

INDIA IN THE 21ST CENTURY: AN AGENDA FOR DEVELOPMENT¹

**by
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India is at the cusp of a major transition. Within a generation a society predominantly of low income rural agriculturists will become one of middle income, urban, industrial and service workers. The absolute size of the rural population will start declining in a decade or so and a massive occupational and locational shift will move a 100 million people from rural and agricultural work to factories and service establishments in cities.

There are other transitions that will accompany this. One is the so called demographic dividend - the bulge in working age population in the North. The South on the other hand will see a rising proportion of aged retirees from the work force and face labour shortages, which are already evident in current migration trends. All this will happen in a global environment where new technologies that replace skilled labour with computer controlled machines will dull the edge of comparative advantage of low cost labour.

The transition will be reflected in the macroeconomic numbers for sure. The already declining share of agriculture in GDP will fall even more, though the shift of population out of rural areas will help to maintain a reasonably healthy rate of increase in per worker income in agriculture. The share of industry and services will zoom up to 90% or so in a matter a few decades and sustain a sharp rise in per worker incomes in urban areas. But the transition that will transform Indian society is better expressed in terms of people and their livelihood. For it is the change in the mind set from rural to urban, from the seasonal variations of agricultural work to the de-seasonalised work in industry and services, from subsistence living to one where discretionary spending is possible. It is a transition that will affect not just the economy but also politics and social relations.

None of this is cast in stone. It does not have to happen. It depends on whether our economic policies are able to maintain growth at the 6-8% rate, which is the current potential, given the 33-34% investment rate. But to do that the present orientation of policies in several areas will require substantial changes and these are outlined in the agenda for development that follows.

¹ This essay draws on the author's columns on the theme "Towards 2050" published in the Business Standard from May 2013 to November 2013.

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Ensuring macro - economic stability

The experience of East Asia has established that a long period of sustained high growth requires well managed fiscal systems, low inflation and buoyant public revenues to kick start infrastructure development. Unfortunately all three elements have been missing for the past few years. Fiscal profligacy for financing huge hand-outs in the name of inclusive growth are the rule at present and also the immediate prospect given the competitive populism between the parties vying for power in the States and at the Centre.

The transition outlined above will never take place if policies focus more on doles and subsidies rather than on the only thing that can truly reduce poverty which is constructive investments to raise the productivity of the few assets that the poor can command – their land and their skills. Nor will high rate of inflation help. Present policies are self-defeating and there must be a reversal to the sort of fiscal rectitude that prevailed in the 2003-08 high growth period.

The structural simplification of the tax system has already begun with the 10-20-30% tax bracket structure in the income tax surviving for a long time and the impending implementation of a general sales tax (GST). But much more needs to be done to rationalise the tax breaks, simplify tax codes and bring in greater accountability and probity in tax administration.

The rationalisation of the tax system should not lead to over centralisation of spending authority. Prudent fiscal management also requires a closer look at the present arrangements for revenue raising and revenue sharing between different levels of government. Fiscal resources should be available as fungible, untied resources to the entity that will make choices and spend the resources, whether it be a municipality, a district panchayat, a State government or the Centre. The present arrangement that requires large discretionary transfers downwards from the Central and State budgets does not encourage responsible approaches to revenue raising and spending. A closer look at how a substantial measure of fiscal autonomy can be granted to each level of government is very necessary.

Shifting the focus of growth to the North

The South, West and the North-West have been the high growth regions so far. The States in the North and East have been left behind, though there are some signs of acceleration in agricultural growth in the past few years. However they are still at the periphery of the industry and services growth story. This will have to change.

Sustaining high growth in India over the next few decades does depend on making the most of the demographic dividend – the bulge in the working age population that will arise as population growth slows down. The bulk of this dividend will accrue in five Northern States – UP, Bihar, Rajasthan, Madhya Pradesh and Jharkhand.

