The State, Capital and Development in 'Emerging' India

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Abstract- *India's story of the last two decades since the country made a transition to a liberal economic policy regime has many sides to it that may be considered somewhat remarkable in the light of her historical legacy. India has in this period certainly been an important part of the story of the 'rise of the rest' and appears to be one of the most successful cases of increased integration into the global economy despite her less remarkable history of industrialization. Instead of losing ground in global competition, Indian big business which till then had grown in the sheltered environment provided by protectionism has experienced a growth more rapid than in the past and stepped on to the global stage. Two decades of development under liberalization, however, has also had a very exclusive character, its narrow social base precluding the possibility of any broad social consensus on liberalization? The durability of such a process in the background of India's long and stable history of having a formal political structure of representative democracy based on universal adult suffrage is then another of its remarkable features. This paper tries to explain how these phenomena that may appear surprising at first sight, are mutually interrelated and linked up with the process of liberalization itself.*

1. Introduction

Whether it is a process of capitalist industrialization and expansion in a Third World country, or its larger economic and social transformation called 'development', the importance of the role played by the state in shaping the outcomes is always crucial. This includes the degree of success it achieves in reconciling the two processes that are not automatically coincident, more so in an economy with a large non-capitalist segment. At first sight India's economic trajectory over the last two decades would appear to be one where great success has been achieved on the economic expansion front, making India one of the prominent examples of the 'rise of the rest' (Amsden 2001). Whether this has happened because of or despite the Indian state may be less clear given that the background to it has been a process of economic liberalization and a redefining of the relationship between the state and private capital in the economic realm. There can, however, be little doubt that there are other dimensions of that trajectory which certainly reflect persistence, and maybe even reinforcement, of barriers to India's escape from the underdevelopment trap.

The totality of India's liberalization story – encompassing its origins and sustenance as well as its consequences – has an enigmatic character to it. Some parts of that story can easily be causally related to others but these explanatory factors themselves often elude simple explanations. How did a country which was amongst the poorest in the world and had one of the less remarkable industrialization experiences of the second half of the twentieth century make the transition to greater integration with the

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global economy and make it 'successfully'? Why has this 'emergence' expressed itself mainly in terms of aggregate economic performance and the positive fortunes of Indian business firms but bypassed the vast majority? How has this increasing divergence between economic growth and development been consistent with the maintenance of India's democratic political system? How long can this kind of a trajectory with two rather different sides to it sustain itself both economically as well as politically? This paper does not provide the comprehensive analysis of the Indian experience of the last two decades that must be the basis for answering such questions. It does, however, highlight some of the important economic forces that have been at work within and outside the purely economic sphere in shaping the multi-faceted story of India's 'emergence'. It argues that the developmental 'failure' of the Indian state in the last two decades has been endogenously determined – it is a joint-product of that very same liberalization which created the conditions for the specific kind of rapid expansion witnessed.

The first part of the paper expands on theme of puzzles associated with India's liberalization story. The next part then briefly reviews the impact of the pre-liberalization economic strategy and the setting up the conditions for the transition to liberalization. This is followed by a description of the economic growth story of the last two decades and how its different elements mutually relate to each other. The fourth part then focuses on examining how the redefining of the economic role of the state has affected the state itself and altered the state-society relationship in a definite direction. At the end, a short conclusion sums up the argument.

II. Indian Liberalization and its Puzzles

The immediate trigger to liberalization was the 1991 foreign exchange crisis which forced India to turn to the IMF for assistance. This was not however the first such crisis, and nor was it the first one where external pressure was brought to bear on the Indian State to influence its economic policies (Ghosh 1999). But the response of the State in 1991 was unlike that in any previous case, initiating a long-term policy shift that continued even after the immediate crisis had passed.

The advent of the liberal economic policy regime in India was also not preceded by any dramatic political change to which the shift could be linked. The very same Indian National Congress which had been at the helm of affairs when India's post-independence dirigiste strategy was put in place also led the initial march towards liberalization some four decades later. In the 1991 general elections that brought it back to power, it was not economic liberalization but the implementation of the recommendations of the Mandal Commission by the previous government and the Ram Janambhoomi-Babri Masjid dispute, and then the assassination of the former Prime Minister mid-way through the elections, which dominated the discourse.

