The State, Capital and Development in 'Emerging' India

Mazumdar, Surajit

September 2012

DRAFT

The State, Capital and Development in 'Emerging' India

Paper presented at the workshop on 'From Asia-Pacific to Indo-Pacific: Rising Powers, Emerging Regions and Transformations in Governance', Indo-Pacific Governance Research Centre, University of Adelaide, Australia, 21st September 2012

Surajit Mazumdar
Ambedkar University, Delhi

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

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

The totality of India’s liberalization story – encompassing its origins and sustenance as well as its consequences – has an enigmatic character to it. Some parts of that story can easily be causally related to others but these explanatory factors themselves often elude simple explanations. How did a country which was amongst the poorest in the world and had one of the less remarkable industrialization experiences of the second half of the twentieth century make the transition to greater integration with the global economy and make it ‘successfully’? Why has this ‘emergence’ expressed itself mainly in terms of aggregate economic performance and the positive fortunes of Indian business firms but bypassed the vast majority? How has this increasing divergence between economic growth and development been consistent with the maintenance of India’s democratic political system? How long can this kind of a trajectory with two rather different sides to it sustain itself both economically as well as politically? This paper does not provide the comprehensive analysis of the Indian experience of the last two decades that must be the basis for answering such questions. It does, however, highlight some of the important economic forces that have been at work within and outside the purely economic sphere in shaping the multi-faceted story of India's 'emergence'.

The paper argues that the developmental 'failure' of the Indian state in the last two decades has been endogenously determined – it is a joint-product of that very same liberalization which created the conditions for the specific kind of rapid expansion witnessed. The state has been central to the 'success' achieved by private capital but only by rendering itself less capable of responding to the requirements of the more fundamental transformation of the conditions of the majority of India's citizens. In the absence of such a transformation, there are questions about the sustainability of the expansion process. There are economic as well as political barriers which have expressed themselves in some manner or the other from time to time. If the former has not so far seriously compromised the aggregative expansion it is only because of the rather distinctive pattern of Indian growth. The dissatisfaction that does exist to the course taken by the Indian state, on the other hand, has not been able to so far crystallize into a political resistance of the proportions necessary to compel any change. Such crystallization in fact is a less spontaneous product of the context which is impelling the state to move in a particular direction. Its emergence is not guaranteed simply by the existence of a political structure where governments have to be elected. When and to what extent India's current economic trajectory will confront its political limits is therefore harder to predict.

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

Indian Liberalization and its Puzzles

Marking the transition to a new stage in India's economic history was the shift in state economic policy initiated in 1991. The strategy of relatively autonomous development with the state playing a leading role as producer and regulator, which was adopted after independence and remained broadly in place for over four decades, was decisively abandoned. Increased integration with the global economy, greater dependence on the spontaneous tendencies of the market system and the primacy of private capital were the defining features of the new strategy. Some liberalization measures had of course been introduced earlier, in the 1980s. To that extent there was an element of continuity between that decade and the period after 1991. Yet the 1980s liberalization did not represent that fundamental a departure from the past strategy of capitalist development. It was accompanied by a fairly rapid expansion of public expenditure and its external sector liberalization process was mainly concentrated on facilitating capital goods imports to produce manufactured products for a protected domestic market. Thus, while the 1980s may have reflected as well as reinforced a process of the changing mindset of policymakers, the decisive break with the past was only made in the subsequent decade.

The immediate trigger to the 1991 liberalization episode was a foreign exchange crisis which forced India to turn to the IMF for assistance. This was not however the first such crisis, and nor was it the first one where external pressure was brought to bear on the Indian State to influence its economic policies. But the response of the State in 1991 was unlike that in any previous case, initiating a long-term policy shift that continued even after the immediate crisis had passed. A similar episode of liberalization in the mid-1960s had been followed by a quick and rapid retreat into one of the most restrictive phases of trade and foreign investment policy and a wave of nationalization. In the 1980s too, the Indian state took advantage of a recovery of the foreign exchange situation and managed to eventually implement an economic policy package which fell far short of the terms attached to the 1981 IMF loan (Ghosh 1999). The changes after 1991 have, however, proved to be durable. Economic policy since then has moved essentially only in one direction, even long after the immediate crisis passed. More deep-seated and long-term changes in the Indian context, and not just a temporary crisis, must therefore explain it.

