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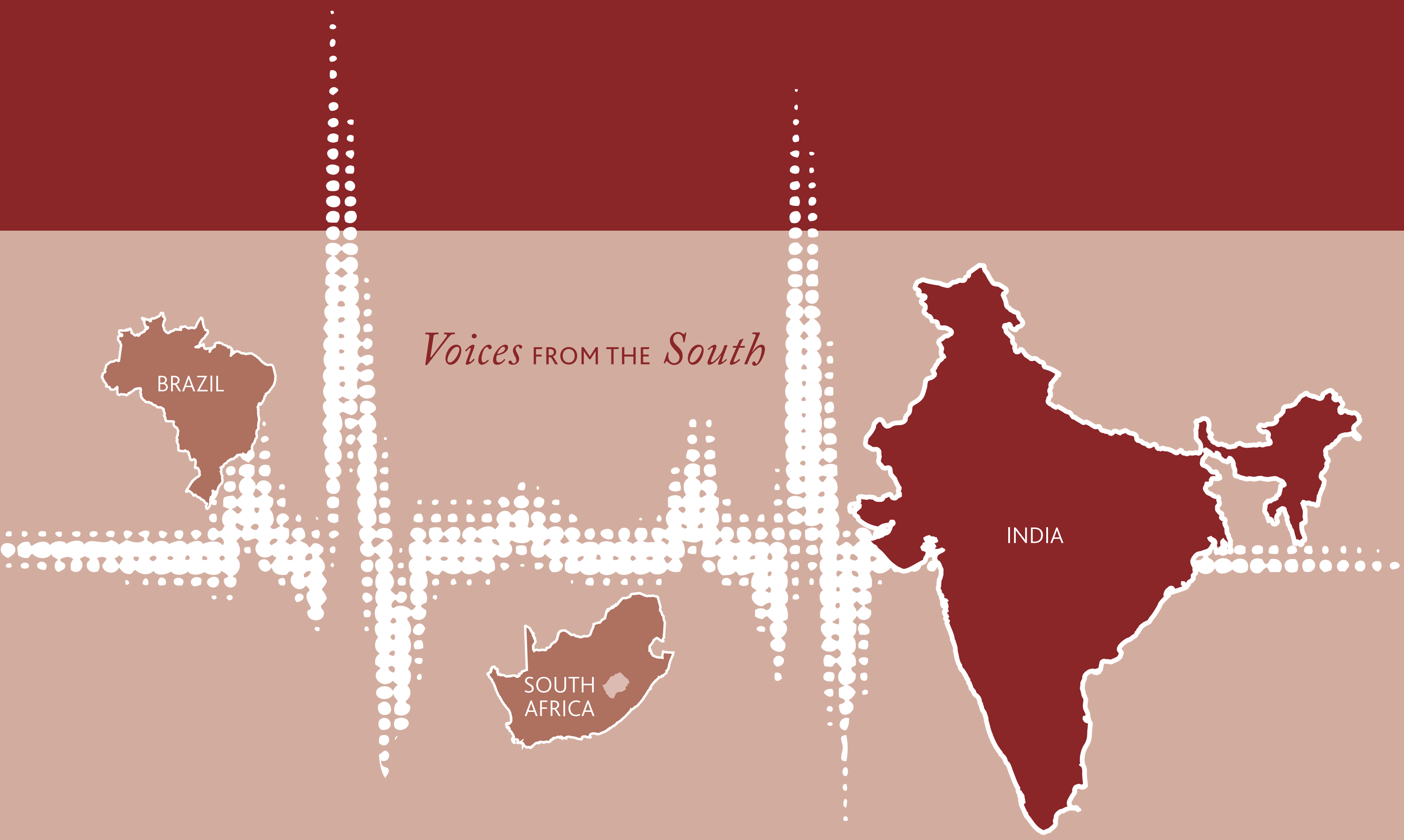
India and the Pursuit of Inclusive Growth



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Introduction

The international financial crisis of 2008 destroyed banks, companies, and jobs across the world. It also undermined the developing world's faith in Western leadership, in Western models of capitalism, in Western models of progress, even in what economists once called the Washington Consensus on macro-economics. In the subsequent vacuum, many began looking for an alternative.

Some have turned to the 'Chinese model'—the 'Beijing consensus'—for inspiration, and no wonder. China has grown with phenomenal speed over the past 20 years. Thanks to this growth, some 600 million people have escaped from poverty. At the same time, China's size and military prowess have given it an outsized strategic and diplomatic significance. The 'rise of China' is now an inescapable cliché of international political debate, so much so that some believe Chinese-style authoritarianism is a desirable, even a necessary component of economic growth.

However, China is not the only developing country which has achieved high levels of growth in the past two decades, and its model is certainly not necessary or even desirable in many parts of the world. Though they do not attract the same kind of attention as China, there are now several large, successful emerging democracies in the developing world, all of which have achieved rapid growth, at least for some periods, without Chinese-style authoritarianism. These include Turkey, Mexico, and Indonesia, as well as the three primary subjects of this series of country papers: India, Brazil, and South Africa. Through the exploration of the history, the economics, and the politics of these three countries, this series seeks to establish the element of another possible road to growth and development: the democracy 'model', or perhaps the 'democracy consensus'.

This report focuses on India, asking what lessons India's experience provides for other countries which want to promote inclusive growth as well as democracy. It is based on four specially commissioned research papers and draws on insights that emerged from a workshop discussion held in New Delhi on the 18th February 2013, attended by Indian economists, political scientists, and journalists.[1]

The report starts by outlining the origins, the resilience, and the character of Indian democracy. It then explores how India shifted from a quasi-socialist dispensation to a more open, private-sector driven economic system through the reform programme initiated in 1991. The subsequent sections examine in detail how India's democratic institutions (political pacts, elections, parliament, courts, and civil society) have affected the country's attempts to promote growth, reduce poverty, stimulate innovation, and keep corruption in check. The final section focuses on the lessons we can learn from India's pursuit of inclusive growth in the context of democracy.

The Story of India's Democracy

With the exception of the two-year state of emergency between 1975 and 1977, India has been a democracy since independence in 1947. Its democracy is vibrant, with regular elections, a multitude of parties, and a strong and active civil society and press. The country has had several peaceful transfers of power from one party to another at both the national and regional levels.

Although these seem obvious points, at the time of independence, many doubted whether Indian democracy would last six years, let alone 60. In 1947, India was one of the world's poorest countries, with only a tiny middle class—the existence of a middle class having long been thought to be a prerequisite for democracy—and limited experience of democratic institutions. Nandan Nilekani, cofounder of Infosys and Chairman of the Unique Identification Authority of India (UIDAI), argues that although the British introduced limited elections as early as 1882, these were structured so as to favour those of a higher caste or greater wealth. A Brahmin was 100 times more likely to possess the vote than a lower-caste Mahar. Rather than spreading civilising effects, Nilekani argues, the British reinforced the caste system and the regional distinctions of Indian society. [2]

The real drivers of democracy were the leaders of India's independence movement, who had mobilised Indians against colonialism and who realised that national unity could be maintained only if the profoundly diverse Indian population had a say in their own affairs. This first generation of leaders—Mahatma Gandhi, Jawaharlal Nehru, and Dr BR Ambedkar—acquired an unshakable commitment to democratic forms of government during the long struggle against British rule. [3]

After almost 65 years of democracy, India's fundamentals are relatively strong. Debate is vibrant: 38 parties and two independents sit in India's 545-seat Parliament. According to the *Democracy Index* compiled by *The Economist*, India is ranked 38th out of 165 nations. [4] The *Index* also gives India high scores on electoral process and pluralism, functioning of government, and civil liberties. It does much less well on political participation and political culture, as levels of corruption are very high—more on this below—creating high levels of public distrust. India has the largest circulation of newspapers in the world, and at least 360 independent television stations. [5] On the whole, Indian media encourages democratic participation and discussion by inspiring different viewpoints. Though the media is often critical of government, in some regions and in some cases it too is affected by corruption.