The intriguing fact that further confronts us is that the progress of Indian liberalization has remained largely immune to the successive changes in government and political realignments witnessed over the last two decades. Parties across the Indian political spectrum, with the exception of the Left, have exhibit no tendency to fundamentally challenge the liberalization paradigm. It would be, however, very difficult to argue that this is a reflection of the emergence of a new social consensus. While a range of discontents did exist in Indian society with the results of the earlier strategy there was no coalescing of these into a shared interest in liberalization. The changeover instead was as sudden as it was far reaching. It was a top-down process with actors within the Indian policy making elite and in international financial institutions initially crafting the policy shift (Sengupta 2008).

If there were any segments of Indian society which came to actively endorse liberalization once it had been initiated, it was Indian business and some part of the middle class. This is important in explaining the durability of the liberalization process given that the social influence of these two groups far exceeds their numerical proportion in Indian society. Of these, the change in the attitude of Indian business is a little harder to explain. Whatever initial misgivings some of them may have had at the beginning, Indian big business came to eventually actively push the 'reform' agenda (Pedersen 2007, Kohli 2009). Its new and the old constituents had, however, grown in a sheltered environment provided by protectionism and built businesses that were mainly 'national'. They had great experience in manoeuvring within and through the system of controls associated with Indian dirigisme but had developed little capacity for self-development of technology (Alam 1985, Tyabji 2000). Why they should have welcomed a greater exposure to global competition is therefore not self-evident. Nor is it quite so simple to explain the great success that corporate India has experienced over the last two decades, which of course has contributed to reinforcing their endorsement of liberalization.

With liberalization the Indian economy did not experience a severe contraction of the kind Latin America and Africa had in the 'lost decade' of the 1980s. Instead it initially sustained the levels of aggregate growth attained in the 1980s, when India started growing faster than in the previous three decades and also faster than the world economy. This was followed by a shift to a phase from 2003-04 onwards when growth rates climbed to heights unprecedented in India's history, accompanied by a sharp rise in the investment and savings ratios. Even the slowdown after the global crisis has been associated with growth rates higher than had been the norm in the 1980s and 1990s. Thus there has been a significant increase in India's share in global production. It has consequently overtaken many developed as well developing countries that three decades ago were considerably larger in economic size than India. This and the appearance of Indian firms on the international stage are the two clear signs of India's 'emergence'. Yet why India, without a history of having built an internationally competitive industrial structure and similarly competitive firms should have become one of the fastest growing countries under globalization, has never been clearly explained?

It bears keeping in mind that in per capita income terms, India is still way behind even many developing countries. This acquires added significance in view of the very exclusive nature of the rising trend in income, which has virtually completely bypassed the overwhelming majority of India's populace (Sengupta, Kannan and Raveendran, 2008, Vakulabharanam 2010). Sharply rising inequality, and that too one accompanied by stagnation of their incomes, has meant that this majority has had no basis for actively supporting liberalization. Widespread discontent amongst them has instead existed and found expression in increased political instability. This has, however, failed to shift the centre of gravity of economic policy making and to that extent the democratic political system has not proved to be a check on a highly inegalitarian growth process. Measures like the National Rural Employment Guarantee Scheme (NREGA) were of course introduced at some point but within the framework of the existing policy paradigm such that they have run into difficulties as the fiscal situation has deteriorated after the global crisis.

III The Pre-history of Liberalization: The State, Industrialization and Transformation after Independence

After the strategy of 'planned economic development' was put into practice in the 1950s, state economic policy was marked by periodic changes in response to contingent circumstances. Till 1991, however, the two core elements of the strategy were maintained. The state remained interventionist in nature and the relative autonomy of the Indian economy was maintained through controls on flows of capital, goods and technologies.

The record of the pre-liberalization strategy in promoting Indian industrialization and development was certainly not spectacular. The pace of industrial growth was greater than in the colonial era (Sivasubramonian 2000) and created a fairly large and diversified industrial sector. However, the larger transformative impact of India's industrialization was of a much lower order than those that occurred in some other Asian developing countries over the same time.