The demographic dividend can be an asset only if we have shift the locus of job oriented non-agricultural growth decisively to the Northern states. This will require a concerted effort by the Centre and the concerned States. Revisiting the fiscal transfer arrangements, as demanded by Bihar, is but a small part of this. The real challenge is not just resources but effective planning and implementation at the ground level for logistical improvements in transport, communication, information linkages and credit flows. Though the big corporates will have to be tempted to go there the initial boost will have to come from public enterprises in the region and from the promotion of small and medium enterprises which should get as much or more attention than corporate growth. The Centre can help by giving higher priority to developing infrastructure along the Gangetic corridor, for instance by duplicating with genuine vigour what they are attempting along the Delhi Mumbai corridor.

A successful effort at boosting non-agricultural growth in the North will affect the South and the West where growth will slow down as the flow of surplus labour from the North diminishes. This more than anything else will bring the private corporate sector to the North. Moreover the sort of tensions that we have seen in Mumbai lately about Biharis will become less frequent.

Ensuring high growth in industry and services

Industry and services will be the primary source of jobs and income growth in the decades to come. Sustaining high growth in these sectors will require three things – continued outward orientation so that we do not slip into stagnation behind protective walls, promoting a competitive environment locally so that successful companies outpace laggards and technological dynamism

India is fortunate in the entrepreneurial base it has in the public and private sector. But it is less than fortunate in a policy system that, despite de-licensing and liberalisation, continues to constrain options for development. Political interference even in so-called deregulated sectors is rife and crony capitalism is the order of the day, both in the Centre and the States. This has to change. We need a genuine free enterprise system where the law and the regulatory authorities intervene in an objective and transparent manner when required to protect the

public interest. This requires a change not just in the political class but also among corporate leaders who are as responsible for crony capitalism as the politicians.

One of the most potent ways of reducing crony capitalism is to promote professionalization of corporate management. This requires a process of gradual transformation of family owned and managed corporations to professionally managed corporations where the separation of ownership and management is clear and management accountability is to the whole share-holding body with boards that are truly independent from management. This is even more true of public enterprises where capricious political interference is rife. Some pressure of this sort has already surfaced from foreign institutional investors. If the domestic financial intermediaries who will handle the savings of a burgeoning middle class also join in instead of taking orders from bureaucrats and politicians this very necessary transition can be secured.

The key to corporate accountability is to make incumbent managements open to displacement. A transparent market for corporate control so that incumbent managements face real threats of takeovers will go a long way towards this. Of course it also needs better accounting and disclosure standards. A market for corporate control that is less concerned about protecting incumbent management will also go a long way towards the consolidation required in many sectors. There is no reason why public sector entities should not also be potential targets for takeovers, though the fears of crony deals will have to be recognised and respected.

Within the manufacturing sector the greatest challenge is that of technological dynamism. Indian industry has established its competence at cost-cutting innovations and reverse engineering. But as a middle income country with a growing share of global markets and a growing global presence it will have to compete with new products, processes and business models to hold its own. Supply driven technology development mainly in government labs is not enough. We need corporate research centres driven by market demands, a replication of the sort of development that has taken place partially in pharmaceuticals. This requires a change not just in official policies but also in the corporate mind-set. Public procurement, particularly for defence needs, can become a potent stimulus for corporate R & D and technological dynamism.

Technological dynamism requires more than money. It requires human resources of adequate quality. The assessments about the employability of Indian engineering graduates is truly depressing. This has to change and this will not happen if we fail to address the quality of education and research in our universities and other teaching institutes.

The infrastructure sector is badly in need of liberalisation. A lot has taken place on paper, and also in reality in sectors like telecommunications. But much more can be done even when we recognise the inherently monopolistic characteristics imposed by available technologies. For instance, even if power transmission has to remain a monopoly we can allow consumers a choice of suppliers and encourage private or cooperative local mini-grids for distributing decentralised power generated in wind mills or solar farms. We also need more competition in primary energy supplying industries like coal and petroleum and if this means looking at the possibility of denationalisation we should do so. The big change is in the orientation of the public sector monoliths who run the power, energy supply, rail and road systems.

Corporate growth will be the primary engine of industrial growth. But both industry and services require a vibrant non-corporate sector. From the point of view of the economy they are crucial for two reasons - the jobs that they provide and their role as start-ups that experiment with new products, processes or business methods. The challenge is to allow the successful ones to flourish and grow to scale. Our existing policies of reservations for small industries are one barrier that can be removed by making all such concessions time bound for each entity so that it has to develop to a point at which it can compete without the concession. For this we need better institutions for early stage financing to incubate new ventures and enterprising funds that focus on taking promising ones to scale.