Historian Ramachandra Guha neatly summed up the contradictions of the Indian situation: very strong democratic elements exist alongside profound problems that weaken democracy. "On the one hand elections are fair and regular; there is a vigorous press and independent judiciary; Indians are freer to speak, learn, and administer themselves in their own languages than in supposedly older nations and allegedly more advanced democracies. On the other hand, politicians in India are corrupt and the police often brutal, the bureaucracy is incompetent, and the divisions of caste, class, and religion produce much social discomfort." [6]

DEMOCRACY AND MARKET REFORMS

As a developing country, India made a remarkably early transition to democracy, and the commitment to representative government remains strong. However, during the first four decades of its independence, India's leaders restrained market-based economic activities and sought to establish a centrally-planned economy. The paradox is that a country and its elite, which so readily accepted the idea of political freedom, did not embrace economic freedom. India's first Prime Minister, Jawaharlal Nehru, admired the economic success of the Soviet Union and the "poor people's" revolution that he thought was taking place in China. He and the majority of the Indian elite believed that only the state could bring about economic growth. In 1958, Nehru defined socialism as follows: "Distribution, which means cutting off the pockets of the people who have too much money, and nationalisation. Both these are desirable objectives." [7] He, as well as most other Indian leaders and experts of the time, believed that the private sector was incapable of driving development and industrialisation. [8]

Trade unions were heavily involved in the struggle for India's independence. Following independence, the trade union movement pushed the government to the left, lobbying successfully for laws which gave extensive protection to labour. These included the Industrial Disputes Act of 1947, the Factories Act of 1948, the Minimum Wages Act of 1948, and the Employees State Insurance Act of 1948. [9] The Industrial Disputes Act of 1947 listed a wide range of industries which could be nationalised. These included banks, railways, coal, textiles, iron and steel, and even foodstuffs.

The core elements of the economic system during this period were the official licences that companies had to obtain if they wanted to manufacture goods and the numerous restrictions on private economic decisions. Up to 80 agencies had to be satisfied before a firm could be granted a licence to produce. In addition, the government sought to determine what private companies could produce, how much, at what price, and from where they could source their capital. The government also prevented firms from laying off workers or closing factories. This economic system came to be known as the 'Licence Raj'.

Some people close to government rejected the view that state planning was the only viable path for India. Prominently, Professor BR Shenoy, who had submitted a 'note of dissent' as part of the panel of economists appointed to appraise Nehru's Second Five-Year Plan, also pointed out that state control of the Indian economy had brought little progress for Indian workers. He noted that, although Indian workers were more than twice as productive in the mid-1960s as they had been in the early 1950s, their wages had only increased by 20 percent. [10]

What followed was, however, an intensification of state interference in the economy. In 1969, the government introduced a policy that placed restrictions on the size of many companies, preventing the attainment of economies of scale. In July of that year, the Prime Minister at the time, Indira Gandhi, issued a midnight ordinance which nationalised the country's 14 largest commercial banks. These banks held 85 percent of the country's deposits.[11] At the same time, foreign banks were prevented from investing in India. This was followed by the Foreign Exchange Regulations Act (FERA) of 1973, which imposed draconian currency controls and restrictions on foreign investment. Other restrictive laws implemented in the 1970s included restrictions on land ownership and on the size of large companies. For example, the Urban Land Ceiling Act of 1976 imposed a ceiling of 500 to 2000 square meters on urban land holdings and introduced major distortions into urban land markets. Some economic liberalisation took place in the early 1980s, and the government began to see private businesses in a more positive light, but India only formally turned away from socialism at the beginning of the 1990s. [12] The Soviet Union had collapsed, and in China, Deng Xiaoping had begun to bring back markets. New ideas about the role of the private sector in generating economic growth, the role of competition in increasing efficiency, and the importance of international trade and foreign investment in improving productivity pushed India in the direction of reforms. [13]

Thus the period from independence to 1991 saw India grow slowly, adding only 1 percent per annum to per-capita income and leaving poverty levels broadly unaffected. In 1991, following the assassination of Congress Party President Rajiv Gandhi, the party appointed P.V. Narasimha Rao as a compromise candidate for Prime Minister. Rao, though close to retirement, rose above the established party factions and pushed government policies in new directions. [14] The reforms that he initiated included the appointment of an economist, Dr Manmohan Singh, the current Prime Minister of India, as the Minister of Finance. Singh, with the support of Rao, devalued the rupee, implemented policies which would encourage exports, and began to remove the core elements of the 'Licence Raj'. [15]

Rao's reforms were nevertheless a response not so much to ideological change, but rather to the pressure to prevent an imminent balance-of-payments crisis. Political unrest, reckless spending, and high oil prices rendered the Indian Treasury bare and left the government with less than two weeks' worth of foreign exchange. The dire state of the country's finances forced the government to airlift 47 tonnes of gold to the Bank of England as collateral, pending an International Monetary Fund (IMF) agreement. [16]

In response to this crisis, Singh devalued the rupee by 18 percent and allowed the rupee to be traded at market rates. The 1991/92 Indian budget aimed to cut the fiscal deficit to 2 percent. Industrial licensing was largely abolished, and foreign investors were allowed to buy up to 51 percent of shares in a number of industries. The government began to disinvest from some parts of the public sector. Other reforms included the abolition of import licensing controls for almost all goods, the reduction of customs duties (which had reached 300 percent in some cases in the early 1990s), the freeing of interest rates, the creation of a national stock exchange, and the introduction of policies designed to permit foreign investment in Indian equities. [17]

Over time, the 1991 economic reforms liberalised capital controls; graduated the rupee to a floating currency; and reduced marginal tax rates on individuals and firms as well as customs and excise duties significantly. The import control system for inputs to production and capital goods was discontinued for most industries.

As a result, markets and economic freedom became a much larger feature of the Indian economic system than before, putting the country in a much better position to harness the economic benefits of democracy. Yet broad support for the reforms was neither sought nor granted. The political scientist Atul Kohli argues that the 1991 reforms were implemented at the highest levels, without much discussion or consultation. To avoid discussing many of the reforms in parliament, the government resorted to legal technicalities, such as putting the reforms into a 'statement' rather than a 'resolution': a resolution has to be discussed in parliament, a statement does not. [18]

In 1996, the Congress Party and Rao were voted out of power, though not as a result of the reforms. In fact, the party that eventually rose to power, the Bharatiya Janata Party (BJP), stood for "self-reliance in the economy," opposed government intervention, and encouraged private investment. However, the most important factors in its victory were the corruption scandals that compromised many top-level members of the Congress Party, as well as the BJP's Hindu nationalism. The outcome of the election was a hung parliament, and between 1996 and 1998 India was governed by a coalition of regional parties which called themselves the United Front. [19] Since then, coalitions have become necessary to govern India. None of these have sought to reverse the reforms of 1991, but none of them have significantly extended the reform programme either.

Democracy and Economic Growth

INDIA'S GROWTH PERFORMANCE

The reforms of 1991 allowed India to achieve rapid economic growth. Previously, between 1950 and 1980, India's GDP growth averaged only 3.5 percent, a rate only half that of the so-called Asian Tigers, whose export-orientated, competitive manufacturing sector grew much more quickly. This rate of growth was far below what the country needed. Between 1980 and 1992, Indian growth accelerated to 5.5 percent, thanks to some economic liberalisation and high levels of public spending which ultimately proved unsustainable. From 1992 to 2003, however, the growth rate was 6.0 percent, and from 2003 to 2010 the country experienced a phenomenal average GDP growth of 8.5 percent.[20] According to the World Bank, India's GDP grew by 6.3 percent in 2011 and 3.2 percent in 2012. [21]

Stupendous gains in enterprise valuations immediately followed the 1991 reforms. Within a year, the stock index doubled in value. The resulting investment boom contributed to the surge in GDP growth. [22]

Jagdish Bhagwati and Arvind Panagariya point out that, thanks to trade liberalisation, the trade-to-GDP ratio rose from 17 percent in 1990/91 to 50 percent by the late 2000s; foreign investment rose from US$100 million in 1990/91 to more than US$60 billion in 2007/08; the liberalisation of telecommunications meant that while only 5 million Indians had telephones in 1990/91, 15 million new users are now added every month. As a result of liberalisation, automobile-production rose from 180,000 cars in 1991 to 2 million in 2010. [23]

More generally, the partial withdrawal of the state allowed private entrepreneurs to take initiatives without requiring state permission, and to test these initiatives in competitive local and international markets. As a result, developments and firms emerged in areas—such as information technology—that no planning process could have foreseen.

The end of the Licence Raj meant that businesses no longer had to secure an industrial licence to operate. In the 1980s, more than half of applications to start businesses were rejected, and licences were often only granted to those who were politically connected. [24] At the same time, easier access to funding—thanks to reforms in the banking system—further boosted Indian business and the country's economy. Apart from large global leaders like Infosys and Tata, it has been estimated that in 2012 small and medium enterprises accounted for 22 percent of Indian GDP. [25] In addition, these businesses are, after farms, the largest employers and account for nearly half of Indian manufacturing output. [26]

As a result, entrepreneurs have become the heart of the Indian economy. Author and former businessman Gurcharan Das argues that the 1990s witnessed a shift in the mind-set of Indians. Previously, the accumulation of wealth had been seen as vulgar, and the stereotype of an entrepreneur had more in common with a Bollywood villain. From the 1990s onwards, the pursuit of wealth became more acceptable and children from upper-caste families increasingly began to follow business-related careers. [27]

At the same time, members of the lower castes also began to take advantage of deregulation, coupled with democratic rights and freedoms, to access opportunities that were previously unattainable. One cause of this was the migration from tradition-bound villages to much more open cities. Nearly half of all *Dalit* households, the lowest caste, now have a member working in the cities, pursuing new professions, or running their own business. Recently, the Indian Planning Commission invited 30 Dalits who had accumulated wealth of more than 10 million rupees (US$160,000) to a special meeting. The leader of the group, Milind Kamble, explained their success in the following terms: "With the emergence of globalisation and the disappearance of the Licence-Permit Raj, many opportunities appeared and many of us jumped on them." [28] When the Indian government asked how many had made use of state support to start their businesses, only one of the thirty said that he had. Deregulation thus opened up opportunities for previously excluded groups to use their entrepreneurial abilities to create wealth and jobs.

