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The high cost of delayed reform

26 Feb, 2008, 0018 hrs IST, Swaminathan S Anklesaria Aiyar, TNN

For a short but incisive economic history of India since Independence, you should read the first hundred pages of Arvind Panagariya's new book (India: The Emerging Giant, OUP). He follows this up with an excellent discussion of key contemporary problems, including poverty and equality, deficits and

He divides the post-independence period into four phases. The first phase, 1951-65, is widely called Nehruvian socialism. But Panagariya describes this as "Take-off under a liberal regime".

Many other academics have come to the same conclusion — that what is derided as Nehruvian socialism actually applies mainly to the Garibi Hatao policies of Indira Gandhi. Yet in fairness to Indira Gandhi, she was widely believed to be implementing a socialist agenda that Nehru launched but could not implement because of vested interests.

Nehru's socialist rhetoric was at odds with his pragmatic handling of the economy. His rhetoric called for the government to control the commanding heights of the economy. He was fascinated with Soviet-style planning. Yet in practice he presided over an era of low tariff and non-tariff barriers, and easy entry of foreign direct

Shell, Exxon and Caltex entered with 100% equity and no conditions. So did dozens of MNCs in pharma and other sectors. This era had price and distribution controls, many dating from World War II, but these (and industrial licensing) became serious impediments only in the 1960s.

Phase 1 witnessed GDP growth acceleration to 4% per year from just 1% during the British Raj. Public investment in infrastructure, industry, agriculture and social sectors increased hugely in the first three Five Year Plans.

Panagariya might have made more mention of institution building in this era, which was a source of immense strength in subsequent dark days, and continues to serve us well 60 years later. Nehru's main fault was that he ignored the vital role of exports, and focused instead on import substitution.

This approach was facilitated initially by running down the huge sterling balances India inherited from World War II, and later by foreign aid. But such

Phase II, Garibi Hatao, was a disaster that slashed India's GDP growth to 2.6%, and per capita growth to almost zero. Sky-high

Phase III, 1981-88 saw the end of garibi hatao and creeping liberalisation that yielded 4.8%

Phase IV, 1988-2006 is called "Triumph of Liberalisation." GDP growth accelerated to 6.3%. Panagariya notes that we may have entered Phase V since 2004, with GDP growth averaging over 8%. Indian companies are taking over foreign companies several times their size. The balance of global economic power is shifting unmistakably away from the US and Europe towards China and India.

To me, this book demonstrates the phenomenal waste and lost opportunities of the first 40 years after Independence. Some will disagree. Kaushik Basu (EPW, 2/2/08) says that some Latin American countries that opened up early were ravaged and savaged. Back in 1991, my Times of India colleagues, Praful Bidwai and Arvind Das, warned that liberal reforms had wrecked many countries in Africa and

I am glad Panagariya has devoted one chapter to telling a tale of two countries,

Infant mortality, literacy, and other social indicators are strongly correlated with GDP per capita. So, the cost of delaying opening up in India till 1991 has to be measured in tens of millions of additional deaths, hundreds of millions left below the poverty line, and possible half a billion deprived of a decent education.

Will Phase V, the era of 8% growth, rectify these shortcomings? Fast growth has certainly provided a revenue bonanza that enables the government to do far more on the social side. But, as Panagariya points out, without reforms in the public delivery system, additional outlays may simply mean additional waste. I am less gung-ho than Panagariya on how far the private sector can replace dysfunctional public services.

Indeed, I worry about the sustainability of 8.5% growth in Phase V. Panagariya thinks that the reforms have been sufficiently wide and deep to explain 8.5% growth. But India ranks only 104th, far behind many African countries, in the Heritage Foundation's Index of Economic Freedom.

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