Industrialization remained limited and the major part of the workforce remained in agriculture. Formal employment expanded to cover barely ten per cent of the workforce, most of it in the public sector. This formed the core basis for an expansion of the middle class. State intervention in agriculture also benefitted a stratum within the agricultural population including the upper segments of the peasantry. Yet widespread poverty remained prevalent.

What however tends to get somewhat obscured in the larger story of Indian development, is the development of Indian big business that import-substituting industrialization enabled (Mazumdar 2008a). As the manufacturing sector became more diversified Indian business groups moved from a situation of being confined to a few traditional industries like the textiles into others such as steel and steel products, chemicals, cement, automobiles and automobile products, industrial and other machinery and consumer electronics. This expansion in newer and more 'modern' industries increased the level of technological sophistication that Indian big business firms dealt with. They learnt to find, absorb, adapt, and profitably use technologies and technological advances across the industrial spectrum even if they themselves did not develop them. In other words Indian private capital did experience a process of 'learning-by-doing', and one that had a somewhat unique character given the constraints within which it happened.

Compared to the position existing at independence, this learning did not eliminate but closed the gap between Indian business firms and the top rung of firms internationally. It made Indian business firms capable of facing global competition even as the continuing weakness on the technological front pushed them in the direction of confronting this competition (Mazumdar 2008a). As the scope for industrial growth through diversification and a successive diffusion of industries exhausted its own scope, the technological requirements of capitalist expansion changed. Opening up was necessary for Indian capital to get the kind of access to technology its new stage of development required, and the facing the competition this would expose them to in turn required an unshackling of the controls they had been subjected too. Thus the conditions for the eventual switchover of Indian capital to the endorsement of liberalization were created through the process of import-substituting industrialization.

In explaining the relatively limited overall success of Indian dirigisme, two major failures of the Indian state stand out. The first of these was the limited success achieved in carrying out the agrarian reform programme after independence (Joshi 1975) to eliminate what was called the 'built-in-depressor' (Thorner 1956). Secondly, Indian big business managed to also escape disciplining by the state (Chibber 2004). What has been pejoratively called the "license-permit raj" was in reality the routine abuse, manipulation, and circumvention of the system of controls to their advantage by big business firms with the assistance of the discretionary decision-makers in the state apparatus. Private capital also successfully beat the revenue mobilization effort thereby limiting the state's ability to expand public expenditures. As a result of these, the extent and the effectiveness of the state support to industrialization and social development were undermined and were later to be used to make the case for the withdrawal of the state. The State's role, however, was still critical in making possible whatever development happened.

It would, however, be a bit of a caricature to represent the Indian state before liberalization as being entirely captive to powerful private interests. The overarching setting of an interventionist economic policy regime also provided a context for significant autonomous state action, with the political pressures emanating from the aspirations of diverse segments of Indian society influencing some of these measures. In addition, while resource constraints may have limited their actual magnitude – the idea that the state had to deliver a range of benefits to all citizens, pejoratively described by some as 'economic populism', was part of the dominant political discourse. At the same time, the milieu made for institutions like the judiciary and some public agencies to develop a particular instinctive attitude that at least partly ameliorated inherent iniquities.

Iniquitous development was therefore written into the script of Indian dirigisme and did give rise to significant social and political conflict. Authoritarianism tendencies also emerged but the political system survived by also checking them. The political structure nevertheless served more as a pressure valve rather than as an effective antidote to the iniquities inherent in the economic and social structure. In doing so, however, it did moderate the effects of these iniquities.

IV Growth and Divergence after Liberalization

The private corporate sector has grown considerably faster than the rest of the economy in the last two decades, and enlarged its share in India's national product from under 15 per cent to nearly a quarter over this period. The gap between its pace of expansion and that of the rest of the economy has also tended to be greater in periods of higher growth. This is an important difference between the pre- and post-liberalization periods. An important significance of this lies in the fact that even after two decades of such growth, formal employment in the private sector in India is under 11 million, up from about 7.68 million in 1991, when the estimated size of the labour force is about 450 million and over 750 million are in the working age group. Even this growth of private sector employment has happened alongside a parallel shrinking of public sector employment from over 19 million to less than 18 million. In other words formal employment has stagnated in absolute terms and its relative share in total employment has shrunk. There has of course been additional expansion of employment in the private formal sector of an 'informal' kind (Government of India, NCEUS 2007). Even taking this into account, it is quite clear that the rapid growth of the corporate sector has made no significant dent in the Indian employment situation.