However, India's labour market is still restricted: Chapter VB of the Industrial Disputes Act of 1947 seeks to make it nearly impossible for manufacturing firms with 100 or more workers to conduct lay-offs under any circumstances. Such constraints make many large, labour-intensive firms uncompetitive in world markets. Small firms, in turn, are unable to compete as they cannot attain economies of scale. For these reasons, India's economic boom differs from the boom experienced by South Korea and Taiwan, among others. India's growth was not based on the use of low-wage labour or manufactured goods for export. Instead, much of India's initial growth-spurt has been because of "brain-intensive" exports. [29]

ECONOMIC GROWTH AND THE STATE

While deregulation was a critical driver of the growth that emerged after 1991, this does not imply that there is no role for the state. Market activities work best with a supportive state and institutions such as an efficient bureaucracy, effective contract-enforcement, and property rights.

Property rights are still weak but are becoming stronger. While initially protected under the Constitution, subsequent amendments removed the provisions for property rights.[30] As a result, disputes are common. It is estimated that up to 80 percent of cases in India's lower courts are to do with land disputes. One in ten murders is believed to be linked to arguments over land rights.[31] However, this is starting to change. With the help of GPS technology, individual Indians are now able to prove their land claims, and courts are increasingly providing land titles to such individuals.[32] Intellectual property rights have also received insufficient protection in the past, but as discussed further below, this problem is also now being addressed.

Providing education directly or through a regulatory environment in which private providers can play a crucial role is another critical function of the state. This determines a country's human-capital levels, which are a major determinant of productivity. India has done well with ensuring that young people have access to education. The gross enrolment rate (GER) at primary level is 100 percent.[33] There has also been some expansion in the higher education sector. At independence, India had less than 30 universities and only 400,000 people in tertiary education. There are now more than 600 universities and 20 million people in tertiary education. The number of other post-school training institutions, such as colleges, has also gone up significantly.[34] However, there are concerns about the quality of education, especially in the public sector, which need to be addressed to create further improvements in human capital.[35]

A number of important institutions were established in the post-Licence Raj era, which helped create new state capacity, as well as improving the relationship between the state and private corporations. These included the establishment of world-class financial institutions, such as stock exchanges and clearing houses. Public-private partnerships (PPPs) also became more common. In 2011, there were more than 700 PPPs in India. More than half of these were to do with the construction of roads, with urban development and education PPPs also accounting for a large proportion. The value of these PPPs was nearly US$8 billion.[36]

Although the regulatory environment in India still has a number of weaknesses, it is improving, which bodes well for economic certainty and further growth.

ONGOING BARRIERS TO GROWTH

Despite the extensive deregulation that occurred after 1991, Indian businesses still face too many restrictions. According to the 2014 World Bank's *Doing Business* report, India was ranked 134 out of 189 countries on the ease of doing business.

On the ease of enforcing contracts, India was ranked 186th out of 189, 182nd on dealing with construction permits, 179th for starting a business, 158th on paying taxes, 137th for trading across borders, 121st for resolving insolvency, and 111th for the ease of getting electricity. [37] Even when compared to 24 other major emerging-market economies, including Brazil and South Africa, as well as Turkey, Thailand, Mexico, and a number of post-Soviet Eastern European states, India still fares badly. Out of the 24 counties ranked, it is rated 21st. On the ten indicators used by the World Bank, India was in the bottom half of the 24 emerging-market countries on seven of them. [38]

India is tackling many of these challenges. For example, the number of days it takes to start a business has dropped from 87 days in 2004 to 27 days in 2014. However, other countries are reforming faster, and making themselves more desirable areas for investment.

THE CURRENT GROWTH SLOW-DOWN

India's economic growth has slowed in recent years. After nearly double-digit growth for a decade, it slowed to under 4 percent in 2013, and is projected by the World Bank and the IMF to reach similar levels in 2014. [39] While growth is still high compared to other developing countries, slower growth has been accompanied by rising inflation (above 7 percent) and a rising fiscal deficit (reaching 4.9 percent in the 2012-13 financial year). [40] This means that lower interest rates and increased government spending are not really available as a means to raise the growth rate. It also suggests that India's economic problems are not cyclical but rather structural in nature. There are, in other words, some fundamental problems in the system that need to be reformed through decisive government action. A recent IMF assessment of India's economy set this out clearly, listing the following structural (or supply-side) challenges holding back the Indian economy:

- Rising policy uncertainty, in particular high profile tax policy decisions announced in the 2012/13 Budget, have reduced foreign investors' interest in India, while the increasing difficulty of obtaining land-use and environmental permits have raised regulatory uncertainty for infrastructure and other large-scale projects.
- As a reaction to recent high-profile governance scandals, project approvals, clearances, and implementation have slowed sharply.
- Supply bottlenecks are particularly pronounced in mining and power, with attendant consequences for the broader economy, especially manufacturing. [41]

The current Indian government recognises these challenges. The Deputy Chairman of the Planning Commission, Montek Singh Ahluwalia, recently declared that despite the inevitable uncertainties created by the 2014 General Elections, "India can achieve an eight percent growth rate, provided it takes measures to do so." [42] He focused, in particular, on the power shortages and interruptions plaguing India, but he provided few details on how exactly the government planned to strengthen policy certainty, scale up infrastructure investment, and eradicate supply bottlenecks.

Preparations for the election in May 2014 created pressure on the government to deliver higher growth, especially as rates were speculated to lead to rising unemployment. However, many fear that the elections will produce grandiose promises and short-term solutions that will raise the deficit and inflation rather than the growth rate.

DEMOCRACY AND GROWTH

The high growth rates of the past 20 years reduced the pressure on the government to continue with the reform programme. Instead, they allowed the national and some state governments to focus heavily on redistributive programmes. Coalition politics and a fractured electorate, while creating some checks and balances, have also made it hard for party leaders to push through comprehensive reforms. Larger parties need to secure the support of small and regional parties by making promises and concessions in return for support. The current nature of Indian politics has, in many areas, produced a politics of compromise that prevents the government from acting decisively.

The political process in India, especially in Parliament, is also being held hostage by partisan politicians. The primary opposition, the BJP, is deliberately flouting parliamentary convention and protocol, which has allowed them to block a number of necessary reforms. [43] During the most recent parliamentary session, such disruptions hampered the passage of bills on land acquisition and compensation as well as pension reform. These disruptions also impeded amendments to the Right to Information Act and Supreme Court rulings on legislators convicted of criminal offenses. [44] Most recently, reforms which would pave the way for foreign direct investment in multi-brand retail got bogged down in a year-long debate. Eventually, the government decided to allow 51 percent foreign direct investment in multi-brand retail trading, but left the implementation to the states. Twelve of India's 29 states agreed to implement the decision, but since then Delhi and Rajastan have rescinded the agreement. Finally, a range of interest groups such as farmers' associations, teachers' unions, and other labour unions have been quite successful at blocking reforms relating to loan-waiver schemes, education, and the labour market.

At the same time, the involvement of India's growing middle class in politics and civic action is bringing about real change. [45] As in other parts of the world, the middle classes are demanding a more effective, less corrupt, and more accountable state. Democratic politics could thereby encourage a more vigorous reform programme based on broad-based support.

This growing demand for better governance is not confined only to the middle class. In 2009, the economist Arvind Subramanian noted: "Recently, Indian voters have started to reward good performance, especially in state-level politics." [46] Popular state chief ministers who have been both highly touted for their economic achievements and richly rewarded by voters, include leaders such as Narendra

Modi in Gujarat, Raman Singh in Chhattisgarh and Shivraj Singh Chouhan in Madhya Pradesh.

The evidence in support of the notion that voters in India are now rewarding parties who deliver better economic outcomes is backed up by data. A study by Poonam Gupta and Arvind Panagariya, found a significant, positive association between economic growth and the electoral prospects of candidates contesting India's 2009 Parliamentary Elections. Furthermore, a July 2013 all-India pre-election survey conducted by the Centre for the Study of Developing Societies (CSDS) found that, of voters who expressed a preference, the economy and development were among the most important determinants of their vote choice. [47] Now that high growth can no longer be taken for granted, and voters are becoming more focused on the importance of growth, the political class has new opportunities to push for reforms with the support of the electorate.

