Chapter Four

INDIA'S POLITICAL ECONOMY

In the previous chapters, we have dwelled upon the importance of trade in the world economy and a country's economy as well as the growth of a multilateral trading regime in economic and political order. It is also acknowledged that developing countries join multilateral regimes with expectations to fulfill their developmental goals and had participated with more vigour in the trade negotiations at the WTO. While engaging in such negotiations a developing country like India has to contend with domestic pressures from its civil society.

The Indian state has had to address the growing influence of market forces, both within India's political economy and in the rest of the global economy since the 1980s.

In this chapter, as we examine India's shift from a predominantly planned economy to that of one desirous of liberating its economy and integrating with the global economy, we shall refer to the changing role of the Indian state and the responses of various actors from India's civil society to it. We shall identify the changes in the trade policies and the impact caused by them on India's political economy. We also deal with the larger question of resistance by civil society to the imperatives for integration with the global economy through the World Trade Organization.

The chapter gives a brief account of India's policy choices with respect to India's domestic and foreign economic policies after her independence, by identifying the causes for such choices and the effects that accrue from them. We observe that while the objectives of development, economic growth and eradication of poverty remain largely the same over the years, the means of achieving them have changed over time. The actions and the activities of the Indian state are now being shaped by both
liberalisation and globalization. This has drastically altered policy orientations in the issue-area of trade and likewise on India's overall policy stance towards international organizations like the WTO.

The first section of the chapter deals with the nature and behaviour of the state in India during the early post-independence years when it opted for a predominantly planned economy. The second section deals with the consequences of "development planning." The third section deals with the 1991 crisis, the economic reforms that were introduced in the wake of it and their impact on India's political economy. The last section deals with the responses of the stakeholders to the economic reforms and builds up a case that though reforms have not been totally successfully in meeting our goals yet they are essential in a globalising trade scenario.

4.1 THE STATE IN INDIA

Characterizing the Indian state always remains a conceptually complex proposition. Some formulations about it are introduced here to bring out some crucial characteristics of the Indian state.

According to Guha, "In the traditional theory of commercial policy, the State is a Godlike benefactor aiming solely at social optimality. Sometimes the optimization is constrained by an autonomous set of non-economic objectives. But in general the state continues to be depicted as a lonely island of altruism in a sea of self-seeking maximizers". (Guha, 1990, p. 38)

He further states that, "over the four decades of independence, the Indian State has grown in size but not in competence. Both its size and its incompetence were dictated by its legacy from the past and the milieu in which it evolved". (Guha, 1990, p. 48)

However, at the time of independence, India also had the dynamic commitment of its leadership to first build a democratic, political structure and then to undertake economic development within it. This leads us towards Bardhan's class-analytical argument about the Indian state.
Bardhan (1984) has correctly argued that the political leadership that inherited power after independence enjoyed special legitimacy about the desirability of using state intervention in promoting non-economic development. The relative autonomy of the state was also enhanced by the fact that the dominant socioeconomic groups in India were (and are) extremely heterogeneous and highly divided which potentially gives policy makers more room to maneuver. This enabled the state to accumulate powers of direct ownership and control in the economy to an extent unparalleled in Indian history.¹

(i) Nature of State

The nature of Indian state in the post independence years was deeply influenced by the colonial legacy and the ideology of the national movement. These gave the Indian state its primary nature of acting as a protective wall against international capital and of embracing the instrument of planning as the key for achieving the objective of economic development. The state in, other words was an instrument for the 'primary accumulation of capital'. The state also derived its interventionist character from the conscious efforts on the part of the political leadership to promote self-reliance and balanced growth.

The dirigiste regime, which India opted for at the time of independence, was largely a result of the colonial legacy that left an economically impoverished India desirous of a degree of isolationism. Bipin Chandra has elaborated on the basic features of the colonial structure in India², which are a major explanation of economic stagnation in colonial India. As the Colonial state was forced to adopt policies inimical to the process of development, the economic vision remained confined to increasing India's capacity to export primary products and to purchase British manufactured goods. Thus, international trade came to be seen as an instrument of exploitation.

This strong economic critique of colonialism became a powerful factor in the economic strategies adopted by the Indian state. There was a clear
belief in the mind of prominent nationalists that India's underdevelopment was a result of the subordination of Indian economy to the needs of British trade, industry and capital. In this regard, Justice Ranade's theory of economic drain contained the belief that free trade represented an unequal economic relationship and that what was needed was self-reliant economic development. What was significant was that self-reliance was defined in terms of avoidance of a subordinate position in the world economy. Pandit Nehru's fears of economic imperialism were vivid and despite his general antistatism Gandhiji too favoured state ownership of all large scale industries. Thus the Indian state, at the time of independence came to acquire an active economic role. As Byres has commented:

"The economic critique of colonialism then was the foundation from which a positive content was supplied for the independent national State; the new State represented the only legitimate form of exercise in power because it was a necessary condition for the development of the nation".

A similar view about the impact of the colonial rule on India's policy planning in the trade arena, was taken by Arun Goyal during interaction with the researcher on 30th June 2004.