The advent of the liberal economic policy regime in India was also not preceded by any dramatic political change to which the shift could be linked. The announcement of the move of course came soon after a new government was formed after the 1991 general elections. The elections, however, brought back to power after a brief interlude of just two years the political party which had dominated Indian politics since the country’s independence. Thus the very same Indian National Congress which had been at the helm of affairs when India’s post-independence dirigiste strategy was put in place also led the initial march towards liberalization some four decades later.

Notwithstanding the fact that the 1991 elections ended what was till then only the second spell of India having a non-Congress Government, the Indian political landscape that formed its backdrop can hardly be described as unchanging. Already visible were many of the overlapping or mutually related trends that have contributed to making the present and the past of Indian politics appear so different. These include the shrinking of the Congress’ stable support base, the rise of right-wing Hindu nationalism, the increasing prominence of regional political forces and the emergence of new political formations built around core support bases in traditionally oppressed social groups (castes). Indeed, it was not the wave of economic liberalization that was to follow virtually immediately after that occupied centre-stage in the 1991 elections. Instead, implementation of the recommendations of the Mandal Commission (caste-based reservation or affirmative action) by the previous government and the Ram Janambhoomi-Babri Masjid (Temple vs. Mosque) dispute, and then the assassination of the former Prime Minister mid-way through the elections, dominated the election related discourse.

Even if at a fundamental level the underlying forces behind the changes in Indian politics and those in the realm of economic policy are the same, no obvious connection can be seen between the two. Instead, one has to confront the intriguing fact that the progress of Indian liberalization has remained largely immune to the many changes in government witnessed over the last two decades and the changing balance between contending political forces and realignments of political alliances associated with these governmental changes. An individual policy here and there may have faced problems but parties across the Indian political spectrum, with the exception of the Indian Left, have exhibit no tendency to fundamentally challenge the liberalization paradigm.

It would be, however, very difficult to argue that the effective near unanimity across Indian political parties on liberalization is a reflection of the emergence of a new social consensus displacing the one that had existed earlier. India's post-independence development strategy had been shaped in the background of her national movement. The struggle to end colonial rule had served to politicise a range of social classes which had potentially conflicting interests and one of its important outcomes was the creation of a formal political structure based on universal suffrage. A consensus on the necessity of maintaining a relative autonomy from the international economy and the importance of the role of the state had evolved alongside, even if there were differences when it came to the details (Patnaik 1999). Even the rising class of

Indian businessmen had played an active part in the formation of this consensus view as they saw these as critical requirements for accelerating India's industrial development (Tripathi 1991, Ray 1985, Srinivasan 2002). No comparable political process lay behind the paradigm shift in 1991. A range of discontents did exist in Indian society with the results of the earlier strategy but there was no coalescing of these into a shared interest in liberalization. The changeover instead was as sudden as it was far reaching. It was a top-down process with actors within the Indian policy making elite and in international financial institutions initially crafting the policy shift (Sengupta 2008).

If there were any segments of Indian society which came to actively endorse liberalization once it had been initiated, it was Indian business and some part of the middle class. This should be considered important in explaining the durability of the liberalization process given that the social influence of these two groups far exceeds their numerical proportion in Indian society. Of these, the change in the attitude of Indian business towards the question of integration with the global economy, from what it had been at independence, is a little harder to explain. Whatever initial misgivings some of them may have had at the beginning, Indian big business came to eventually actively push the 'reform' agenda (Pedersen 2007, Kohli 2009b). The constituents of Indian big business at the time of liberalization were not identical with those who had been dominant at independence. They were, however, not entirely different either. A mix of old business groups that had successfully survived and newer ones who had risen to prominence later made up Indian big business at the time liberalization began (Mazumdar 2011). All of them, the new and the old, had grown in a sheltered environment provided by protectionism and built businesses that were mainly 'national' – investing, producing, selling and raising finances mainly within that domain. They had great experience in manoeuvring within and through the system of controls associated with Indian dirigisme but had developed little capacity for self-development of technology (Alam 1985, Tyabji 2000). Why they should have welcomed a greater exposure to global competition is therefore not self-evident. Nor is it quite so simple to explain the great success that corporate India has experienced over the last two decades, which of course has contributed to reinforcing their endorsement of liberalization. Instead of being swamped by global competition, Indian business has grown in this period more rapidly than in the past and acquired a more international character.