The other side of the story of Indian growth relates to the principal sector of employment[1], namely agriculture. Here, the withdrawal of the state and other measures associated with liberal economic policies gave rise to a deep-rooted agrarian crisis since the 1990s (Patnaik 2003, 2007, Reddy and Mishra 2008). Over 200,000 suicides by farmers since then was only one symptom. Some pockets of dynamism apart, the agrarian crisis has had a generally adverse effect on livelihoods. Distress driven exit from the sector on the other hand could not be absorbed by the rapidly growing private corporate sector with the result that non-agricultural informal employment has swelled. Moreover, this has happened in a situation where the agrarian situation has held down the reservation wage in non-agricultural activities.

The wage-depressing tendencies in India have been so strong that real wages have been flat or creeping downwards even in the private formal sector despite the sector's rapid growth Increasing informalization and the attitudinal changes liberalization has brought to the working of public agencies and the judiciary (Bhattacharya 2007, Papola and Sharma 2004, Roy Chowdhury 2005) have created conditions for increasingly flexible labour markets, erosion of collective bargaining and the greater role of capital in setting the terms of work. Wages in the formal sector have thus come to reflect more clearly the general labour-market situation making their trend an indicator of what has happened to income-levels in general in the last two decades. Given that India is still an extremely poor country, the trend of income stagnation and depression over large segments of its population is a particularly striking phenomenon. That food consumption trends also reflect these is testimony to the grim situation. With public expenditure also being constrained by the logic of liberalization, these conditions cannot be easily changed either.

The low levels of wages have also served to provide enabling conditions for a very different trend in the salaries of white collar employees in the private corporate sector with higher levels of education. They have ensured that these high salaries do not overinflate the total wage and salary bills of corporate firms. Indeed, the distribution of income within the private formal sector during this period has shifted decisively in favour of surplus incomes at the expense of compensation of employees. Low wages have also effectively raised the real incomes of those with higher salaries because they result in the cheap availability of a range of labour-intensive services. Insofar as many of these are non-tradable services they have also contributed to keeping the exchange rate lower than what purchasing power parity would dictate. All of these in turn have meant that the cost of production of labour-intensive tradable services also tends to be low in India, even when they involve large high salary employment as in India's software sector.

Rapid growth of the corporate sector and corporate profits has thus remained consistent with a rising trend in salaries of sections of the employees of the sector. In response, public sector salaries have also eventually gone up and more so at the higher end of the salary range. Between the two, and also because of their becoming part of a geographically mobile global work-force, there has been a considerable enrichment of an upper crust in India's middle class. The expansion and widening of that segment, which had happened to an extent earlier, has, however, almost completely ceased.

Such sharp differences in the income trends of different segments of employees are of course symptomatic of a larger story of increasing inequality. These income distribution trends have also reinforced the narrowness of the Indian domestic market with greatly different effects on the demand for industrial products and for services. The holding down of incomes of a large majority of the population has continued to keep them out of the market for manufactured goods. At the other, rising incomes of those already in the market has resulted in further diversification of their demand, increasingly in favour of services. This has meant that the aggregate consumption demand pattern has been shifting in favour of services.

Even with low wages, Indian manufacturing has not found too many niches in the internationalized system of production characteristic of the globalization era where it is competitive. Lack of public investment in health, education and infrastructure has been the problem here, contributing to keeping productivity low relative to other competing nations. On the other hand, wages are already very low and account for a very small proportion of industrial costs. The scope for gaining competitiveness by wage depression therefore practically does not exist. Thus, even while manufactured exports have grown and there has been some change in their composition, manufactured imports have tended to grow even faster. India's trade deficit has consequently become very large, with oil and gold imports adding their bit too. Indian industry therefore continues to be mainly domestic market oriented and India has not been a major recipient of the world market oriented 'efficiency-seeking' FDI. India's greatest export success after liberalization has been in services and that too in a very specific category of information technology (IT) and IT-enabled services. A significant surplus in services trade has been complemented by large inflows of remittances to partly compensate for the expanding trade deficit.