Besides, the nature of state in India at the time of independence also reflected the international environment. It was a typical Third World state as defined by Clapham "a combination of fragility and power" a prize to be fought for. Though this state is a powerful agency for extraction and control, it is prevented from becoming a totalitarian structure because it is readily permeated by the society in which it exists. However, there is a lack of organic unity or shared values between state and society, which leads to resistance by society to changes brought about by the state. The neopatrimonial nature of the state ensures that any attempt by the state to promote radical economic change is likely to exacerbate domestic conflict. The problem of controlling the economy "exemplifies the nature of the Third World state through its intricate mingling of domestic and external, as well as economic and political, elements"
Terence J. Byres, speaking from a Marxist political economy perspective, characterizes the Indian state as "the source of planning, its fons et origio in suggesting planning, validating it and then embracing it in India, with the avowed aim of securing 'development'. He calls it the "architect" the agent and the "ultimate arbiter" of planning", leading to "an almost Hegelian assumption that the State has an independent identity, a will and a capacity to choose of its own". It is also important to remember that this nature of state reflected a fairly widespread intellectual consensus of the time. The prevailing opinion was naturally for a rapid and forced march toward industrialization. Jalan's (1993) observation of how the interventionist development strategy had the sanction of various economists is instructive in this regard. 

(ii) The Behaviour of State

The Indian state typified all the above features, leading Gupta to comment:

"At a discursive level, the state in independent India is like theatre. It has its tragedies, tragic comedies, comedies and farces. This is more so if one looks at the behaviour of elements of political class in relation to different regimes." 

These factors determined behaviour of the Indian state in the post-independence years. The ideology of development planning led it to actively intervene in the trade and industry sectors of its political economy. The fallacy to which the Indian policy makers fell prey was that governments will succeed in securing the objectives of economic welfare whereas free market will fail. They "fell into the trap of a binary logic, whereby if the market was considered to be inadequate then the alternative must be a system of discretionary commands on the part of the State". (Guha 1990, p. 36) Thus, the state consciously followed a path of self reliant economic development based mainly on planning and import substitution.

The Nationalist economic perspective that was crystallized in the "A Plan of Economic Development for India" (popularly known as the Bombaby
Plan) showed clear emphasis on industrialization. It reflected the conviction that to make industrialization consistent with a viable balance of payments position minimized imports were essential. Added to this, was the firm belief that India's main exports (at that time) of primary products would only lead to deterioration in the terms of trade. This economic logic coupled with the colonial hangover led a nascent Third World state to impose upon civil society a model of development planning that was based on inward orientation and import substitution. The five years plans, based on the Harrod-Damor model and the Mahalanobis Model, exhibited these strategies. The policies found strong support from the US that contributed $4 billion in aid through 1962.

While the consequences of the above strategy will be discussed in the later section, it is pertinent to note the response of various stakeholders to a system where the state is assigned a predominant role. As Guha comments, in India's case the "different producers groups, powerful trade unions and the political and the bureaucratic elite's agreed upon set of behavioural rules to protect their respective interests". Bardhan (1984) has dwelt at length on the major economic groups which organized themselves effectively for the process of rent seeking through political pressure. He speaks of the rich farmers, the domestic capitalists and the educated urban middle class and says that these heterogeneous interest groups fought and bargained for their share in the spoils of the system and compromise in the form of log-rolling.

Thus, while an equilibrium in the political economy might have been achieved but it was certainly not surprising that the resultant economy was neither dynamic nor did it meet the development objectives. Moreover, as we shall see in Chapter Five, these interest- groups became vociferous in their protests when the state opted for a liberal trade regime, ostensibly in defense of national interest but in reality, in defense of their own sectoral interest, causing India to behave in a self mitigating, reactive approach at the WTO.
4.2 THE FALL OUT: 'PARADISE LOST'

"The men are able, the organization is adequate the procedures are intelligently devised. Why, then, have the plans, since 1956, so persistently run into crises."

A.H. Hanson

Though the aim of this study is not to analyze the success or failure of India's Development Planning strategy, on which there is abundant literature, it cannot be denied that certain crucial factors which became responsible for India's shift to a more open economy, were direct consequence of this strategy. This section aims to throw light through relevant data, at two factors—one the failure to meet objectives of growth and poverty alleviation; second increasing isolation from world trade.

(i) Development of Underdevelopment

As per the Human Development Report (HDR) of UNDP, 2003, India's per capita income was $462 in 2001, making it rank 162nd in a list of 206 countries. Accordingly to HDR, India has a Human Development Index value of 0.590 making it rank 127th out of 175 countries. As per data collected by National Sample Survey (NSS), 26% of India's population is below poverty line. India also fares poorly in other indicators of development such as life expectancy, literacy rate and infant mortality. The unemployment level remains distressing. There is need for generation of additional employment opportunities to the tune of 8 to 10 million per year on an average between 1992 and 2002. While saving and investment rates increased from 10% in 1950-51 to over 20% in 1980-81, these were not translated into higher growth rates as losses on the productivity front offset the gains of resource mobilization.