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

It bears keeping in mind also that despite a near tripling of her per capita income levels over the last two decades, India on this count still is way behind even many developing countries. This acquires added significance in view of the very exclusive nature of the rising trend in income, which has virtually completely bypassed the overwhelming majority of India’s populace (Sengupta, Kannan and Raveendran, 2008, Vakulabharanam 2010) such that even food consumption levels have fallen for large segments of the population from the already low levels of the pre-liberalization days. Sharply rising inequality, and that too one accompanied by stagnation of their incomes, has meant that this majority has had no basis for actively supporting liberalization. Widespread discontent amongst them has instead existed and found expression in increased political instability. This has, however, failed to shift the centre of gravity of economic policy making and to that extent the democratic political system has not proved to be a check on a highly inegalitarian growth process. In the background of the disaster of the ‘India Shining’ campaign in 2004[1], the relatively favourable revenue situation created by very high growth, and a government dependent on the support of the Left, India’s poor did receive some limited attention compared to the complete neglect of the previous decade and a half. Measures like the National Rural Employment Guarantee Scheme (NREGA) were introduced during this period but within the framework of the existing policy paradigm. Even such modest efforts at redressing the worst effects of India’s growth trajectory, however, have run into difficulties as the fiscal situation has deteriorated after the global crisis.

[1] This was an advertising campaign run by then incumbent BJP-led National Democratic Alliance Government in the run up to the general elections. It backfired because it projected an image of India that was in sharp contrast to the lived reality of a large number of Indians.

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

The formal governing structure of the Indian republic was put in place soon after the country's independence from British rule. Its key elements were a federal system of government with cabinets and elected legislatures at the central and state level, with a division of powers between them. This was followed by the linguistic reorganization of states. The constitutional framework of Government that came into being had its antecedents in the 'constitutional reforms' brought about by the erstwhile British rulers. The constitution of independent India however severed the direct political ties with Britain, and eliminated the many special powers that had been exercised by the non-elected bureaucracy. It extended the electorate to include the entire adult population, and replaced the system of representation by 'classes and interests' with one of territorial representation. The administrative apparatus of Government, the police force and the army of independent India were inherited from British rule as they were (Bettelheim 1977).

The strategy of 'planned economic development' was also put into practice from the 1950s. State economic policy was to be subsequently marked by periodic changes as a result of frequent adjustments in response to, or forced by, contingent circumstances. The heydays of planning were consequently effectively restricted to the decade of the Second and Third Five-year plans. Through all those changes, however, the two core elements of the strategy were maintained. The state remained interventionist in nature and the formal structure of planning often continued to be the mechanism of that intervention. At the same time relative autonomy was maintained through controls on flows of capital, goods and technologies though they were never completely stopped.

The record of the pre-liberalization strategy in promoting Indian industrialization and development was certainly not spectacular. The pace of industrial growth was greater than in the colonial era (Sivasubramonian 2000) and in itself a fairly large and diversified industrial sector came into being. However, industrial growth was unstable and the increases in per capita levels of industrial production and the industrial sector's share in aggregate output remained within limits. Industrial expansion was mainly domestic market based - manufactured exports remained very limited and were also dominated by low-tech labour-intensive products. Structural changes in employment lagged even further behind that in output. The major part of the workforce remained in agriculture and formal employment expanded to cover barely ten per cent of the workforce. This formal employment expanded more in the public than in the private sector and this formed the core basis for an expansion of the middle class. State intervention in agriculture also benefitted a stratum within the agricultural population including the upper segments of the peasantry. Yet widespread poverty remained prevalent. All in all, the larger transformative impact of India's industrialization was of a much lower order than those that occurred in some other Asian developing countries over the same time.