The link between agriculture and organised services will become much stronger than at present. By 2050 the number of persons dependent on agriculture will be less than one per hectare of gross cropped area as against the present worker area ratio of 1.5 with a consequent increase in average farm size and possibly an increase in mechanisation. Given how demand is evolving there will have to be a shift from food-grain oriented farms to more complex enterprises that grow a variety of higher value products like fruits and vegetables and animal husbandry products. This cannot be driven by technology extension and the driving force will come from the marketing end as was the case with milk cooperatives. This will not happen without major changes in the regulatory environment for agricultural marketing which tie farms to local mandis for marketing.

Promoting an energy transition

India is not a fossil fuel rich country, despite its large coal reserves. The key deficiency is in the availability of petroleum resources as it is central to the development of a motorised urban economy and is the preferred source of household cooking fuel. India's energy policy will inevitably be driven by the need to expand access to modern energy, ensuring security of supplies from

overseas and, increasingly, by environmental concerns about local air quality and, globally, about carbon emissions and the risks of climate change.

At present our energy policy is living in the past and addressing yesterday's challenges. The central challenge looking at the decades ahead is to develop a mix of primary energy that promotes access, ensures security of supplies and protects the environment. Coal and nuclear may offer a measure of security of supply. But they are suitable only for power generation and have their own environmental challenges. Moreover coal has a huge carbon price unless there are major breakthroughs in clean coal technology and carbon capture and storage. Petroleum and natural gas have a lower carbon footprint and are the preferred fuel for mobility and household use. But they mean a high degree of import dependence in a global environment where we may soon pass the peak of oil production. For all of these reasons India must look to a much larger contribution from renewables like hydel, solar and wind power. Along with ambitious demand management, they must become the centre piece of a low carbon energy strategy that can help to widen access, ensure energy security and reconcile energy use and environmental protection. Given this perspective energy technologies, particularly for energy efficiency, nuclear power, renewables and clean coal may be far more important in determining a country's place in the world power structure than ownership or control over oil.

Such changes in primary energy mix will imply that a much larger proportion of energy use will be mediated through electricity for example by the replacement of liquid fuel based vehicles by electric or fuel cell based cars. But the electricity system will have to be very different from the centralised monolithic systems of today. Open access, already permitted by law, must become a reality so that consumers have a choice of suppliers. Decentralised mini grids run privately or cooperatively should be encouraged to ensure better use of decentralised renewable energy resources. Smart grids that involve two way communication between using appliances and electricity supply sources so that adjustments to cope with demand and supply balances can take place at both ends will be essential.

Coping with the urban challenge

The challenge of rapid urbanisation is perhaps the one we are least equipped to meet. Between 2010 and 2050 India is expected to add about 500 million to its 2011 urban population of 377 million. Our development priorities are dominated by the demands for rural infrastructure and rural poverty alleviation. Looking ahead, these priorities will have to change with vastly larger sums being made available for urban infrastructure and affordable housing and a start made on poverty alleviation schemes in urban areas.

Resources for urban investment are important. But the central challenge is more about urban institutions than about money. Three major changes are required to cope with the challenge-radical reform of the urban land market comprehensive reconsideration of building codes and planning restrictions, and decentralisation and empowerment of city administrations.

Our urban land markets do not encourage the optimal use of land. Planning restrictions often work against urban forms that are more compact and less energy and transport intensive. Land transactions are mired in corruption because so much of the value of the land depends on planning restrictions and how they are interpreted or, for suitable sums, modified by the local authorities. In major metros much of the vacant or underused land is held by urban authorities or some public sector entity like the railways, the port trust or the defence ministry. Private developers are forced to move beyond city limits into peri-urban areas, where, with the connivance of corrupt politicians and bureaucrats they make a fortune by buying at the agricultural rate and securing a change in land use that allows them to get the rates that prevail for urban residential and commercial space. They too often sit on land banks, so that new entrants move even further out. We end up with high housing costs, a patchwork of sprawling development with vast vacant areas in between, leading to unnecessary costs for infrastructure and transport.