The table below gives an international perspective on India's growth performance and its clearly seen that India's growth performance was close to the bottom of the group during 1965-80 and improved to the middle of the range in 1980-90.
India's Economic Growth: An International Comparison

Growth Rates of GDP

<table>
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</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total</td>
<td>Agriculture</td>
<td>Industry</td>
<td>Total</td>
<td>Agriculture</td>
<td>Industry</td>
</tr>
<tr>
<td>Bangladesh</td>
<td>1.7</td>
<td>0.6</td>
<td>1.5</td>
<td>4.3</td>
<td>2.6</td>
<td>4.9</td>
</tr>
<tr>
<td>India</td>
<td>3.6</td>
<td>2.5</td>
<td>4.2</td>
<td>5.3</td>
<td>3.1</td>
<td>6.1</td>
</tr>
<tr>
<td>China</td>
<td>6.8</td>
<td>2.8</td>
<td>10.0</td>
<td>9.5</td>
<td>6.1</td>
<td>12.5</td>
</tr>
<tr>
<td>Pakistan</td>
<td>5.2</td>
<td>3.3</td>
<td>6.4</td>
<td>6.3</td>
<td>4.3</td>
<td>7.3</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>4.0</td>
<td>2.7</td>
<td>4.7</td>
<td>4.0</td>
<td>2.3</td>
<td>4.6</td>
</tr>
<tr>
<td>Indonesia</td>
<td>7.0</td>
<td>4.3</td>
<td>11.9</td>
<td>5.5</td>
<td>3.2</td>
<td>9.0</td>
</tr>
<tr>
<td>Thailand</td>
<td>7.3</td>
<td>4.6</td>
<td>9.5</td>
<td>7.6</td>
<td>4.1</td>
<td>9.0</td>
</tr>
<tr>
<td>Turkey</td>
<td>6.2</td>
<td>3.2</td>
<td>7.2</td>
<td>5.1</td>
<td>3.0</td>
<td>6.2</td>
</tr>
<tr>
<td>Chile</td>
<td>1.9</td>
<td>1.6</td>
<td>0.8</td>
<td>3.2</td>
<td>4.2</td>
<td>3.4</td>
</tr>
<tr>
<td>Mexico</td>
<td>6.5</td>
<td>3.2</td>
<td>7.6</td>
<td>1.0</td>
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<td>1.0</td>
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<tr>
<td>Brazil</td>
<td>9.0</td>
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<td>10.1</td>
<td>2.7</td>
<td>2.8</td>
<td>2.1</td>
</tr>
<tr>
<td>Korea</td>
<td>9.9</td>
<td>3.0</td>
<td>16.4</td>
<td>9.7</td>
<td>2.8</td>
<td>12.2</td>
</tr>
</tbody>
</table>


Since 1947, India's GDP growth can be divided into 3 stages. The first stage lasted till the mid-1970s where the Hindu rate of growth of 3.5% prevailed. The second stage from late 1970s to 1980s saw the average GDP growth rate increase to 5 percent and the third stage from 1992-1997 where the average growth was 6.8%.

It is tempting to correlate slow growth with development planning and the increase in growth with the gradual opening of the economy and economic reforms, but as stated earlier, that is not the subject of this study and these statistics are only used to indicate the actual state of affairs in the India polity after 50 years of conscious policy-making.

India's inward orientation thus had significant economic costs in lower overall growth and stagnating living standards vis-à-vis other Asian nations like Japan and China.

As Guha (1990, p.46) points out, the developmental role of the state became "inextricably associated with the creation of opportunities for rent seeking activity."
It is worthwhile to present two quotations before elaborating upon how India became isolated from the global economy.

"I do not want my house to be walled on all sides and my windows stuffed I want the cultures of all the lands to be blown about my house as freely as possible. But I refuse to be blown off my feet by any "

M.K.Gandhi, June 1, 1921

"Between 1965 and 1991, instead of changing course as many countries did, we tightened our system, making it more rigid and bureaucratic. Even China changed course in 1978, letting in competition and set out on a historic path of growth, India continued to eliminate competition because it regarded it as wasteful."

Gurcharan Das, 2002, p 174

While Mahatma Gandhi's famous lines show India's grandiose tradition of accommodation, the second quotation shows that the same spirit could not pervade over economic policy makers. Even if Nehru's vision of "control of commanding heights of economy" by the state was justified as being the need of the hour, the fact that India's closed economy did more harm than good during the 1970's and 1980's can not be denied. The view echoed by Rakesh Mohan that "we have paid dearly for the follies of the dark decade of 1970s" captures the broad picture. Not only were the main objectives of poverty alleviation and growth not achieved, the shackles of bureaucracy created barriers in the path of entrepreneurs and drove investors away. In this regard, Gurcharan Das tells an interesting episode that how Aditya Birla in his global factory chain for manufacturing carpets set up factories in Thailand, Indonesia, Belgium but not in India because of the closed economy.