What however tends to get somewhat obscured in the larger story of Indian development, particularly because it expressed itself more clearly only later, is the following. Import-substituting industrialization did provide a background for a significant development of Indian big business whose original background was in mercantile activities (Mazumdar 2008a). The transformation of Indian capital from where it had been at independence went much further than the overall progress of Indian industrialization might suggest. Private corporate capital's relative share in the economy did not increase significantly except in the initial years of the period. It also became more confined to manufacturing activities as it was squeezed out by the public sector from other spheres like banking and finance, mining, transport and communication, electricity, etc. As the manufacturing sector became more diversified, however, Indian business groups moved from a situation of being confined to a few traditional industries like the textiles into others such as steel and steel products, chemicals, cement, automobiles and automobile products, industrial and other machinery and consumer electronics. This expansion in newer and more 'modern' industries increased the level of technological sophistication that Indian big business firms dealt with. They learnt to find, absorb, adapt, and profitably use technologies and technological advances across the industrial spectrum even if they themselves did not develop them. In other words Indian private capital did experience a process of 'learning-by-doing', and one that had a somewhat unique character given the constraints within which it happened.

Compared to the position existing at independence, this learning did not eliminate but closed the gap between Indian business firms and the top rung of firms internationally. This was to prove to be important for facing the challenges that liberalization was to throw up – it made Indian business firms capable of facing global competition particularly in the environment with which they had a special familiarity, namely the Indian domestic market and economic space. If this made them more willing to accept such competition, the continuing weakness on the technological front also pushed them in the same direction (Mazumdar 2008a). As the scope for industrial growth through diversification and a successive diffusion of industries exhausted its own scope, the technological requirements of capitalist expansion changed. Opening up was necessary for Indian capital to get the kind of access to technology its new stage of development required, and facing the competition this would expose them to in turn required an unshackling of the controls they had been subjected too. Thus the conditions for the eventual switchover of Indian capital to the endorsement of liberalization were created through the process of import-substituting industrialization.

In shaping the story of Indian industrialization and development before liberalization, both what the state did as well as its failures were important. In explaining the relatively limited overall success of Indian dirigisme, two major failures of the Indian state stand out. Both reflected the limits to its ability to impose itself on powerful economic interests. The first of these was the limited success achieved in carrying out the agrarian reform programme after independence (Joshi 1975) to eliminate what was called the ‘built-in-depressor’ (Thorner 1956). If dominant landed interests thwarted the institutional change in agriculture that was necessary for an accelerated process of industrialization, Indian big business managed to also escape disciplining by the state (Chibber 2004). What has been pejoratively called the “license-permit raj” was in reality the routine abuse, manipulation, and circumvention of the system of controls to their advantage by big business firms with the assistance of the discretionary decision-makers in the state apparatus. This became thus an entrenched part of business behaviour and the clientelism, corruption and cronyism associated with it became more pronounced with time (Goyal 1979, Kochanek 1987, Virmani 2004). Private capital also successfully beat the revenue mobilization effort thereby limiting the state’s ability to expand public expenditures. As a result of these, the extent and the effectiveness of the state support to industrialization and social development were undermined and were later to be used to make the case for the withdrawal of the state.

It would, however, be a bit of a caricature to represent the Indian state before liberalization as being entirely captive to powerful private interests. Indeed it was not even the case that a fixed and exclusive set of favoured business firms remained the beneficiaries of state patronage throughout. This is what created the possibility for new constituents in India’s business elite to emerge. The state's general promotional role in enabling the industrialization process, which expressed itself through a rising share of the public sector in total output, was also critical. This provided the backdrop for diverse firm histories - of decline, survival and of rise. The development of the financial system to support private capitalist accumulation and the backward and forward linkages of public investment for instance were extremely important. Notwithstanding the shortcomings of Indian land reforms, the extensive involvement of the state in other ways in the agrarian economy was also crucial (Patnaik 1994, Rao 1994). Even if success on the agrarian front was not spectacular, it was critical.

The overarching setting of an interventionist economic policy regime also provided a context for significant autonomous state action. For instance, the period of the most intense economic difficulties, from the mid-1960s to the late 1970s, also saw the high tide of nationalization and government takeovers of many stricken private sector companies. While it may not be correct to suggest that these were exclusively responsible, the political pressures emanating from the aspirations of diverse segments of Indian society did influence the nature of these measures. In addition, while resource constraints may have limited their actual magnitude – the idea that the state had to deliver a range of benefits to all citizens, pejoratively described by some as 'economic populism', was part of the dominant political discourse. At the same time, the milieu made for institutions like the judiciary and some public agencies to develop a particular instinctive attitude that at least partly ameliorated inherent iniquities, including in the area of labour regulation.