Democracy and Poverty Reduction

TRENDS IN POVERTY REDUCTION AND INEQUALITY

For the first nearly four decades after independence, economic growth expanded the absolute size of the Indian economy, but population growth reduced the gains from growth in per-capita terms. From 1956 to 1981, when the Licence Raj restricted the growth rate to 3.2 percent, per-capita growth actually fell below 1 percent per annum. Even this income was not distributed evenly, and the income that did accrue to the poor was insufficient to lift many people above the poverty line. As a result, the proportion of Indians living in poverty actually grew from 45 percent in 1951 to 56 percent in 1974. [48] In 1951, it was estimated that about 45.3 percent of the population lived in poverty. In 1983 this had barely changed, with 43 percent of the Indian population still stuck in poverty.

This situation began to change in the 1980s. Per-capita growth rose to 2.4 percent for the period 1982—88, and then rose again to 3.8 percent for the period up to and including 2003. During the period 2004 to 2012, per-capita growth reached 6.6 percent. Such a growth rate has the potential to double the income of all Indians in just over 10 years. [49]

These growth rates brought about dramatic poverty reduction. After 1983 the poverty rate began to decline, and since 2000 poverty reduction has accelerated to over 2 percentage points per year. According to the official poverty estimates provided by the Indian Planning Commission, the proportion of the Indian population living below the poverty line fell from 44.5 percent in 1983 to 27.5 percent in 2005 and 20.5 percent in 2010. In other words, 187.5 million Indians exited poverty between 1983 and 2005. [50]

The latest figures available from the National Planning Commission are for 2011/12 and indicate that poverty has declined further to 21.9 percent. The extent to which these improvements are a direct outcome of high growth rates is further substantiated by the tight fit between accelerations in both GDP growth and poverty reduction. [51]

However, these patterns have been called into question by those who argue that the poverty line, i.e. the income level below which people are defined as poor, has been manipulated by Indian authorities or is set too low. However, the accepted poverty line for poor countries is the World Bank poverty line of US$1.25 per capita per day. In India, poverty lines have undergone revision and the official poverty line is now the Tendulkar poverty line which, when converted into a national average and multiplied by the purchasing power parity rate of exchange, comes to almost exactly US$1.25. [52]

Inequality in India has meanwhile remained relatively constant over the past 30 years. In 1983, the Gini in India was between 32.6 and 30.3 (depending on the way incomes are measured). By 1999/2000 the Gini had decreased slightly to 29.5. The first decade of this century saw a slight increase in inequality along with a big decrease in poverty. In 2011/12, inequality was between 31.0 and 33.6—still lower than all of India's BRIC counterparts. [53] China also experienced a large drop in poverty over the same period as India, but inequality has not decreased. China's Gini measure has been on an upward trend. In 1981, inequality in China was only 23.2, but increased steadily to 33.4 in 1999 and 42.1 in 2009. [54]

The proportion of Indians who do not have enough to eat has also fallen dramatically. For example, in 1983 some 17.3 percent of Indians claimed to go hungry all or some of the time. By 2004/5 this had dropped to 2.5 percent. [55] The number of people that reported that they went hungry dropped from more than 120 million to 27 million.

INCLUDING DISADVANTAGED GROUPS

Disadvantaged groups, especially those classified as Scheduled Castes and Scheduled Tribes, have experienced significantly larger declines in poverty than other Indians. This trend emerged during, and almost certainly as a result of, the high growth rates achieved in the mid to late 2000s. Poverty for Scheduled Castes fell by 9.4 percentage points and that for Scheduled Tribes by 15.3 percentage points relative to the 6 percentage points for non-Scheduled Castes between 2005 and 2010. While these groups remain relatively disadvantaged, the gap between them and the rest of the Indian population is now rapidly closing. [56]

As noted before, though the Dalits, or the 'untouchables' still fare poorly on incomes and other indicators, their rate of improvement has been substantial. A survey of Dalits in two districts of Uttar Pradesh—one of India's poorest states with a population of almost 200 million—found that their standard of living had risen dramatically between 1990 and 2007. In 1990, in the Azamgarh district of the state, with 4.6 million people, less than 1 percent of Dalits had a television, less than 1 percent had access to a telephone, and just less than half owned a bicycle.

By 2007, some 22 percent of Dalits in the district owned a television, nearly 40 percent had access to a phone, and more than 80 percent owned a bicycle. In the Bulandshahar district, with 3.5 million people, the trends were broadly similar, although nearly half of the Dalits in that area owned a television. Two-thirds of Dalit children were in school in 2007, compared to a fifth in 1990. In addition, the proportion of Dalits reporting some form of discrimination had also dropped. [57]

EDUCATION LEVELS AND INCLUSION

Over the past 30 years, the educational attainment of disadvantaged Indians, despite some uncertainty over the data, has almost certainly improved. Disadvantaged Indians are defined here as Muslims or people who are members of the Scheduled Castes and Tribes. In 2009/10 the average duration of education for young, disadvantaged Indians was six years, the level of education attainment for young Indians who do not fall into these categories was 7.2 years. Young people are defined as individuals between the ages of 8 and 24.

In 1983, disadvantaged young Indians had an average of 2.5 years and the rest 4.3 years of schooling. This means that, in 1983, disadvantaged young Indians attended schools for about half the amount of time (58 percent) compared to their more privileged counterparts. By 2009/10, that gap had narrowed to 83 percent. This shrinking gap in educational achievement is expected to continue. [58]

In addition, the gap between the educational achievement of male and female youth is also falling. In 1983, under-privileged females aged between eight and 24 had only 51.9 percent of the educational attainment of their male counterparts. When looking at the entire population in the same age group, the numbers were only slightly better, with female educational levels at 62.8 percent of that attained by males. By 2009/10 there had been drastic improvements. Under-privileged female youth had an educational attainment rate of 90.3 percent compared to males. For all Indian youth, females had an educational attainment level of 92.7 percent of male levels. [59]

CLOSING WAGE GAPS

In addition, the ratio between the real wages of women and men in urban areas is also closing. In 1983, women aged between 15 and 24 earned 71 percent of the wages of men in the same age group. By 2009/10, women aged between 15 and 24 were earning more than men. Women now earn 1.03 rupees for every rupee earned by men in this age group. Between 1993 and 2009, this age group had seen an annual average growth rate in real wages of 3.4 percent. For men, this growth rate was 3.2 percent; for women it was 4.4 percent. [60]

For Indians aged between 25 and 59 the gap between the real wages of men and women in urban areas also closed, but not at such an impressive rate. In 1983, women's wages were 56 percent of those of men. By 2009/10 this had narrowed to 75 percent. The average annual growth rate of real wages of urban Indians in this age category was 3.2 percent between 1993 and 2009. For men, the annual average growth rate was 3.1 percent; for women it was 4.1 percent. [61]

THE PERFORMANCE OF POVERTY ALLEVIATION PROGRAMMES

In recent years, India has become increasingly inclusive as poverty levels have dropped and education and wage gaps have closed. These trends have been linked to economic growth, and not to government policies aimed specifically at promoting inclusion and reducing poverty. One of these is the Public Distribution System (PDS), a system aimed at helping poor people access food. Under the rules of the PDS, the government procures goods such as grain and rice from poor farmers, rather than using the mechanisms of the market. The government then redistributes these goods to 'fair price' shops, where the food is sold at a discounted price. People have to be in possession of an identity card in order to receive the subsidised food.