The decision to control market forces in public interest degenerated into a tool for political and other patronage dispensation with grave
consequences. Most significantly, "India became increasingly insulated from the world economy under this development strategy. The volume of world exports expanded at an average rate of 7.9 percent annually from 1950 to 1973 but India's exports grew by only 2.7% annually".22

Its trade policy had the direct effect of limiting its participation in world trade- between 1951 and 1993, India's share of world trade plunged from 2.4 to 0.5%.23

Such isolation meant lack of competition and it led to a point when Indian Industry became sluggish and it had no incentive to upgrade technology, to reduce costs or improve efficiency. Debroy lists eight specific policies of government that curbed competition and provided a huge cosy, protected domestic market for profits.24 Besides, as Debroy points out, the licensing and protection was arbitrary and without economic rationale. This atmosphere suited certain interests groups like domestic producers, bureaucrats and elite and it was these groups, as we shall later, that resisted economic reforms

Besides the extensive and rigid control framework was what Bhagwati (1994) has called "India's persistent failure to seize the gains from trade". Though export pessimism was a shared belief in the 1950s, even accepted by economists like Prebisch and Nurkse, it soon became a discarded theory. "But while the most successful developing countries adopted their polices in light of the emerging reality of rapidly expanding trade prospects, India policies continued to be based on the unrealistic and false premise of export pessimism."25 while this cut off India from the rest of the world, failed to address its problems of poverty and growth, it also created a "rentier" as against an entrepreneurial economy which as we shall see later put vested interests over national interest.
4.3 1991: ‘THE SECOND COMING’

"A moment comes, rarely in history, when we step out from the old to the new, when an age ends, and when the soul of a nation, long suppressed finds utterance".

Jawaharlal Nehru, Independence Day Speech

It is ironic that these words by Pandit Nehru, also hold true for the changeover India, in 1991 towards a Liberalisation, Privatization and Globalization (LPG) economic framework that gained currency from then onwards. Against a backdrop of ill-development and non achievement of objectives of growth, the state had to accept that India could no longer be "The Solitary Reaper". As Byres has commented, if the "retreat" to economic liberalisation suggests the virtual abandonment of economic planning in India, then on this view, it is the state itself that has, quite independently and after due consideration taken the decision to withdraw. There was a growing consensus among the leadership that "India did not plan too much, in certain important ways it just planned inadequately." Moreover, a section of civil society had already been pointing to the fact that state controls on economic activity and inward orientation had cost India dearly in slow growth (Bhagwati, Desai, 1970), (Bhagwati, Srinivasan, 1975). Within the government too, many important reports put together by the bureaucrats had since 1970s been recommending liberalisation of economy.

Among external factors, the collapse of the Soviet Union undermined India's faith in central planning and also led to new political paradigms on India's security needs. China's phenomenal growth after 1978, when it opened its planned economy, also opened the eyes of Indian policy makers about the need for radical reforms in the economic policy regime. The desire to be the 'Asian Tiger' no doubt propelled the economic reforms package.

However, it must be recognized that it was not as if the reforms were suddenly thrust upon the Indian society. As a matter of fact 'reforms are evolutionary and not revolutionary'. In the 1970s and the 1980s there had
been attempts, albeit abortive, to open up the economy which had to be given up due to political pressures. Kohli provides a good analysis of liberalisation in Indira Gandhi's and Rajiv Gandhi's tenure. He states that the trend towards liberalisation of the economy was initiated by Indira Gandhi. Coupled with a change in attitude towards international institutions such as the IMF, many important economic decisions were taken by Indira Gandhi during 1981-82 pertaining to decontrol in certain industries in the Indian economy. By 1984, "liberalisation of industrial licensing, easing of access to imports coupled with lowering of import duties and promotion of foreign technical collaboration became the key aspects of the government's industrial policies".

However, these changes did not evoke sharp political and social reactions because they were part of an overall political strategy, the scale of change was minimalist and there was a deliberate attempts to maintain continuity from past.

It was during Rajiv Gandhiji's tenure that there was a genuine attempt to make a decisive shift from the state-controlled, import-substitution model to a liberal model of development. The "take-off" seemed imminent. However, the political situation and events ensured that though commitment to economic liberalisation was vocal, actual policy changes were few. Significant among these was the 'New Fiscal Policy' 1985 which replaced import quotas with tariffs and laid out long term patterns for taxation. The broader aim was to relax the degree of state control over the private economy. The resultant growth (5.7% in the 1980s from 3.75 in the earlier years) of GDP though could not be sustained, but made liberalisation politically acceptable.

It must be noted here that what also grew was the fiscal deficit and the current account deficit. The debt-service payments and inflation scene also worsened. "Political and external factors exacerbated the tenuous fiscal situation. Frequent changes in the Central Government toward the end of the 1980s created political uncertainly and eroded confidence in the government's ability to manage the economy and maintain stable economic
policies with the collapse of the centrally planned economic of Eastern Europe and the Soviet Union, larger trade with these economics broke down. The Gulf war of 1990 hit India hard. (Srinivasan, Tendulkar 2004 p 26)

Severe external payments crisis in 1991 forced the government to undertake major macroeconomic policy reforms, ignoring the resistance from rent-seekers of the control regime. As Bhagwati (1994 p.3) has commented, "reform by storm has supplanted the 'reform by stealth' of Mrs. Gandhi's time an 'Reform by reluctance under Rajiv Gandhi". "The reforms indeed heralded a major change in the country's development strategy. India gradually abandoned the use of quantitative controls in economic management in favour of market based instrument. There was a decisive move away from inward orientation and towards greater integration with the global economy. Finally the reforms signaled a shift away from an overstretched, overstretched, rigid and inefficient public sector and toward greater reliance on the private sector." (Srinivasan, Tendulkar, 2004, p.29) Gurucharan Das gives a detailed account of how the troika of Man Mohan Singh, P. Chidambaran and Montek Singh Ahluwalia authorized the reforms under Narasimha Rao29 leading to the July,1991 declaration in the Parliament 30

The reforms were in three major areas of domestic industrial investment policy, foreign investment regulations and foreign trade.