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

Growth and Divergence after Liberalization

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

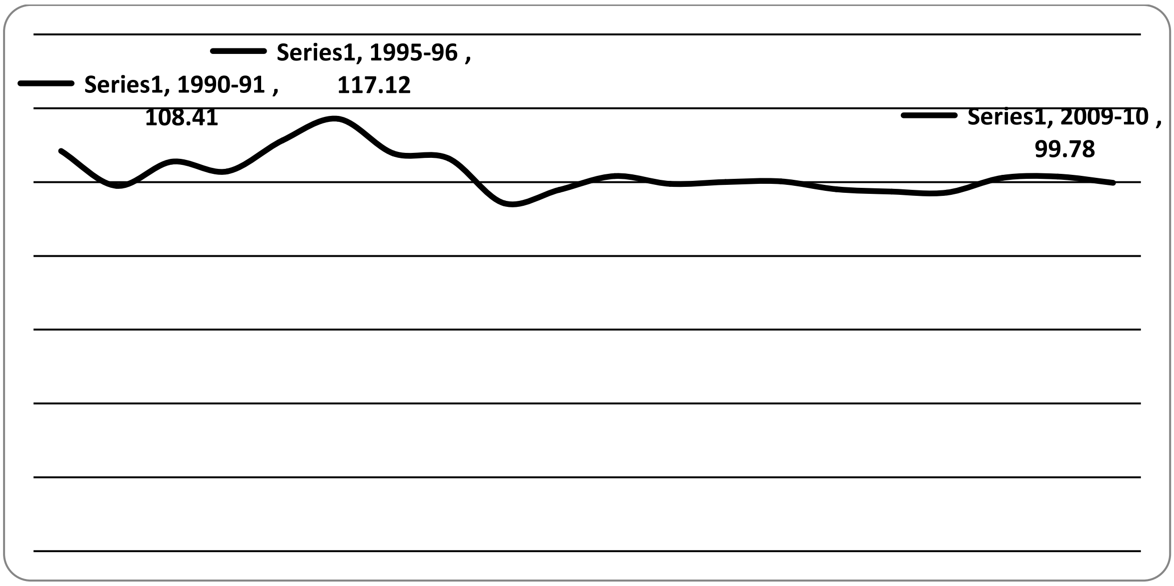
The other side of the story of Indian growth relates to the sector which has been and still remains the principal sector of employment[2], namely the agricultural sector. Here, the withdrawal of the state and other measures associated with liberal economic policies gave rise to a deep-rooted agrarian crisis since the 1990s (Patnaik 2003, 2007, Reddy and Mishra 2008). Over 200,000 suicides by farmers since then was only one symptom. Some pockets of dynamism apart, the agrarian crisis has had a generally adverse effect on livelihoods. Distress driven exit from the sector on the other hand could not be absorbed by the rapidly growing private corporate sector with the result that non-agricultural informal employment has swelled. Moreover, this has happened in a situation where the agrarian situation has held down the reservation wage in non-agricultural activities.

The wage-depressing tendencies in India have been so strong that real wages have been flat or creeping downwards even in the private formal sector despite the sector's rapid growth (Figure 1). In the industrial sector, this has been aided and enabled by the increasing informalization of formal sector employment and the attitudinal changes liberalization has brought to the working of public agencies and the judiciary (Bhattacharya 2007, Papola and Sharma 2004, Roy Chowdhury 2005). Thus, despite the legal framework of labour regulation having remained relatively unchanged there has been a movement towards increasingly flexible labour markets, erosion of collective bargaining and the greater role of capital in setting the terms of work. These have created the conditions for wages in the formal sector to reflect more clearly the general labour-market situation making their trend an indicator of what has happened to income-levels of large segments of India's population in the last two decades. Given that India is still an extremely poor country, the trend of income stagnation and depression over large

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

segments of its population is a particularly striking phenomenon. That food consumption trends also reflect these is testimony to the grim situation.

Figure 1: Index of Real-Wage per Worker in India’s Organized Industrial Sector (2002-03=100)



Source: Central Statistical Organization (CSO), Annual Survey of Industries and Government of India, Ministry of Finance, Economic Survey

Thus the effect of Indian liberalization has been to impart to the economy a structural feature whereby the overwhelming part of the workforce is caught in a permanent low-wage or low-income trap. With public expenditure also being constrained by the logic of liberalization, these conditions cannot be easily changed either.