The system has been plagued by inefficiency and corruption. In 1993/94 only 28.3 percent of poor households accessed food through the PDS. This accounted for only 9 percent of their total consumption. In addition, the poor received only 14 percent of total food subsidies, with the rest of the money going to wealthier middlemen. In more recent years, the system has improved, but in 2009/10 only 53 percent of the poor accessed food through the PDS, while 34 percent of Indians who are not defined as poor were able to access it. In total, less than 15 percent of food and fuel subsidies reach the poor. About a quarter is simply unaccounted for, pointing to massive corruption, while the better off commandeer the rest. [63]

The Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) is another example of a government programme that has a limited impact on poverty. Brought into force by an Act of Parliament in 2005, the aim of the scheme is to provide 100 days of unskilled manual work for impoverished Indians. It is estimated that the expenditure of the MGNREGA will eventually account for more than 1 percent of Indian GDP. However, MGNREGA has again benefitted better-off Indians more than those who are poor. In 2009/10 some 60 percent of the beneficiaries of the scheme did not qualify as poor; they nevertheless received 17 percent more work days than the poor. The poor received only 22 percent of the total employment programme expenditures earmarked for them. [64]

POVERTY AND URBANISATION

India's urban population has increased from a quarter of the population in 1989 to 32 percent in 2012. [65] This represents a large increase in absolute numbers. In 1989, the number of people living in urban areas was 215.5 million. By 2012, this had increased by more than 80 percent, with the number of urban Indians reaching 391.5 million people. [66]

The McKinsey Global Institute estimates that the proportion of people living in urban areas in India will reach 40 percent by 2030. [67]

The National Planning Commission has shown that there is a large difference in poverty levels between urban and rural areas. [68] In 2011/12 rural poverty was measured at 25.7 percent compared to an urban poverty rate of 13.7 percent. Between 1993 and 1999, there was a strong correlation between an increase in urbanisation and a reduction in poverty in surrounding rural areas. A World Bank study showed that for every increase of 200,000 residents in an urban area, the resulting decrease in poverty in rural areas of the same district was between 1.3 and 2.6 percentage points. [69] Increased urbanisation has been an important secondary cause of the lower poverty levels in India.

POVERTY REDUCTION IN INDIA'S STATES

There are large variations in poverty levels between the states of India. According to the National Planning Commission, in 2011/12, the state with the highest level of poverty (using the Tendulkar line) was Chhattisgarh, with nearly 40 percent of the state's 25.5 million population living in poverty. The state with the lowest rate of poverty was Goa, where only 5 percent of the population lived in poverty. [70]

Goa's good performance may be skewed by the fact that it is India's smallest state by area and fourth smallest by population with only 1.5 million inhabitants. In states with more than 20 million inhabitants, the lowest poverty rate was in Kerala. In that state, 7 percent of the population lived below the poverty line. It also had the lowest rate of urban poverty for any state with a population of more than 20 million, at 5 percent. With regard to rural poverty, Punjab had the lowest rate of poverty for states with more than 20 million inhabitants, at 7.7 percent.

Advocates of state intervention in the economy often point to Kerala, which has the highest life expectancy in India (at 74), as well as the highest literacy levels. [71] The state also has the lowest rates of infant mortality, maternal mortality, and malnutrition, as well as low rates of poverty. [72] The Indian government considers Kerala one of India's three most developed states, along with Goa and Tamil Nadu. [73]

However, on other indicators Kerala fairs poorly. It has one of the highest unemployment rates in India, with high rates of suicide and alcoholism. The state does not have an industrial or manufacturing base and much of the income it receives is from remittances. Approximately one in six workers from Kerala now works overseas, primarily in the Persian Gulf, and one in three households in Kerala has a family member that works abroad. [74] With large numbers of relatively well-skilled people in Kerala with no prospects of work, many choose to take their chances elsewhere.

More importantly, Kerala's achievements do not seem to be the product of state-level policies. Private rather than state provision appears to play a large role in delivering health and education services. In 2010 more than half the children in Kerala aged between seven and 16 attended private rather than public schools, one of the highest rates in India. The figures for healthcare are similar, with a majority of Keralites opting for private healthcare. [75] Kerala's advantages also predate Indian independence. In1947, nearly half of all Keralites were literate, compared to an overall Indian literacy rate of just 18 percent. [76] Bhagwati and Panagariya have shown that, once this initial advantage is accounted for, there is nothing unique in the outcomes achieved by Kerala. On the contrary, since independence, other

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states such as Gujarat and Maharashtra have closed literacy and health gaps more quickly. [77]

Gujarat is a state that has done well in promoting growth and industrialisation, partly as a result of business-friendly policies implemented under the leadership of Narendra Modi. During his term, the government has cut red tape, improved the effectiveness and responsiveness of the bureaucracy and improved the levels of infrastructure. [78] In the eight years leading up to March 2012, Gujarat's economy grew an annual 10 percent at constant prices, against 6.45 percent in the eight years leading up to March 2002 (Modi took office in October 2001). This economic growth was still ahead of the all-India average of 6.16 percent (although a number of states, such as Maharashtra and Tamil Nadu enjoyed even higher rates of growth). [79]

As in the whole of India, these impressive growth rates were accompanied by large declines in poverty and rapid improvements in health and education levels. [80] The beneficiaries of these trends include Muslims, who are often regarded as discriminated against in Gujarat. According to Indian government statistics, the poverty rate for Muslims in that state was only 11.4 percent in 2011/12. A few years previously it had been nearly 40 percent. The overall poverty rate for Muslims in India is 25 percent. [81]

Gujarat has performed well but the source of this performance is not entirely clear. Many of the state's business-friendly reforms were put in place before Modi came to power. Gujarat also has a long coastline and much open and unused land, which has helped attract large industrial investors. [82]

DEMOCRACY AND POVERTY

As is the case for economic growth, the links between democracy and poverty reduction are not straight-forward. It is clear that the growth of the economy and accompanying rises in per-capita incomes have been the most important determinants of the dramatic reductions in poverty that India has experienced. As a result, the relationships between democracy and growth and democracy and poverty will overlap a great deal.

Certainly, democratic pressures have played a central role in keeping the government's attention firmly focused on poverty alleviation. Although many of the strategies chosen to date have not been sustainable or effective, that does not mean that electoral pressure cannot be useful in the future. If India focuses again on growth, and if the electorate continues to push for inclusive growth, the outcome could be very positive. Revenues generated from growth could be used to fund education and health programmes that will benefit all Indians, for example, rather than just a select few.

It is clear from the Indian experience that, while the mere existence of democracy will not necessarily lead to rapid poverty reductions, democracy does work when leaders implement effective growth-promoting policies, when they avoid the pitfalls of unsustainable and ineffective redistribution programmes, and when elections and other democratic institutions do the job of keeping politicians focused on serving the best interests of the public as a whole.

Democracy and Innovation

In some fields, India is able to compete at the technological frontier. It has developed nuclear weapons, is one of the few countries in the world to operate an aircraft carrier, has landed a probe on the Moon, and has recently launched another to Mars. Many of its scientists, engineers, and professionals are world-leaders in their field. At the same time, the country still fares relatively poorly on a number of indicators relating to innovation. These formal measures are not the only way to assess the innovativeness of India, however. Indians are pioneering an innovation paradigm known as *jugaad*. This can be defined as a frugal and flexible approach to innovation which does not often lead to patents or dramatic advances at the technological frontier. Rather it produces stripped-down products or cost-effective means of producing products and services, which make them accessible to lower income consumers. Given the relatively low levels of income in India, this form of innovation is highly suited to India's current circumstances.

MEASURING INDIA'S PERFORMANCE

The *Global Innovation Index (GII)* is the primary global indicator of a country's innovation performance. This is a joint venture between the World Intellectual Property Organisation (WIPO) and INSEAD, an international graduate business school based in Paris, France. A country's position on the *GII* is determined by three separate indices—an innovation output index, an innovation input index, and an innovation efficiency index. These indices are then broken down further into separate pillars which then provide an innovation score. The innovation input index is based on five pillars: institutions, human capital and research, infrastructure, market sophistication, and business sophistication. The innovation output index measures knowledge, technology, and creative outputs and the innovation efficiency index measures the ratio of innovation output to innovation input.

On the *GII* of 2012, India managed a ranking of 64th out of 141 countries. On innovation input, India ranked 40th, on innovation output 96th, and on efficiency 2nd. By way of comparison, Russia was ranked 51st, South Africa 54th, and Brazil 58th, while Switzerland was ranked the most innovative country in the world in 2012. [83]

China's overall rank on the *GII* is 34th. On innovation input it is ranked 19th, on innovation output 55th, and on efficiency 1st. There are areas where India performs well, and these are due to democratic institutions such as freedom of expression. However, it fares poorly due to poor infrastructure, poor educational outputs, low investment in research, and a lack of business sophistication. [84]

India's share of global publications in international journals is 3.5 percent, and is ranked 9th globally. In the 1990s, its share had dropped as low as 2 percent, but recovered to its current levels. This was due to an increase in funding for research, which dropped sharply in the last decade of the 20th century. [85] India's research spending of just less than 1 percent on R&D has also remained static for the past two decades. [86]

INDIAN BUSINESS INNOVATION

Since the end of the Licence Raj, the Indian business sector has grown rapidly and a number of companies have become very successful, particularly in the information technology, pharmaceutical, and automotive sectors.

The Indian IT sector has introduced the 'global delivery' model to the world. This is a way of developing and delivering customised software from development centres situated across the globe, by taking advantage of distributed skills and lower costs. In addition, India's pharmaceutical and transportation companies account for most of India's R&D. About 60 percent of all R&D in India is linked to these two sectors.