The literature on economic reforms of India is abundant.31 As far as this study is concerned, we have focussed primarily on the effect of reforms on foreign trade to indicate how India's integration with the global economy deepened and this raises pertinent questions to our key argument. We also examine the changes in tariffs and tax structure, as the impact of reforms in these two areas was tremendous and evoked sharp responses from the stakeholders.
(i) Change in Direction of Trade

Reforming foreign trade was a significant step in India's external sector reform. The trade deficit in 1990-91 amounted to 3.2% of GDP and hence policy reforms aimed at erasing the export pessimism were essential. The redesigning of foreign trade policy covered a broad area. It aimed at:

- rationalization of exchange rate policy,
- liberalisation of imports,
- incentives to exporters,
- simplification of procedures and transparency in taxation.

Sharan and Mukherji\(^3^2\) have analysed the foreign trade changes from 1991 onwards. While the growth rate of exports fluctuated there was no doubt that the direction of India's foreign trade had changed. Srinivasan, Tendulkar (2004, p.47) also conclude that "the aggregate value of exports (in US Dollar terms) grew at an average rate of 19.7%, annually from 1993 to 1995 before falling dramatically to average 1.6% a year during the period 1996-99." They also state that "post liberalisation growth of exports and imports encouraged competition and innovation in addition to shifting domestic resources toward higher productivity cases." They have also analyzed the direction of India's trade, pre-reform and post-reform triennia (Table attached as per Annexure 6), compared India's share of world incremental extended manufacturing exports with other countries and concluded that though trade liberalisation improved India's export performance, it still lagged behind other rapidly growing Asian nations, primarily because early liberalisation helped these nations to diversify their trade and achieved a higher growth rate.

An analysis of post-independent India's share in world trade, given in the table in the next page, shows an alarming decline.\(^3^3\)
India's Share in World Trade: 1950-98

<table>
<thead>
<tr>
<th>Select Years</th>
<th>India's share in world exports (%)</th>
<th>India's share in world imports (%)</th>
<th>India's share in world trade (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950</td>
<td>1.85</td>
<td>1.71</td>
<td>1.78</td>
</tr>
<tr>
<td>1960</td>
<td>1.03</td>
<td>1.69</td>
<td>1.36</td>
</tr>
<tr>
<td>1970</td>
<td>0.64</td>
<td>0.65</td>
<td>0.65</td>
</tr>
<tr>
<td>1980</td>
<td>0.42</td>
<td>0.72</td>
<td>0.57</td>
</tr>
<tr>
<td>1990</td>
<td>0.52</td>
<td>0.66</td>
<td>0.59</td>
</tr>
<tr>
<td>1991</td>
<td>0.50</td>
<td>0.56</td>
<td>0.53</td>
</tr>
<tr>
<td>1992</td>
<td>0.53</td>
<td>0.61</td>
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</tr>
<tr>
<td>1994</td>
<td>0.58</td>
<td>0.60</td>
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<tr>
<td>1998</td>
<td>0.61</td>
<td>0.63</td>
<td>0.62</td>
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</tbody>
</table>


This only reinforces our earlier argument that the inward orientation policies adopted by India led to its increasing isolation from the global economy. It, therefore, became imperative that India switched its path and opt for integration with the world economic order in order to realise its multifarious objectives of growth and development.

(ii) Changes in Tariff and Tax Structure

Krasner has commented that "tax collection is generally a good indicator of the ability of a state to extract resources from its own society. He states that there is a strong relationship between economic development and the nature of tax structure. His argument that developing countries are far more dependent on trade taxes than are industrialized nations holds goods for India as the state has relied heavily on tariffs and high duty rates in customs for its monies. About 99% of customs revenue, which comprises 24.2% of the centre's total tax collection (2000-2001), comes from import duties. The customs tariff, over the years, had become complicated in terms of multiple rates, innumerable exemptions and excessive controls.
In 1990-91, the unweighted average normal tariff was 125%, with a peak rate of 355%. In 1993-94, the corresponding figures were 71% and 85%. In the budget of 1994, the peak rate was reduced to 65%, which came down to 40% in the 1997-98 budget and currently stands at 15% (Union Budget, various years).

The rationale behind reduction of tariffs was to make the domestic industry competitive. The objective to meet East Asian levels was also present. As the then Finance Minister stated, "I have already promised that our customs tariff would be brought down to East Asian levels. I will like to move progressively within three years to reduce the number of rates to the minimum with a peak rate of 20%".