The key lies in unfreezing the developmental uses of publicly controlled land. Innovative ways of doing this in partnership with the private sector can be developed if the process can be put at arm's length from politics, made open, transparent and accountable.

At present our city administrations are virtually powerless and the ministries at the State capitals take all the crucial decisions on finance, spending and planning. State level politicians are unwilling to let go of the huge opportunities for money making that arise from planning decisions. This has to change. We need fully empowered local governments with full authority over planning and spending and the fiscal capacity to finance this spending - an entrepreneurial mayor (possibly directly elected), local committees to give a more direct voice to citizens at the community level, transparency in decisions about land use changes that alter values, open information on contracts and so on.

Establishing a structured social security system

Rapid growth will lead to a reduction in the incidence of poverty. But there are regions that get left behind and individuals who, if not assisted by the State will remain mired in poverty. Of course the challenge of reaching left out regions can

be addressed much more easily if the locus of growth shifts towards the Northern states where the bulk of poverty is concentrated.

An important question that we have to face is whether poverty is a group phenomenon or an individual one. At present we have designed many policies on the assumption that a whole group, defined on caste or religious lines, needs special treatment with positive discrimination. It could be argued that such a group orientation will not reach the poor as benefits may be captured largely by the creamier layers in the group. Hence positive discrimination in favour of such groups may be justified on grounds of historical injustice, but is not necessarily the best way of tackling the core goal of poverty reduction.

Schemes and policies that are directly targeted at households below the poverty line are not subject to this criticism. However many of the schemes designed in this fashion have another failing – they do not address the core challenge of raising the productivity of the poor and often just hand out doles that corrupt intermediaries can capture. Hence we will require policies that bring the poor into the high growth economy by raising the productivity of the few assets they have, improving their access to acquiring new assets and enhancing their skills to allow them to profit from new opportunities offered by a fast growing economy.

Along with this, we will need safety nets that to protect people near the poverty line (on both sides of it) from vulnerability to sudden demands like catastrophic health expenditures or recovery from disaster.

But social security in an urbanised India will have to look beyond anti-poverty programmes as traditional structures of support in times of adversity break down. India, like every capitalist economy, will need a system of social insurance covering health care, unemployment and old age needs. Schemes for low cost or subsidised health insurance, education scholarships, old age pensions and even some form of unemployment protection have been put in place in a piece meal and ad hoc manner. We now need to work towards a structured family support system that brings together all welfare entitlements under one umbrella using the aadhar system as the base for doing this. A unified social security administration can be set up to deliver all such entitlements.

Health insurance is a more complex challenge. At present less than 20% of the population has such coverage and most of them are in the public or organised private sector. Catastrophic health expenditures are one of the major factors leading to families falling into poverty. We still have a great deal of work ahead of us in terms of establishing a geographically dispersed health care system. But assuming this is done we will also have to make a start on a health insurance system that, in time, ensures universal coverage, at least for major illnesses.

Conserving the environment

The pollution load and resource pressures we will experience with growth are directly related to material throughput and energy use in the economy. With 6-8% growth this will be six to ten times larger than at present. Considering the fact that we already face major environmental and resource pressures, managing these pressures has to be an integral part of development.

Indian planners have shown some sensitivity to what could be described as rural environmental problems with special schemes for ecologically stressed areas. With the stabilisation of rural population by the middle of the next decade and the subsequent absolute decline, the focus of environmental concerns will shift to the consequences of a more rapid pace of industrialisation and urbanisation. Thus the management of urban air pollution, congestion, chemical hazards, congestion, noise pollution will become increasingly important.

The management of urbanisation and industrialisation related pollution problems will pose major challenges for public administration and create yet another window for collusion between corrupt politicians and bureaucrats and irresponsible private sector managers. We need an independent environmental agency charged with implementing the law and, at the other end, engage city administrations more fully in the enforcement of the law.