Although Indian companies have not been at the forefront of technological innovation, they have been leaders with regard to process and product innovation. Perhaps the reason for the relative lack of formal innovation at the technological frontier within Indian business is due to the practice of jugaad. [87] For example, the Indian Institute of Technology (Madras), Vortex Engineering, and ICICI Bank, found an innovative way of leveraging technology for rural benefit when they experimented with installing ATMs in a rural area near Madurai in Tamil Nadu. Conventional ATMs had high fees and were unreliable due to power cuts. After four years of experiment and modifications, the Gramateller's cash dispensing machine (CDM) was introduced. It uses less power than conventional machines, consuming 72 watts of electricity as opposed to the conventional 1 800 and is cheaper at US$790, a fifth of the normal price. [88]

The Jaipur Foot is a low-cost prosthetic limb. It uses local materials and costs as little as US$35. It has been made available across India by the Bhagwan Mahaveer Viklang Sahayata Samiti, a charitable organisation. [89]

The Arvind Eye Hospital was established by Dr G Venkatswamy, a retired government ophthalmologist. Many Indians lose their sight due to cataracts that are otherwise treatable. Venkatswamy revolutionised the treatment of cataracts by using the time of doctors for only the most critical parts of the cataract surgery, and using support staff for all other steps of the process. This radically reduced the cost of cataract-removal. The surgery for poor patients was subsidised by those who could afford to pay for the procedure. [90]

The model developed by Arvind Eyecare has been copied in a number of other fields of healthcare—from maternity to retinopathy (damage to the retina of the eye) to heart surgery.

This type of innovation in India has also filled gaps that the government cannot. Mera Gao Power (MGP) is a company that supplies electrical solar grids to villages in Uttar Pradesh, that are not on the Indian electricity grid. Each grid supplies enough electricity to power 35 households for seven hours each evening. At a cost of 100 rupees per month (about US$2) each household is supplied with two LED lights and a power point. Although the initial setup costs are relatively high (it costs about US$1,000 for each grid) the company expects to recoup its money over three years. By 2014, the company is hoping to supply 100,000 households with electricity. [91]

Despite the ingenuity reflected in these innovations, some have pointed out that jugaad often reflects solutions that are quick-fix, not particularly robust, and non-scalable and that they are a reaction to resource scarcity and a complex regulatory system. In a more deregulated and conducive business environment, it could be argued, more Indian businesses would be able to move away from the jugaad paradigm and develop innovations to compete at the technology frontier.

MULTINATIONAL INNOVATION

An area where India has excelled is in the number of foreign R&D centres that have been set up in the country by multi-national corporations (MNCs). According to some estimates there are currently 850 foreign-owned R&D centres in India. [92] Between 1995 and 2008, MNCs accounted for 53 percent of patents awarded to Indian inventors by the US Patent and Trademark Office. A limitation of the various multinational R&D centres in India is that the links with the broader Indian economy are poor—spill-overs between the two have been infrequent.

US PATENTS GRANTED TO INDIAN INVENTORS OR INDIAN ASSIGNEES [93]										
	1976-1994					1995-2008				
Field	MNC	Indian Corp.	Indian Res./ Acad.	Others	Total	MNC	Indian Corp.	Indian Res./ Acad.	Others	Total
Chem	158	19	40	69	286	432	651	962	203	2248
EE/IT	28	1	1	11	41	1789	66	44	62	1961
Instr.	13	2	1	22	38	255	23	54	55	387
Mech.	22	8	2	24	56	101	46	23	46	216
Other	2	3	1	8	14	23	6	3	17	49
Total	223	33	45	134	435	2600	792	1086	383	4861
Proportion	51.3%	7.6%	10.3%	30.8%	100%	53.5%	16.3%	22.3%	7.9%	100%

EDUCATION AND INNOVATION

A barrier to further innovation in India is the relatively poor performance of the tertiary education sector. No Indian university is in the top 200 universities in the world, and only one is in the top 500—the Indian Institute of Science, Bangalore. [94] By contrast, South Africa has three universities in the Top 500, Brazil six, and China 28.

During the prime ministership of Jawaharlal Nehru, the country aimed to create a number of high-quality technological institutions—the Indian Institutes of Technology (IITs). These were established to produce quality graduates in, particularly, engineering and management. Five had been established by the 1960s, but momentum slowed. A sixth was only opened in the 1980s and there has been only one other established since then.

However, in the 1990s, as growth started to take off, demand for engineers and other skilled people increased. This resulted in the creation of a number of private tertiary training institutions. The quality of these institutions is variable, but not enough is known about how these private institutions compare with public ones.

India's IITs can be considered the elite of Indian tertiary institutions, and produce the majority of Indian university research. However, compared to leading institutions from the rest of the world, India does relatively poorly. The research productivity of IITs is estimated as being only one tenth that of the world's leading research universities. This is due to inadequate funding, weak postgraduate funding (the focus of IITs has generally been on undergraduate programmes), and the absence of strong faculty appraisal systems.

INTELLECTUAL PROPERTY PROTECTION

India's weak regulatory framework around the protection of intellectual property has, in a slightly contradictory fashion, actually boosted innovation, especially in the pharmaceutical industry. Strong protections for intellectual property were a legacy of the British Empire. In 1970 the Indian Patents Act weakened many of these protections with especially important consequences for pharmaceutical companies. The new Act prevented companies from patenting new molecules, as well as shortening the period of patent protection.

India's role in the World Trade Organisation (WTO), and especially its participation in the Uruguay Round—which ended in 1994—pushed the country to reintroduce product patents in food and drugs which it had abolished in the 1970s. The Indian Patents Act was amended in 2004, 2005, and 2006. Although the law has changed to increase protections, the procedural environment is still lacking and the Indian patent database is still poor. Although an online patent database has been established, it is not as comprehensive or detailed as that of the United States, for example.

Indian courts have generally been conservative in granting awards for patent and intellectual property infringements. Although this means that intellectual property is not captured by corporations for very long periods, it also limits protection for inventors who may not be adequately protected from the possible infringement of intellectual property rights.

POLICY INNOVATION

Since the establishment of a National Advisory Council (NAC) in May 2004, India has begun to innovate in the area of social policy. The NAC is made up of academics and social activists from outside government and is chaired by Sonia Gandhi, the Congress Party chairman. Two major government policy innovations have been implemented, which were first conceived of within the NAC.

The first of these is the National Rural Employment Guarantee Scheme, which was launched in 2005. The second is the Right to Information Act (RTI), also passed in 2005, which gives citizens the right to obtain information from any government agency in India. This has acted as an important check not only on corruption but also on arbitrary government actions.

Another new policy initiative that may have a major impact on India is the Right to Education (RTE) Act, which came into force in 2010. This made education a fundamental right for children between the ages of six and 14. In addition, private schools have to reserve 25 percent of places for children from impoverished or discriminated backgrounds. The schools will be reimbursed for the cost of these places by the state.

An innovation with massive potential is the Unique Identity (UID) programme. This seeks to create a near fool-proof biometric database of all residents in India, making it by far the world's biggest online biometric database. The UID programme is by far the largest application of biometric identification technology to date and will improve the delivery of government services, reduce fraud and corruption, facilitate robust voting processes, and improve security. Being able to authenticate the identities of impoverished Indians will allow them to access welfare programmes, to which they have often been denied access because it has been difficult to confirm who they are. [95]

IMPROVING INDIA'S INNOVATION PERFORMANCE

Although the incentive for firms to innovate has improved since liberalisation, the inputs necessary for innovation—funding, skilled and trained staff, and basic research and development—have not kept pace with the needs or capacity of firms. Social and cultural barriers to innovation—including poor teamwork and the enduring importance of upward hierarchical progression—remain problematic. At the same time, efforts to boost economic innovation through government intervention have been ineffective due to a lack of strategic vision, inadequate resources, and poor implementation. [96]

However, India has made a number of efforts to ensure that it is not left behind in the global 'innovation race'. The National Knowledge Commission (NKC) was established in 2005 to promote policies that increase India's knowledge base. The NKC has produced white papers calling for reform of the higher education sector, including the establishment of new universities. However, opposition from a number of communist parties (which were members of the ruling coalition between 2004 and 2009) has meant that these recommendations have largely been ignored. Although they were picked up again after 2009, nothing concrete has been achieved yet.

In addition, a regulatory framework drawn to allow foreign universities to set up campuses in India, and to impose stricter standards on private universities still awaits approval by Parliament. The opposition from politicians, who directly or indirectly control much of the private higher education sector, currently ignores the electoral importance of the middle class, and those aspiring to reach it, who would benefit from increased choice and quality.

Another important initiative by the Indian government is the creation of a National Innovation Council (NIC), which was established in 2010. This was created in order to foster an innovation culture to solve social problems. Some of the initiatives that it has announced include the creation of a US$1 billion 'Inclusive Innovation Fund', the establishment of sectoral innovation councils, and the building of 'innovation eco-systems' around selected Indian higher-education institutions. These ideas have yet to be translated into action.