(Budget speech of the Finance Minister, 2001, Part-B)

The move towards moderate rates of taxation and simpler procedures with a view to improve compliance and reduce litigation, was an essential component of India's tax reforms, much before it became an WTO imperative. They were the logical outcome of an inherent recognition that India needed to streamline its trade policy system to align it with the rest of the world. The Report of the Tax Reforms Committee35 (The Chelliah Committee) in 1991, stressed this "tariff policy should have some relation to the stage of development and in a developing country, while the market should have a large role to play; the structure of import duties should be used to achieve the longer term goals of industrialisation and to further the strategy of dealing with the world market."

(Final report of the TRC, 1993, Para 2.9)

Mehta (1999), in his authoritative study on 'Tariffs and Non-tariff Barriers of Indian Economy'36 has also analysed the changes in India's trade regime. In studying the change in the protection with respect to the tariff structure, he shows that the average MFN tariff rates have significantly and consistently declined from 1993-94 onwards from the rate of 86.4% to 25.4% in 1998-99. However, he also concludes that the average tariff rate of
India's import is still significantly higher than those of countries like China, Indonesia and Malaysia:

**India and other select developing economies: average collection rates.**

<table>
<thead>
<tr>
<th>Country</th>
<th>Year</th>
<th>Average tariff Rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>India</td>
<td>1997-98</td>
<td>26.29</td>
</tr>
<tr>
<td>Malaysia</td>
<td>1996</td>
<td>3.10</td>
</tr>
<tr>
<td>Mexico</td>
<td>1995</td>
<td>3.75</td>
</tr>
<tr>
<td>China</td>
<td>1996</td>
<td>6.00</td>
</tr>
<tr>
<td>Philippines</td>
<td>1996</td>
<td>11.54</td>
</tr>
<tr>
<td>Thailand</td>
<td>1996</td>
<td>6.9</td>
</tr>
</tbody>
</table>

(Value of Import duty collected/Value of Imports of goods


The high tariffs during 1994-95 were much higher than the "bound rates" of tariffs during the Uruguay Round, compelling India, as we shall see, to make further reductions and hence by 1998-99, India's' applied tariff rates were lower than the committed bound rates in the Uruguay Round. The implication is that despite a domestic commitment to liberalisation, it took international obligation to achieve policy transformation. This is a major finding for our conclusion.

**4.4 RESPONSE OF STAKEHOLDERS**

We have seen the Indian state imposing its will on society by opting for a predominantly planned economy. When the Indian state chose to integrate with the global economy the stakes for civil society were higher than ever. Hence, it is essential to study their response to this change. Important stakeholders in the India socio-political milieu include the political parties, the bureaucracy, the Industry and the entrepreneurs. In addition, the Marxist response to liberalisation cannot be ignored. These responses are important because they influence the negotiating strategy in a multilateral
trading regime. When we examine the actual negotiating stances of India at the WTO in the next chapter, we need to remember that it has been influenced and shaped by the response of domestic forces. Hence a study of these factors is essential before we embark on India's engagement with the WTO.

In this regard, Jos Mooij's article, "Economic Reform and Political Interpretations. A review of the literature on the Politics of the Reforms Process in India" provides the various interpretations regarding the political factors that have shaped the reforms. He identifies two main approaches viz. state centered and the society centered. The state-centered approach analyses the processes within the India's' bureaucracy and political arena that made the reforms possible. This happened primarily, because the political elites were confident that the reforms will not fundamentally alter their privileged position in India's political economy.

Among the society-centered explanations, the most notable one is that of Bardhan (1984) wherein he locates the economic reforms process within the wider political economy of India. According to him important realignments in the composition of the dominant coalition made the reforms possible. The first pertains to the changing role of state. "There is a slow, and at times grudging acceptance within the bureaucracy that the Indian state has overextended itself in the economy, far beyond the limits of its administrative capacity." (1984, p.131) The second is the shift of political power from the traditional elites to the lower castes as a result of reservation policies. Consequently, the traditionally privileged upper castes began to feel marginalized in their access to state and hence showed no hesitation in supporting the pro-market policies as a means to acquire a new role as agenda setters.

He also points out that there was less division in the business community (as represented by FICCI and ASSOCHAM) on the issue of opening up the economy. While the few traditional big business houses that had thus far captured the Indian Industry was comfortable in the inward orientation of the economy, the growth of dynamic medium-sized industrial
companies ensured resentment against import restrictions. This became a factor that the government could not ignore.

Kohli\textsuperscript{37} also elaborates on the divergence of interests within the business community. He says that the nature of the division of power between state and business is clearly evident in the policy process.

"The business community in India has tended to react to rather than to lead economic policy. Its power is closer to being one of veto than of agenda setting". However, the response of the business groups to the government's new economic policies were generally favourable; the only concern was towards the extent the economy should be opened up.