The low levels of wages have also served to provide enabling conditions for a very different trend in the salaries of white collar employees in the private corporate sector with higher levels of education. For one, combining with the limited growth of employment they have ensured that these high salaries of a section of employees does not overinflate the wage and salary bills of corporate firms. Indeed, the distribution of income within the private formal sector during this period has shifted decisively in favour of surplus incomes (Table 1). Even as the share of the corporate sector in total national income has grown sharply, that of one of its components, namely compensation of employees, has actually declined. Low wages have also effectively raised the real incomes of those with higher salaries because they result in the cheap availability of a range of labour-intensive services. Insofar as many of these are non-tradable services they have also contributed to keeping the exchange rate lower than what purchasing power parity would dictate. All of these in turn have meant that the cost of production of labour-intensive tradable services also tends to be low in India, even when they involve large high salary employment as in India's software sector.

Table 1: Shares of the Private Organized Sector Output and its Components in India's Aggregate Net Domestic Product (NDP) (Percentages)

Component	1999-00 Base Year Series					
	1990-91	**1996-97**	**2002-03**	**2003-04**	**2004-05**	**2007-08**
Compensation of Employees	7.72	6.01	6.61	6.69	6.46	6.82
Operating Surplus	6.35	11.44	11.96	12.56	14.08	16.62
Total Private Organized NDP	**14.07**	**17.45**	**18.56**	**19.26**	**20.54**	**23.44**
	2004-05 Base Year Series					
	2004-05	**2005-06**	**2006-07**	**2007-08**	**2008-09**	**2009-10**
Compensation of Employees	6.35	6.48	5.93	5.80	5.70	5.55
Operating Surplus	13.21	15.55	17.24	17.85	17.27	16.78
Total Private Organized NDP	**19.55**	**22.04**	**23.16**	**23.65**	**22.97**	**22.32**

Source: Central Statistical Organization, National Accounts Statistics

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

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

Even with low wages, Indian manufacturing has not found too many niches in the internationalized system of production characteristic of the globalization era where it is competitive. Lack of public investment in health, education and infrastructure has been the problem here, contributing to keeping productivity low relative to other competing nations. On the other hand, wages are already very low and account for a very small proportion of industrial costs[3]. The scope for gaining competitiveness by wage depression therefore practically does not exist. Thus, even while manufactured exports have grown and there has been some change in their composition, manufactured imports have tended to grow even faster. India’s trade deficit has consequently become very large, with oil and gold imports adding their bit too. Indian industry therefore continues to be mainly domestic market oriented and India has not been a major recipient of the world market oriented ‘efficiency-seeking’ FDI. India’s greatest export success after liberalization has been in services and that too in a very specific category of

[3] The share of wages in the value added of India’s formal industrial sector is barely 10 per cent and as a proportion of the value of output they are under two per cent.

information technology (IT) and IT-enabled services[4]. A significant surplus in services trade has been complemented by large inflows of remittances to partly compensate for the expanding trade deficit.

Not surprisingly, Indian growth since liberalization has been driven more than ever before by expansion of tradable and non-tradable services and construction activities rather than by that of tradable manufactured products. In the absence of significant domestic and external market growth, industrial growth in India has become excessively dependent on demand generated by investment. This, under liberalization conditions has meant private corporate investment, which has a strong tendency to be concentrated in manufacturing. This, however, has made for great instability in that investment and also industrial growth (Mazumdar 2008b). This has completely stalled India's industrialization process and the share of industry in total output has stagnated since the mid-1990s at levels far below those historically achieved by successful early or late industrializers (Mazumdar 2010). It is only the steady growth of services and their rising weight in total output that has prevented aggregate growth trends from fully reflecting the instability that has afflicted both agricultural as well as industrial growth.

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

---

[4] Apart from India's low-wage economy, underlying the export success in IT has been has been the long-standing existence of an English-language based tertiary education sector, a legacy of both her colonial and dirigiste pasts.

activity. In a sense, therefore, the corporate sector in India has grown by *de-industrializing* itself (Table 2).