DECENTRALISATION AND INNOVATION

India's federal structure has created 'laboratories for innovation' in many states. For example, Tamil Nadu introduced the 'midday meal' for school children in 1982, providing one meal per day. This helped to raise enrolment rates. In 2001, a

Supreme Court ruling extended the midday meal scheme across India. [97] However, not all states have the administrative and logistical capacity to follow suit. In 2013, 23 children in Bihar died after eating their school-provided midday meal. [98] Poor hygiene has led to similar problems elsewhere.

Bihar has found an innovative solution to increase the rate of enrolment of girls in high school. It provided every 14-year-old girl with a bicycle. Consequently, the enrolment of girls in areas with the bicycle programme increased by 30 percent. [99]

Madhya Pradesh, a state in central India, introduced a law in 2010, which guaranteed the delivery of public services to residents of the state within a certain time-frame. If services were not delivered within the stipulated time-frame, the officials responsible would be fined. [100] In 2012, eight other states replicated Madhya Pradesh's Public Service Delivery Guarantee Act. [101]

DEMOCRACY AND INNOVATION

Political pressures in a democracy can lead to some harmful policy innovations that are populist in nature and economically unsustainable. The 2013 Right to Food Security Act is one such example. Critics suggest that the Act would massively increase pressure on the fiscus, costing about 3 percent of India's GDP.[102] It is estimated that the scheme will come to encompass between 10 and 28 percent of government expenditure, and reduce farmer productivity. [103] Furthermore, doubts were raised that a greater distribution of food to Indians would result in a reduction of hunger. [104] The main opposition party, the BJP, initially criticised the law, saying that it was not a food security law but a 'vote security' law, aimed at helping Congress stay in power in the national elections. [105]

Innovation in India is a reflection of the country as a whole. In some areas it is a world-leader in technology, yet for many people the standards of education are among the worst in the world and the ongoing red tape and lack of support from government bureaucracies often make it difficult to innovate in India. The best way forward is to continue strengthening democratic institutions so that information and ideas can continue to circulate freely while leaders are pressurised to implement better education policies, extensive infrastructure programmes, and civil-service reform, which will then enable the country to achieve more of its innovation potential.

Democracy and Corruption

In the era of high taxes and onerous licensing procedures, many Indians were forced to operate in the 'unofficial' economy—or had no choice other than to bribe bureaucrats and politicians in order to obtain licences and permits. Thus did the Licence Raj help entrench a culture of corruption in Indian business and society. Even today, there is a corrupt nexus between many in big business and government interests. More recently, that nexus has begun to unravel.

While India is ranked as more corrupt than most Western countries, it also lags behind most of its emerging-market rivals. According to Transparency International's *Corruption Perceptions Index* of 2013, India emerges as 94th of 177 countries—alongside countries like Benin and Algeria, and behind countries such as Liberia and Sri Lanka. [106] Brazil, South Africa, and China, rate better than India. The perception of corruption in India has also been increasing over the last decade. [107] Measuring the likelihood of multinational businesses having to pay bribes, the *Bribe Payers Index* 2011 ranked India 19th out of 28 leading economies, behind Brazil (14th) and South Africa (15th) but ahead of China (27th) and Russia (28th). [108]

Ordinary citizens are frequently expected to pay a bribe for government services, ranging between a connection to a water supply, the issuing of an identity card or passport, the facilitation of income-tax refunds, and opening a case of theft in a police station. [109] In 2013, some 54 percent of Indians admitted to having paid a bribe in the previous 12 months compared to a global average of 27 percent. [110] Janaagraha, a Bangalore-based NGO estimates that the average Indian will pay over US$4,600 in bribes over their lifetime. [111]

Despite deregulation, there is still a sizeable unofficial or 'black' economy. However, its size is disputed. The American

NGO, Global Financial Integrity, reported in 2013 that India's black economy was 42 percent of the official economy, having risen from being about 25 percent in the pre-reform era. An Indian think-tank, the National Institute of Financial Management, estimated the size of the black economy was much lower, 17 percent of GDP in 2010/11. According to the organisation, the unofficial economy had been equal to 30 percent of GDP in the early 1970s. [112]

While low-level corruption has become a norm, high-level corruption is also widespread, possibly growing. Some of the major scandals implicating the government and Congress include the misallocation of funds earmarked for the 2010 Commonwealth Games; the sale of telecoms licences which cost tax payers US$39 billion; and the 'Coalgate' scam, which implicated Prime Minister Manmohan Singh, and is estimated to have cost US$34 billion. [113]

Corruption is not restricted to those in the national government. In 2011, a senior member of the largest opposition party, the BJP, BS Yeddyurappa, had to resign. He was serving as the Chief Minister of Karnataka when he was implicated in an illegal mining scandal. A number of other scandals in the then BJP-ruled state of Uttarakhand showed that the former governing party was also prone to corruption. These included allegations about corrupt land deals, the awarding of construction contracts for 17 hydropower stations in the state to one company, and the misuse of funds earmarked for a Hindu religious festival. [114]

PARTY-POLITICAL FUNDING IN INDIA

One of the major causes of corruption is the unsatisfactory state of political funding in India, which has a long history.

In the first two decades of Indian independence, political parties were financed through private donations and membership dues, as well as corporate donations, which were legal but subject to certain restrictions. This was reversed in 1968 when corporate donations to political parties were banned to eliminate the influence of big businesses over political parties. It has also been speculated that the ban, implemented by Prime Minister Indira Gandhi, was to stop corporate interests from funding opposition parties. However, this ban on corporate funding was not matched by funding from the state, which opened the door for illegal funds, or so-called 'black' money to fund daily expenses or election campaigns. [115]

A 1974 Supreme Court ruling further restricted expenses incurred by candidates on election campaigns but their party and supporters could spend freely. In 1985, the ban on corporate donations to political parties was lifted, following an amendment of the Companies Act. However, this did not end the dependence of Indian political parties on black money, owing to a combination of the absence of tax incentives for corporate donations to political parties and the normative entrenchment of black money contributions. Paradoxically, the growing political plurality of India further undermined the move to make political donations more transparent. Businesses had to deal with a wide range of parties and individuals at the national and state levels, making the funding of all parties unaffordable. Legal donations have to be made public in annual reports, and as businesses do not want to be penalised for supporting political rivals they prefer to stick with the customary practice of secret illegal political donations.

In 1998, free air time was provided on state television and radio to seven national parties and 34 state parties. [116] This made elections less expensive for some and may have reduced the reliance on black money.

In 2003, the Election and Other Related Laws (Amendment) Act made company and individual contributions to parties (not individuals) 100 percent tax deductible. The result was a rise in transparent contributions: between 2003 and 2009 (the last election year in India) contributions to the ruling Congress increased by a factor of 35, while contributions to the main opposition, the BJP, increased by a factor of eight. [117] However, transparent contributions still make up only a small proportion of contributions to political parties.

The lack of internal democracy in many Indian parties, as well as the lack of transparency and accountability, has meant that financial accountability within parties is absent. Furthermore, party leaders have no incentive to raise funds through large numbers of small donations—it is easier to raise large sums through lobbying a relatively small number of large donors. This, along with the farcical expenditure ceilings and the absence of state funding for parties, means that a corrupt equilibrium is perpetuating itself.

In addition, the Indian economy is still subject to large amounts of state control, which means that governing parties have tremendous discretionary influence. Some argue that the 'Licence Raj' has been replaced by the 'Tender Raj' where state control over mining and other economic activities creates situations where those with political connections find themselves at the front of the queue for government contracts. [118]

DEMOCRACY AND THE FIGHT AGAINST CORRUPTION

The first measure to combat corruption in India was the Prevention of Corruption Act (POCA) of 1947, which incorporated sections of the Indian penal code. However, increasing corruption led to the formation of the Santhanam Commission of 1962, which made three primary recommendations. The first was the formation of a Central Vigilance Commission (CVC) in 1964, which would investigate complaints or suspicions of improper behaviour against civil servants, and the second was the appointment of a Chief Vigilance Officer in each ministry. Its third recommendation was the amendment of the POCA to make the possession by a civil servant of assets disproportionate to their income a crime. [119]

Other bodies were also instituted to fight corruption. The Central Bureau of Investigation (CBI) was established in 1963, but it was essentially a police agency. In addition, it is hamstrung by India's federal system, and each of the country's states has its own anti-corruption bureaus. In 1998, the CVC became a statutory body to supervise the activities of the CBI. [120] The Comptroller and Auditor-General (CAG) was also set up to audit and scrutinise government accounts.