He also speaks of the support given by the urban middle class as they correlated the liberalisation of Indian economy with tangible economic rewards. Liberalisation implied for the first time, "an economy that was not beset by shortage of consumer goods." Also the phenomenon of the middle income groups buying stocks and becoming a significant contribution to industrial investment created a structural link between middle income groups and business groups. As their stake in the economic health of industry increased, so did their concern to promote and support better policies within India's political economy. Kohli goes on to elaborate those actors and groups that did not support the economic initiatives.

Among political parties, a surprising source of opposition to the new policies had been the Congress rank and file. Discontent emerged from the fact that liberalisation of the economy did not go down well with the party's ground-level workers who had to constantly deal with localized problems of poverty and hunger. Old Congressmen took refuge in the ideological stance that equated liberalisation with abandonment of sovereignty. It was only the Balance of Payments crisis in 1991 that silenced this opposition within the party.

More notable was the dissent by the BJP. The BJP maintained That India's move towards liberalisation was wrong because it meant renewed
exploitation of a developing nation by forces of neo-imperialism. As a result of economic reforms, the nation was advancing into a state of *enclave economies* where the Multinational Corporations flourished and domestic industry suffered. Such neo-imperialist argument was also based on the hypocrisy of the West, which preached free trade but in practice resorted to quotas and tariffs to further their national interests, thereby implying a decline in the terms of trade for India. While this argument cannot be ignored, it appears without any justification. Neo-imperialism, in principle, imposes limits on domestic sovereignty and leads to underdevelopment through increased dependency on the Western states. There is no evidence to prove that the Indian reforms resulted in either of the two situations.

The BJP also based their opposition around the Swadeshi plank. They built their anti liberalisation arguments on the principle that "an open Indian economy will not only increase poverty and inequality but that it will lead to the destruction of those benefit that have derived from a planned economy, especially its much vaunted independence and self-reliance". They also created the wider xenophobic strand of thinking that "liberalisation equates with westernization and western culture will destroy, self evident 'traditional Indian values'." The 'Swadeshi' colour to opposing reforms grew, as we shall see in Chapter Five on India's accession to the WTO.

The 'left' opposition claimed to be more 'broad based' and politically feasible. They argued that liberalisation would not lead to growth, but would undermine long cherished national goals of self-reliance and socialism. The way to boost growth was through agriculture led economic development and improved public sector performance.

Another group that remained negative about the reforms was the peasants and the rural group (Kohli, 1991, p 335) Though it is difficult to quantify their opposition towards reforms, it is clear that led by political interest groups, they perceived reforms as pro rich and anti poor. Their negative reaction may not have been coherent but it was real and it created a direct conflict between the rationale for liberalisation and the need for
political support. This became the quintessence of the 'Soft State' that India became leading to a 'crisis of governability'.

"Over the past two decades, a legitimate and moderately stable State that was confident of its ability to lay out India's agenda for socioeconomic change has evolved into a reactive State. This State is omnipresent, but feeble; it is highly centralized and interventionist and yet seems powerless. It has the responsibility to foster the life chances of its many diverse social groups, but rather than initiating action, it primarily reacts.

Moreover, the State now appears capable neither of dealing with the concerns of diverse interest groups nor of directing planned development".  
(Kohli, 1991, p. 8)

This indictment of state has emerged primarily because a lack of consensus building over the issue of liberalisation ran throughout the change in the economic path. This, in turn, led to more ill-informed opposition as we shall see next at the time of India's accession to the WTO. Moreover, the reforms reshaped the political context. As Mooij comments, on one hand, they went "together with a rise in Hindu fundamentalism and enhanced social and regional polarization and on the other, they resulted in a cause of concern for the domestic market and industry".

It can not also be denied that the reforms vastly increased rural urban income inequalities. Utsa Patnaik gives an elaborate account of how a developing country has been transformed into a 'Republic of Hunger' and "how gains of four decades have been wiped out in a single decade of economic reform." She bases her argument on the sharp decline of per capita food grains absorption which came down from 177 kgs. to 155 kgs. during the 90s, as a result of "an unprecedented decline in purchasing power in rural areas following directly from a number of deflationary polices at the macroeconomic level combined with international price declines, for the large volumes of export crops produced in India following trade liberalisation". The record increase in food grains exports, which as we have noted earlier, brought cheer to the economy, is called an "utter scandal and
disgrace" by her because it happened at a time when millions of the rural poor were going hungry and the government preferred to feed foreigners rather than undertake widespread food for work programmes. While this Marxist criticism of the neo-liberal polices behind the reforms may be narrow, it serves as the perfect illustration of the dichotomy in the pluralist society of India which cannot be ignored by governments. "We cannot integrate at the cost of our own disintegration" - it is the lesson of history and it is being brought into sharp focus by civil society's concerns. (this will be further elaborated in Chapter Six when delineating the TRIPS agreement.) This clearly indicates that liberalisation in India involves trade offs between growth oriented and equity-oriented objectives of India's economic policies. As Jagdish Bhagawati has commented, growth can by pass and even hurt certain groups but the answer to this problem lies not in opposing growth but to use and appropriate policy of diversification in tandem with the growth policy.