Table 2: Share of Private Organized NDP from different sectors in India's NDP

Sector	1990-91	1996-97	2002-03	2007-08
1999-00 Base Year Series				
Agriculture	2.21	2.18	1.39	1.21
Industry excl. Construction	***6.44***	***8.03***	***6.83***	***7.39***
Services and Construction	***5.62***	***7.33***	***10.35***	***14.84***
Total Private Organized	14.26	17.55	18.56	23.44
2004-05 Base Year Series				
	2004-05	**2007-08**	**2008-09**	**2009-10**
Agriculture	0.56	0.46	0.46	0.44
Industry excl. Construction	***6.10***	***6.97***	***6.90***	***6.52***
Services and Construction	***12.90***	***16.22***	***15.61***	***15.36***
Total Private Organized	19.55	23.65	22.97	22.32

Source: CSO, National Accounts Statistics

Indian business groups have clearly been the principal beneficiaries of rapid corporate growth. Capital inflows into India did of course increase significantly after 1991. These have been, however, dominated by portfolio flows with even a significant component of direct investment being of a similar 'financial' nature (Chalapati Rao and Dhar 2011). Such flows, and the openness of the economy to them, have increased the range of financing options available to Indian firms rather than being competitive in nature. Foreign investment by Indian firms has also been facilitated by these inflows supplying the necessary foreign exchange. While the presence in India of foreign firms through foreign direct investment has become more pronounced after liberalization, it remains narrow in spread.

Indian big business thus has been able to find ample space for its own growth and development in the process of India's integration into the global economy. Partly this reflects the strengths it had acquired in the earlier stage of industrialization. There is, however, little evidence to suggest that barring the pharmaceutical industry, there has been any significant increase in the innovative capacity of the Indian private sector (Mani 2009). Even in pharmaceuticals, Indian firms lack drug development capabilities (Chaudhuri 2008, Jha 2007). In the other highly internationalized sector, software, innovative activity in India has been mainly by foreign R & D units (Mani 2009) and Indian firms have found their niche in a relatively subordinate position to the internationally dominant firms in the sector (D'Costa 2004). In other words, Indian firms still rely primarily on their experience in sourcing and using technology rather than making it. This probably explains their relatively minor presence in sectors where proprietary technology is a critical element in competitive strength (like automobiles). The pattern of Indian growth has therefore been to their advantage. In a number of services and construction activities, the role of self-development of technology in any case tends to be limited, but other assets like familiarity with local conditions and networks are critical because of their non-tradability. Even the pattern of internationalization of Indian firms, dominated as it has been by acquisitions, has been explained as being more a process of acquiring competitive strengths like innovative capacity rather than their result (Nayyar 2008). There is, however, an additional element in the success of Indian big business – the support of the state.

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

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

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

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

One side of the state-capital relationship under liberalization has been its role in facilitating the success of *Indian* capital in the face of global competition. The gradual and calibrated nature of Indian liberalization has contributed to this and facilitated the adaptation and adjustment of Indian big business to the new competitive context. It has also helped them set themselves up in many of the new sectors opened up for private capital in which they had no previous experience. The state also took countervailing measures when there was any significant threat to Indian business from foreign capital[5]. More explicit state support has helped sectors like the export-oriented IT sector break into and maintain their position in global markets[6] (D'Costa 2009).

Individually as well as collectively, Indian private capitalist firms have therefore not scripted their success in the last two decades without the generous helping hand of the state. The stranglehold of capital over the state has, however, meant tilting it against the interests of other segments of Indian society who have found it far more difficult to claim the state's attention. Under the mutually reinforcing pressures of globalization, fiscal constraints and the growing clout of Indian big business, the capacity of the state to respond to the conditions of these sections except through the further promotion of private capital has been considerably circumscribed. Every phase of upturn in the aggregative economic performance generates a reluctance to do anything that might adversely affect the 'animal spirits' and the 'state of confidence' of the private investor. Every downturn generates a tendency for measures to revive these. This state of effective blindness of the state, reflected by political parties to an even greater extent when in government, has also been reinforced by the middle class endorsement of liberalization. The middle class is of course automatically a social group with a naturally strong presence in the administration, the media as well as in academia. The Indian middle class under current conditions is also becoming more exclusive since it is largely

[5] One prominent example of this is the creation and then the subsequent virtual killing of the 'market for corporate control'. This was achieved by the easing of restrictions on inter-corporate investments in response to lobbying by Indian business groups so that these groups could increase their stakes in companies controlled by them.

