in 1991, we cannot wait for such a doom to bring about a change.

There is a dire need for another dose of economic reforms in order to revive India's growth potential. The biggest challenge that India faces today is its infrastructure deficit. Reform is much needed in the markets for inputs like power, labour, capital, and land. The reforms of 1991 that liberated the product market left the factor market for these basic inputs out of their purview, and they are still under state influence. According to a report by the consulting firm McKinsey, India is short of \$190 billion in the infrastructure sector and is in urgent need of capital. 2% of road length carries 40% of all road traffic of the country. Due to the fragmented nature of the industry, road transport services in India are poor with high logistical costs. For India to grow at 8-10% a year, electricity supply must double in a decade, which is difficult because, even though the government has sought private investment in power stations, the supply chain is still largely unreformed. Fuel (mainly coal in India) is dug up by the state, which does not have enough funds to raise its production fast enough. The generation and distribution of power by the state at less than the market price has led to major losses in the GDP. With the Indian population growing at phenomenal rates,

there is a need to create around 12 million jobs per year for the next two decades. Many of the people entering the workforce are unskilled and from the poorest regions, placing a demand for better education and transport infrastructure.

Reforms in Foreign Direct Investment (FDI) rules are much needed, especially in the retail sector, which is one of the largest employing industries in the country. There has been slow growth in this sector due to inefficient and outdated technology and poor organisational structure. It is largely controlled by small-scale operations due to which Indian suppliers have not been able to deliver to the consumers. According to Indian Commerce Minister Anand Sharma, 30% of agricultural produce does not reach the market, and 50% of the remaining 70% is lost due to poor transportation and storage technology. This is a gross waste in a developing country with millions below the poverty line. This inefficiency due to lack of organisation is the root of India's problems. Increasing the cap on FDI in the retail sector will allow foreign firms to enter the country and make major investments, setting the country on a path towards further modernisation, and help it to increase consumer spending and address food inflation.

Bureaucracy has been scaring foreign investors away. The heads and chief executives of India's most prestigious firms have expressed their frustration and state that they have lost the will to cooperate with India's corruption-laden government. Indian firms themselves seem to be in favour of investing abroad than at home; in areas that may project the weaknesses of the nation, such as importing more expensive natural resources like coal despite having the fifth-largest reserves in the world; owing to a lack of infrastructure to tap them. Capital expenditure has been

slowing sharply and a further dip may hurt both short-term and long-term growth figures as well as the economy's capacity, which will have an adverse impact on investor confidence and this might turn into a vicious cycle. Like other emerging economies, India needs to build up a structural setup that ensures a long-term growth trajectory in order to ensure investor confidence.

All of India's economic woes can be traced back to the Indian political system. The economic slowdown has been partly attributed to domestic issues like pressures of democratic politics. There is a political crisis with a paralytic central government. At present, the ruling party is holding together a coalition of smaller parties to form a majority in the parliament, called the UPA. In its current form, it is weak and fragmented, and the parliament, due to lack of a clear majority, is losing power to regional parties that threaten to pull support over major reform issues as they are more interested in short-term consequences. The opposition party, BJP, has been more committed to unfolding the weaknesses of the Congress rather than working towards finding solutions. In 2012, Pranab Mukherjee (Finance Minister at that time) stated, "Coalition politics and federal considerations played their roles in holding up economic reforms on several fronts, ranging from diesel and LPG pricing to FDI in retail". Although bills on tax reform, subsidy reduction, and FDI reform exist (with a recent enforcement of the Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act, 2013 after deliberations lasting for 2 years), but a divided parliament is unable to pass the bills. There are long delays in political decisions and deliberation of bills that accrue to important policy decisions with far-

reaching economic outcomes, such as a new sales tax (Goods and Services Tax). In the current system of taxation, it is difficult for businesses and investors to run operations across the states due to the differing tax regulations. There is a desperate need for reform of tax laws in India. If passed, the reform bills will bear fruit in a very short time, fuelling business and inducing confidence.

India's position regarding the fiscal budget is grim. The government has been spending on fuel and fertiliser subsidies programmes, which has been possible in the recent past due to GDP growth averaging around 8%. But now, with dwindling growth rates, there is a need to curtail spending, discontinue these subsidies, and divert the funds to other sectors. The government's efforts in this area have not been fruitful due to opposition from regional parties. Using tactics like 'All-India Bandhs' against the government's efforts to repeal the subsidies, regional parties have become a hindrance for any reform. Even FDI in the retail sector has seen the same fate, with Mamata Banerjee, Chief Minister of West Bengal and an important UPA ally, pulling the plug and ending support.