Not surprisingly, Indian growth since liberalization has been driven more than ever before by expansion of tradable and non-tradable services and construction activities rather than by that of tradable manufactured products. In the absence of significant domestic and external market growth, industrial growth in India has become excessively dependent on demand generated by investment. This, under liberalization conditions has meant private corporate investment, which has a strong tendency to be concentrated in manufacturing. This, however, has made for great instability in that investment and also industrial growth (Mazumdar 2008b). It is only the steady growth of services and their rising weight in total output that has prevented aggregate growth trends from fully reflecting the instability that has afflicted both agricultural as well as industrial growth.

The corporate sector's unprecedented expansion under liberalization has happened despite the constraints on industrialization because business firms have found profitable opportunities in the fast-growing services and of late also in construction. Rising incomes at the top as well as the transmission of speculative sentiments from the global economy via inflows of capital contributed to a sharp upturn in the growth of the construction sector. Services and construction have thus displaced manufacturing as the principal spheres of private corporate activity. In a sense, therefore, the corporate sector in India has grown by *de-industrializing* itself.

Indian business groups have clearly been the principal beneficiaries of rapid corporate growth. Indian big business thus has been able to find ample space for its own growth and development in the process of India's integration into the global economy. Partly this reflects the strengths it had acquired in the earlier stage of industrialization. There is, however, little evidence to suggest that barring the pharmaceutical industry there has been any increase in the innovative capacity of the Indian private sector and even in this exceptional case the advance has severe limits (Mani 2009, Chaudhuri 2008, Jha 2007). In software too, innovative activity in India has been mainly by foreign R & D units (Mani 2009). In other words, Indian firms still rely primarily on their experience in sourcing and using technology rather than making it. The pattern of Indian growth has therefore been to their advantage. In a number of services and construction activities, the role of self-development of technology in any case tends to be limited, but other assets like familiarity with local conditions and networks are critical because of their non-tradability. There is, however, an additional element in the success of Indian big business – the support of the state.

V 'Retreat' and 'Capture': The Indian State Under Liberalization

The transition to liberalization at one end was marked by a 'retreat of the state' insofar as both actual economic policy and its rationalizing ideology were oriented towards withdrawing the state from many of the direct roles it had been expected to perform in the past. This, however, itself required the state to assume a new role – that of overseeing that process of retreat and opening up of the economy, shaping their extent and speed, facilitating private sector entry and operation in the spheres from which it was withdrawing, etc. Thus the 'retreat' of the state was a necessarily qualified one. The very nature of the process – involving as it did privatization of public enterprises, setting the rules of private entry into a slew of sectors lacking competitive markets which were earlier dominated by the public sector (telecommunications, power, mining, petroleum and gas, banking, insurance, airlines, etc) and then creating the mechanisms for regulating them – made it amenable to manipulation by private interests just as the old control regime was. The difference was that liberalization, by opening up vast spheres of profit-making to private capital strengthened the incentive for such manipulation. The recourse to public-private partnerships in the development of infrastructure and a partly speculation driven expansion of the real estate sector have further reinforced this. It is not surprising therefore that instead of the development of arms-length relationships between the state and private capital, liberalization has given rise to corruption, cronyism and clientelism on an even larger scale.

In a deeper structural manner, the retreat of the state has also increased the leverage of private corporate capital alongside that of financial markets. Along with opening up of the economy have come inherent fiscal restrictions on the state. Constrained in its ability to drive the economy's growth process through public investment, the state has to induce the private sector to play that role. Policy has therefore had to be oriented towards encouraging private investment and that too in a context of global competition. This has had a feedback loop reinforcing itself – tax concessions rather than public expenditure have become the mechanism of inducing private investment while revenues have become dependent on the *levels* of corporate profits since rates cannot be raised. The placing of the private sector in such a privileged position has in turn made the adoption of a friendly attitude towards it a part of the general culture of state functioning in India. In a federal set-up like India's, the degree of this has been enhanced by the competition for investment between states that liberalization has forced them into. At the same time large business firms which have established themselves in key sectors have increased their clout and thus influence on regulatory policy in them. Moreover, in a globalized context, private business enterprises have also become the standard-bearers of "nationalism", "national-interest", and "national achievement" so that national success tends to be seen as something that coincides with their success.