It is perhaps, a growing realization of the above fact that has made a Marxist like Lord Meghnad agree that it is in India's interests to become proactive in its liberalisation policies. Says he, "India must liberalize - not because it has no choice - but because it is the best choice. India must liberalize because that way alone can it become a rich and prosperous nation, that way alone is there any hope of conquering poverty." 41

4.5 ANALYSIS

This chapter has thrown light in certain key areas of India's political economy. We have attempted to analyse the nature of Indian state. We have also addressed the question of why did it choose to follow the path of inward orientation and import substitution. We reach the conclusion that the post-independence Development Planning was a legacy of colonial past and reflected the ideology of the then political leadership.

While it was appropriate at that time, India lost out by not changing to an open, liberal economy in time. It also became evident that the stated
goals of growth and development were not achieved through the predominantly planned economy. India also became increasingly isolated from the global economy and became rather like an island operating in the world trading system. This had adverse implications on India's share of world trade. It also created a protected environment for the domestic industry.

The need for economic reforms had been growing. The 1991 crisis made them an imperative. Trade liberalisation was introduced in a comprehensive manner. The reforms evoked sharp reactions from various stakeholders. This response is significant because it later on would shape our negotiating strategy at the WTO. Acceptance of reforms was made difficult because they were perceived as being against the national interest. Neo-imperial and Marxist criticism impede the state's choices, making it a "Soft State". This consequently affected negotiating strategies. The choice that a nation like India faces springs from the dilemma of trade-offs between growth and equity-led objectives and the perceived loss of autonomy from the stakeholders.

However, we also see that international obligations can become a means to overcome domestic opposition and hence aid the state in achieving its goals. This refers to our earlier finding in Chapter Two that it is beneficial to be a part of the global trading system and then optimize the gains accruing through it rather than be an isolated unit. There are limits on such integration and these have to be identified and resolved at the domestic level.

This leads us to conclude that the crisscross of domestic pressure-play limits the level of integration the state wants to opt for. No state can integrate with the global trading order at the cost of political stability. This is the unit-level problem that we referred to in Chapter One and shall elaborate in the next Chapter.
CHAPTER NOTES

1. See Pranab Bardhan's article *A Political economy Perspective on Development in The Indian Economy Problems and Prospects*, Bimal Jalan (Ed), 1993, p. 321


3. Ibid above p 18

4. Nehru had asserted in the National Planning Committee report (1949) p. 47 that self reliance "does not exclude international trade, which should be encouraged but with a view to avoid economic imperialism" Also see Srinivasan, Tendulkar *Reintegrating India with the World Economy*, 2004, p. 6, for his views.

5. Terence J. Byres *The State, Development Planning and Liberalisation in India*, 1998, p 86.


7. Byres, Supra note 5, Chapter -1, p. 46, 56.

8. Jalan Supra note 1, see introduction p. xii


10. See Isher J Ahluwalia's article 'Contribution of Planning to Indian Industrialization in Byres ,supra Chapter -7


14. See S Chakravarty *Development Planning in India* and also A. Guha *Economic Liberalisation, Industrial Structure and Growth in India*.

15. phrase used by Andre Gunder Frank in Francine R. Frankel's *India's Political Economy 1947-1977, the Gradual Revolution*, 1978, p.163


18 See Debroy supra note 16, p. 34

19 See Srinivasan & Tendulkar *Reintegrating India with the world economy* 2004, p 12

20. See Rakesh Mohan's article *Industrial Policy and Controls* in Jalan Supra, p .86


22 Srinivasan and Tendulkar Supra, p. 16


24. Debroy ibid g. 45, lists QRs on imports, restrictions on FDI, industrial licensing the MRTP act, FERA, Public Sector reservation, SSI reservation and Government Procurement Policies.

25. From Jagdish Bhagwati in *India in Transition: Freeing the economy*. He provides a lucid account of the Model that India adopted, what went wrong, and what is to be done. He refutes the argument that India's disappointing economic outcome was a trade off for her political success as democracy.


27. For eg. Reports of the Alexander Commission, the Dagli Commission, the Arjun Sen Gupta Commission and the L.K. Jha Commission.


30 July 1991 Statement of Industrial Policy removed industrial licensing (except in 19 industries) and eliminated Barriers under MRTP act.

- Parikh Kirit. Political Economy of Growth and Reforms in India.
32 Sharan V and Mukherji, in India's external Sector Reforms, Chapter-3 (O.U P.)
34 Stephen Krasner Structural Conflict.
35. The Chelliah Committee 1991, was preceded by the Alexander Committee or trade Policy (1978), Tandon Committee (1982) and Abid Hussain Committee (1984), all stressing on overhauling India's EXIM Policies. The work continues with committees like the Kelkar task force (details available on http://commerce.net.in).
37. Kohli Supra note 28.
40. See J Bhagwati's article Growth Poverty and Reforms, in Raj and Uma Kapila Supra Note 13. He gives a sharp criticism of those economists that are themselves the unwitting cause of perpetuation of poverty. Rather true heroes like Dr. Manmohan Singh have vigorously worked for reform policies.
41. See Meghnad Desai's paper What should be India's Economic Priorities in a Globalising World (Public lecture organized by ICRIER and ASSOCHAM).