The Indian democratic process makes enforcement of sustainable policy reforms more difficult due to powerful opposition from interest groups. Examples include farmers against the loss of subsidies, and protected industries fearing foreign competition. Politicians do not prefer to cause unrest among powerful interests, which are the source of funds for all their political activities and personal bank accounts. They are disinclined to foment conflict with public-sector unions over privatisation or tax reforms. Elected politicians are extremely short-sighted, their vision lasting only till the next elections. The quality of Indian politicians

has decreased and many of them are out of sync with modern day realities. Most of them are corrupt, and disinterested in serious reform. The increasing number of politicians with criminal records and the use of bribes to get party tickets and vote banks completely erode India's democracy. Historian Ramachandra Guha wrote recently, "There are allegedly 'democratic' politicians who abuse their oath of office and work only to enrich themselves; as well as self-described 'revolutionaries' who seek to settle arguments by the point of the gun". Only serious electoral reform can ensure a better breed of politicians.

Scams delegitimise state action. Thus, growth-sustaining reforms include cleaning up political funding and combating corruption. Institutional reform to expand and cleanse the judiciary, speed up prosecution and reform political funding are pro-growth steps that need to be taken immediately. A political reform that has often been suggested is to publically mandate intra-party elections at all levels in all recognised parties and maintain a public register of their memberships. It is ironic that the world's largest democracy runs its party system in an almost feudal manner, making any kind of change extremely difficult because a paternalistic approval is needed from the old leaders and new leaders can hardly ever challenge them with a bold vision.

Base politics induces a degree of financial non-viability by providing goods and services that are not paid for, such as power theft and giveaways. If the state government pays for the power it demands, even for giving away to farmers and entrepreneurs, power will turn into a commercially viable sector and people will start investing in it. Appointing ministers for telecom and roads might lead to concentrated efforts in these areas in order to generate visible results,

rather than simply pocketing money from these sectors. But resolving such issues is essentially a question of political will.

Another area where a political revolution must precede economic reforms is governance of states that underperform with respect to their potential. For instance, Bihar has the potential of becoming the largest producer of sugar in the country due its agro-climatic features that are ideal for sugarcane, which can even survive an occasional flood. But sugarcane needs to be crushed right after being harvested and this requires the presence of sugar mills in the vicinity of the field. These sugar mills are largely under the state government, leaving them at the mercy of protection racketeers and corrupt officials with no personal motive to bring up more mills. Though reforms may be initiated by the national government, state governments play a decisive role in implementation and must be made more accountable.

Reforms are more likely to be sustainable the more institutionally embedded they are and the less they depend on any particular individual. They need to be comprehensive enough to not be sabotaged by the unreformed sectors of the economy. Hence, implementation is extremely critical. Because reforms need long time horizons, the politicians in power need to realise the need to take some bold steps for future benefits, moving past the trivialities of gaining power in the next elections.

Economic growth in the country has occurred mainly due to the dynamism of the private sector, in spite of a corrupt government. As stated by Vijay Kelkar, policymaker and chairman of the 13th Finance Commission, India needs a reform stimulus than a fiscal stimulus, and the most pressing economic reforms are squarely in the realm of politics. Any kind of economic

reform now needs to be preceded by a political revolution, in order to provide the institutional structure needed for the reform to be sustainable.

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Excavating India's tourism potential

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Indian economists are trying their best to solve the BOP crisis. While they are looking for methods to attract foreign income, they have overlooked the enormous tourism potential our country holds. France, in the year 2012, had 83 million foreign tourists while USA had 67 million foreign tourists. India had only 6.6 million foreign nationals, out of which a good percentage were NRIs visiting their relatives. India has a history that predates those of European nations. We have artefacts that show great advances in human intelligence and a treasure of natural resources as well. The problem is that we are not able to market as well as develop our resources in a way that attracts tourism.

We just use our natural resources for industrial development. Our lakes and rivers simply serve as drains for industrial waste. We need to rejuvenate our resources, and make them ideal for a paradise-like holiday experience in the lap of nature, coupled with adventure sports, wildlife

safari and other such activities. Infrastructure for the same should not be massive since we don't want to disturb ecology. Rather, we should involve the local populace, who will find a new source of livelihood and thus have a vested interest in safeguarding the resources as well.

India has 30 UNESCO World Heritage Sites, with another 30 in the waitlist. UK has only 28, with tenfold number of tourists visiting them. Why? Because we lack investments in tourism infrastructure — roads and other forms of connectivity, tourism police, financial services, hotels etc. Tourist sites lack basic amenities and are situated in the middle of cities. They are places which stubbornly display all negative attributes of a problematic tour, proving the shallowness of the promise of the Government of India to provide royal treatment. If we want foreign visitors to experience India's cultural heritage, we need to maintain, restore and renovate our historic monuments. To accomplish this, government agencies should work diligently with private players, and more importantly, we should be proud of our architectural heritage and not ruin it ourselves. Indian citizens are also irresponsible and their behaviour is far from the principle of '*atithi devo bhava*'.

Another issue is that globetrotter is undercharged for sightseeing in India. The entry fee for an alien traveller at Ajanta caves is only Rs 250, which is even less than \$5. An international tourist, who has spent about a thousand dollars to visit a country, will certainly be willing to give more than what he/she spends on a chocolate sundae.

In the globalized world, technology and skyscrapers are not the only things that attract tourists; it is the distinct culture and traditions which catch their attention. Millions participate in La Tomatina in Spain