A number of recent initiatives also ensure full background disclosure of assets by candidates for public office. In November 2000, the Delhi High Court ordered the Indian Election Commission to collect, and make public, data on the criminal records of candidates, their education, and assets, including those of their spouse or any dependent relatives. This development has led to greater transparency with regard to the background of Indian electoral candidates. [121]

The passage of the Right to Information Act (RTI) in 2005 further mandated the disclosure of official information on any matters within six weeks of an appeal being filed, with the exceptions of national security and personal privacy. The People's Ombudsman (Lokpal) Act, passed in December 2013, will result in the creation of an ombudsman with investigative power to fight corruption. [122] Investigations will be triggered by reports from the public against public servants. However, the bill has been criticised for being too weak and not broad enough in its coverage.

To tackle party finance problems, the Indian Election Commission proposed that political parties be required to maintain accounts vetted by auditors specified by the Election Commission. Failure to do so would result in deregistration. The Commission also recommended in March 2013 that political parties must identify their donors—including those pledging small amounts, as these were often used to disguise large, unidentified sources of funds.

Overall, the lack of political will from government and inefficient functioning have made these laws and agencies relatively ineffective in the fight against corruption.

For example, a 2008 analysis of the performance of the anti-corruption branch of the CBI between 1980 and 1984 revealed that nearly 700 people had been investigated and 273 had been charged, of which 144 were convicted. Only four people spent more than 20 days in prison. However, in 2008, there were still 71 of these cases on appeal in the country's high courts. The agency was still pursuing cases more than 20 years after the initial investigation. [123]

Data about the general backlog in Indian courts from recent years are not available, but in 2008 more than 50,000 cases were waiting to be heard in the Supreme Court, more than 4 million in the high courts, and nearly 30 million in the lower courts. The average caseload for an Indian judge at any one time is more than 2,000. [124]

There is also corruption within the judiciary. In 2012, the anti-corruption arm of the police in Maharashtra (of which Mumbai is the capital) challenged a number of findings of a judge, who since 2007 had acquitted 41 out of 45 people charged with corruption. The Maharashtra police did not agree with 31 of these acquittals and questioned the judge's integrity. [125]

In addition, Indian politicians often use the law as a shield for those accused or found guilty of corruption, rather than as a weapon against them. In July 2013, the Supreme Court ruled that any person convicted of crimes with punishment of two years or more was not eligible to be a member of the Union Parliament or any state legislature. However, the national cabinet overruled this with an ordinance. [126]

There was much resistance to this move, both from within the Congress party and from ordinary citizens. The Vice-President of Congress, Rahul Gandhi (who is not a member of the Cabinet), said the ordinance was "nonsense" and called for it to be scrapped. [127] The *Times of India* also began a campaign against the ordinance, and the newspaper reported that within less than a week its campaign had received the support of more than 700,000 people. [128] Bowing to this pressure, the Cabinet withdrew the ordinance in October 2013. [129]

THE ANTI-CORRUPTION MOVEMENT IN INDIA

The government's failure to combat corruption has led to the emergence of a large citizen-driven anti-corruption movement, which has threatened the power of the ruling United Progressive Alliance (UPA). Anna Hazare, a social activist, kickstarted the anti-corruption movement in 2011 largely gathering support from the media and the frustrated urban middle classes.

This development reflects an increasingly active media and civil society within India, which has taken up and magnified public discontent. The anti-corruption movement and the resulting media coverage (along with widespread protests against abuses of the rights of women) have unsettled politicians and political parties at national and state levels.

In 2012, the anti-corruption movement split because of differences between Hazare and another leader of the movement, Arvind Kejriwal. The latter wanted to politicise the movement, while Hazare wanted to keep it outside of formal politics. Subsequently, Kejriwal formed the Aam Aadmi Party (Common Man's Party) in November 2012. The party's main platform is the fight against corruption, but it claims that its tenets come from *swaraj*, or self-rule through clean governance, a concept popularised by Mahatma Gandhi. The party stood in elections in Delhi, to choose law-makers for the state's assembly in December 2013. Its performance surpassed expectations, securing 28 of the 70 seats in the state's legislative assembly, and winning 30 percent of the votes in the state - more than Congress which secured 25 percent of the vote. Though the BJP emerged with the largest vote-share of 33 percent, the AAP subsequently became the state's governing party, with support from Congress. [130]

As part of its commitment to fight corruption, the AAP introduced an anti-corruption hotline in Delhi in January 2014. The line received more than 4,000 calls within a few hours of being launched. According to Kejriwal, who was briefly the state's Chief Minister, more than 50 of these reported cases of corruption will lead to sting operations. [131]

In addition, there have been a number of citizen initiatives to combat corruption. For example, the website I Paid a Bribe was started in August 2010, by three Indian activists. The site allows people to anonymously report bribes paid and requests for bribes and has gained international prominence as a model initiative. In 2014, the website had received more than 24,000 reports of people paying bribes in India in the previous four years, worth almost US$10 million. [132]

The zero-rupee note is a further innovative way in which Indians fight corruption. The idea is the brainchild of an expatriate Indian academic, Satindar Mohan Bhagat. On a trip back to India from the United States, he was continuously asked for bribes for free services. The zero-rupee notes he created could be given to officials as a way of saying no, and of shaming those who attempt to extort bribes. Fifth Pillar, an anti-corruption NGO, took up the idea and began by distributing 25,000 zero-rupee notes in Chennai in 2007. [133]

DEMOCRACY AND CORRUPTION

Although corruption is endemic in India, democracy has empowered civil society and started to pressurise politicians. A number of scandals would not have been exposed without the country's investigative media. India's political institutions—such as Parliament and the courts—can and have played an important role in making sure legislation exists to combat corruption. The Lokpal Act and the Right to Information Act are prime examples of this. Free speech and political protest have been critical for the fight against corruption. The successes of Anna Hazare's movement and the AAP have given Indians a method of reducing corruption that would not exist without strong democratic institutions. The emergence of the AAP and its phenomenal electoral success could lead to some real change with respect to corruption.

Concluding Remarks

India became an independent democracy in 1947, but it took decades to unleash its economic potential. After the 1991 economic reforms, the private sector became the engine of an expanding economy. Entrepreneurship and creativity began to play a central role in economic affairs, and the country joined in, and benefitted from, a globalised world.

As a result, India experienced phenomenal growth during the course of the 2000s, while poverty levels fell. Although democratic pressures and conflicts of interest have sometimes delayed reforms that might lead to faster growth, India's democratic leaders did implement critical reforms when they were truly needed. With some exceptions, there is now an understanding among politicians that no party can satisfy its supporters unless the economy is growing.

For the past 23 years Indians have enjoyed the benefits of growth within a democracy (regular elections, freedom of expression, civil rights, and at least elements of the rule of law) while also moving up the development ladder. And, as India develops, incomes rise, the middle class grows, and the extent of political engagement amongst the electorate intensifies. Democracy does not automatically generate inclusive growth, nor does growth necessarily strengthen democracy. What the Indian experience demonstrates, however, is that under the right circumstances democracy and development can become mutually re-enforcing processes.

The middle classes' rising engagement in public life and politics is exemplified in the 2011 anti-corruption efforts. Increasingly, voters demand "law and order and crime-free streets; they want rule of law, and accountability from politicians, bureaucrats, and policemen; they want the corrupt to be punished; they want well-functioning public services; they want high-quality education". [134] In the future, it may be that the party that can best address middle-class concerns will win elections. Politicians who can put together a pro-growth or pro-reform coalition may be poised for national success. As we have seen, this has already happened in some states.

Governments in India, like in Brazil and South Africa, have been particularly adept at pushing through meaningful reform programmes in the face of an economic crisis. As India faces a future of 3 to 6 percent growth, with rising unemployment, as well as inflationary pressures and high government deficits, the pressure for a new round of reforms will grow. This should be seen as an opportunity for Indian politicians to restart the stalled momentum of reforms. They should seek to increase the competitiveness and dynamism of the Indian economy by further reducing restrictions on foreign investors, reducing fiscal deficits by developing a new affordable approach to welfare, deregulating labour markets and creating a much better business environment by drastically reducing red tape, and providing more support for entrepreneurial ventures. These reforms are not only necessary in themselves to help economic growth to move back to higher levels, but they will reduce the many opportunities for officials to be obstructive to development and ask for bribes. Without this reform, kickbacks on government contracts, as well as the quid pro quo in party contributions will continue.

The best way for India to sustain its pursuit of inclusive growth is to strengthen—not weaken—democracy. More accountable and more transparent forms of government will make it more difficult for corrupt politicians to keep their jobs. Such governments will be encouraged to deliver better services, in a cost-effective manner, without pursuing unsustainable forms of redistribution, but rather seeking to create as many economic opportunities as possible, through which the poor will be able to rise permanently out of poverty.

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