On the resources front the two big issues will be freshwater and forests. India is blessed with ample rainfall. However 50% of the annual precipitation falls on just 15 days and 90% of the country's rivers only carry water for four months in the year. A substantial part of North and East India falls in the Ganga-Brahmaputra basin and the Indus basin that originate in the Himalayas and are partly snow fed. The big challenge however is that this supply will not go up with rising population and growing urban and industrial demands. We are already facing ground water stress in many areas and most of our big cities face water shortages. The only way to manage this growing mismatch between demand and supply is water conservation on a scale and urgency that we sometimes see in energy conservation.

Forest protection will remain a major source of friction between growth advocates and environmentalists and between local communities and corporates. In fact the accelerated pace of urbanisation and industrialisation will aggravate these pressures. There is no easy answer except to say that, like other densely populated countries, India too should seek to obtain minerals and other resources from the more sparsely populated resource-exporting countries and conserve its

own forest base even if it means leaving some valuable mineral resources lying beneath the forests unutilised.

India will also face global pressures to contain its carbon emissions. It has so far avoided this on the grounds of the historical culpability of the developed world for causing the global warming problem and the necessity of energy for development. However there is growing pressure, not just on India but also on other large developing countries like China to do the same on the ground that without that the global goal of containing climate risks cannot be attained even if the developed world were to roll back their emissions drastically. Moreover concerns about the impact on competitive strength reinforce the pressure from the developed countries. India has to see this as an opportunity and try and gain a first mover advantage in energy efficiency and renewable energy technologies that will be the growth element in the world energy economy.

Reforming politics

The reform of public administration is something that the Government attempts and abandons at regular intervals. This reflects the persisting dissatisfaction with the efficiency and integrity of public services. Lately the issue of corruption has acquired political salience. There is also some evidence to suggest that the electorate rewards performance. But the emphasis on public administration misses the point. The core problem of governance is the way our political system has evolved to encourage corruption and even criminalisation. That in turn is a product of deeper social forces that have shaped the party system.

Today our parliamentary democracy is dominated by regional and caste interests and the national parties that try to rise above them are yielding ground. The tenor of our political is very rural with panchayat politics stretching all the way from the village to the regional and national level. One major political challenge is to ensure that the delimitation of constituencies keeps pace with urbanisation and ensures that rural areas are not over represented in the Central and State legislatures.

An urbanising and industrialising India requires a different type of politics, one based on class and economic interests rather than on inherited identities of region or caste. Right wing parties that reflect the interests of the propertied classes exist in embryo. What we are missing is a true social democratic party that can speak for the industrial proletariat that will rise rapidly in numbers. The present left parties have become marginalised into being just regional entities. A diverse and sprawling country like ours needs a left force that is less rigid ideologically, more capable of absorbing diversity of views and that provides an avenue of upward political mobility to young men in a hurry. It must also keep a significant

proportion of the middle class on its side and that means that it must be far less prone to corruption than our present parties. Can this political transition be secured?

In the last quarter of the nineteenth century USA had a high growth economy which rested on an alliance between robber baron industrialists, land speculators and pliable and corrupt politicians who preserved privilege by exploiting ethnic vote banks. If this sounds familiar it is because the India of today has a lot in common with America in the Gilded Age when great fortunes were made and venal politicians reigned. Land transactions, resource concessions and their version of what could be called public-private partnerships for infrastructure were the route to quick riches and at the root of the rot in the political system. In India today they are a part of the corrupt politics of exploitation that combines high growth and civic decay.

In the US it changed when a wave of public anger brought a couple of reforming Presidents to power who promised 'a square deal' for ordinary citizens and started the process of breaking the power of the cartels. Can this happen here even though we do not have a presidential system and the public voice is articulated largely through political parties? Will mounting street protests see the emergence of a political leader who can articulate forcefully the political transformation that a rapidly growing, urbanising economy needs? Or will we go the British and Continental route of a trade union movement spawning the birth of a social democratic alternative?

Only time will tell how our polity evolves, but evolve it will as the mind-set of people changes with urbanisation and industrialisation. Hence one seeks comfort in the poet Seamus Heaney's view:

“History says, Don't hope
On this side of the grave.
But then, once in a lifetime
The longed for tidal wave
Of justice will rise up,
And hope and history rhyme”