The status enjoyed by corporate capital in India and its voice and influence over policy making process, have perhaps never been greater than has been the case under liberalization. Granting 'concessions' and providing 'incentives' to private capital, and using the state's power to facilitate private capitalist expansion (as in the case of land acquisition for private industrial, infrastructural, and real estate projects), have become second nature to the Indian state. The state's ability to discipline private capital has been further eroded and a permissive attitude towards capitalist lawlessness has also been a perceptible feature of this period. The retreat of the state has thus meant effectively a greater degree of state capture by sectional interests, in a structural sense as well as in the sense of a few well connected business groups commanding tremendous individual influence.

One side of the state-capital relationship under liberalization has been its role in facilitating the success of *Indian* capital in the face of global competition. The gradual and calibrated nature of Indian liberalization has contributed to this and facilitated the adaptation and adjustment of Indian big business to the new competitive context. It has also helped them set themselves up in many of the new sectors opened up for private capital in which they had no previous experience. The state also took countervailing measures when there was any significant threat to Indian business from foreign capital. More explicit state support has helped sectors like the export-oriented IT sector break into and maintain their position in global markets (D'Costa 2009). Individually as well as collectively, Indian private capitalist firms have therefore not scripted their success in the last two decades without the generous helping hand of the state. The stranglehold of capital over the state has, however, meant tilting it against the interests of other segments of Indian society who have found it far more difficult to claim the state's attention. Under the mutually reinforcing pressures of globalization, fiscal constraints and the growing clout of Indian big business, the capacity of the state to respond to the conditions of these sections except through the further promotion of private capital. Every phase of upturn in the aggregative economic performance generates a reluctance to do anything that might adversely affect the 'animal spirits' and the 'state of confidence' of the private investor. Every downturn generates a tendency for measures to revive these. This state of effective blindness of the state, reflected by political parties to an even greater extent when in government, has also been reinforced by the middle class endorsement of liberalization. The middle class is of course automatically a social group with a naturally strong presence in the administration, the media as well as in academia. The Indian middle class under current conditions is also becoming more exclusive since it is largely reproducing itself rather than being expanded by increased penetration by upwardly mobile sections of other social groups.

Thus, the trajectory that the Indian economy has traversed over the last two decades has carried within it an underlying basis for not only the increasing divergence witnessed but also its persistence working through the erosion of the state's capacity to respond to it.

VI Conclusion

The import-substituting industrialization centred economic growth process after India's independence was characterized by an uneven development. The degrees of structural change and social progress it brought about were limited by some crucial weaknesses which the state was unable to overcome. Yet it produced a not so visible transformation of Indian big business and its context as to make it ready to accept and even desire a greater degree of integration with the global economy and removal of other kinds of state control it had originally accepted as necessary. This set the stage for a durable transition to liberalization with the consequences of the shift being an intensification of the process of uneven development. One side of that uneven development created a powerful constituency aggressively favouring liberalization. This included Indian big business, which has experienced exceptional growth and driven the process of India's 'emergence', and a segment of the middle class. At the same time, the very logic of the liberalization process increased the leverage of private capital with the state. Capitalist priorities have thus pressed down even harder on an already constrained state which had always exhibited a weakness in its capacity to discipline private capital. State support, now in new ways, was important for the success of an Indian capital under globalization. The result, however, has been that the Indian state has become more exclusive in its outlook and unresponsive to any pressures emanating from the other side of uneven development whereby the large majority of the populace is caught in a low-income trap. The growth process characterized by highly concentrated increases in income, constraints on public investment and economic openness has been unable to create the conditions for sustained industrial expansion. Instead this growth has maintained itself, aided by the low-wage context, by assuming a pattern dominated by the expansion of services and construction activities. This trajectory is showing signs of being under strain but not any indicating any impending change of course.

End Notes

[1] In 2009-10, 53 per cent of the labour-force was in agriculture while the rural labour-force share in the total was over 71 per cent.

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