[6] Apart from the state sponsoring the development of software technology parks from 1991, the software sector has also been the greatest beneficiary of fiscal incentives like an extended tax holiday. The state has also politically supported the sector's efforts to gain and maintain international market access, including in the recurrent controversy over outsourcing. The critical need of the IT sector of a skilled workforce has been met to a great extent by public tertiary education institutions, many of them a legacy of the past.

reproducing itself rather than being expanded by increased penetration by upwardly mobile sections of other social groups.

Thus, the trajectory that the Indian economy has traversed over the last two decades has carried within it an underlying basis for not only the increasing divergence witnessed but also its persistence working through the erosion of the state's capacity to respond to it. The following statement made nearly a decade and a half ago was perhaps made by observing the early signs of this tendency.

> "It is, then, plausible to suggest that this latest phase of independent India is characterized by an intensification of conflict in the economy, in the polity, and in the interaction between economy and polity. There can be no doubt that the need for conflict resolution is much greater than ever before. But the task has become more difficult. And the effort is much less." (Nayyar 1998: 3129)

Conclusion

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

References

Alam, Ghayur (1985), 'India's Technology Policy and Its Influence on Technology Imports and Technology Development', *Economic and Political Weekly* 20 (45-47): 2073-80.

Amsden, Alice H. (2001). The Rise of "The Rest": Challenges to the West from Late-Industrializing Economies, New York: Oxford University Press.

Bettelheim, Charles (1977) *India Independent* (Translated from the French by W.A. Caswell), New Delhi: Khosla and Co.

Bhattacharya, Saumyajit (2007) 'The State and Labour Market Reforms: Vicissitudes of the Changing Relationship between State, Labour and Capital – An Appraisal of the Neo-Liberal Reforms in India', paper presented at the Global Labour University Conference, 1-3 April 2007, University of The Witwatersrand, Johannesburg.

Chalapati Rao, K S and Atulan Guha (2006), ‘Ownership Pattern of the Indian Corporate Sector: Implications for Corporate Governance’, Institute for Studies in Industrial Development Working Paper No: 2006/09.

Chalapati Rao, K S and Biswajit Dhar (2011), ‘India’s FDI Flows: Trends and Concepts’, New Delhi: Research and Information Systems on Developing Countries (RIS) and Institute for Studies in Industrial Development (ISID).

Chaudhuri, Sudip (2008) ‘Ranbaxy Sell-out: Reversal of Fortunes’, *Economic and Political Weekly* 43(29): 11-13.

Chibber, Vivek (2004) *Locked in Place: State Building and Late Industrialization in India*, New Delhi: Tulika Books.

D’Costa, Anthony P. (2004), ‘The Indian Software Industry in the Global Division of Labor,’ in D’Costa, A.P. and Sridharan,E. (eds.) *India in the Global Software Industry: Innovation, Firm Strategies and Development*, Houndmills, Basingtoke: Palgrave Macmillan, 1-26.

D’Costa, Anthony P. (2009) 'Economic Nationalism in Motion: Steel, Auto, and Software Industries in India', *Review of International Political Economy* 16 (4): 620-48.

Ghosh, Jayati (1999): “Liberalization Debates”, in Terence J. Byres (ed.) *The Indian Economy: Major Debates Since Independence*, New Delhi: Oxford University Press, 295-334.

Government of India (2007) National Commission for Enterprises in the Unorganized Sector (NCEUS): Report on Conditions of Work and Promotion of Livelihoods in the Unorganized Sector, New Delhi.

Goyal, S.K (1979) *Monopoly Capital and Public Policy*, New Delhi and other places: Allied Publishers Private Limited.

Jha, Ravinder (2007) ‘Options for Indian Pharmaceutical Industry in the Changing Environment’, *Economic and Political Weekly* 42(39): 3958-67

Joshi,P.C (1975), Land Reforms in India: Trends and Perspectives, Bombay, Allied Publication.

Kochanek, Stanley A. (1987): “Briefcase Politics in India: The Congress Party and the Business Elite” Asian Survey, 27 (12): 1278-1301.

Kohli, Atul (2009) 'Politics of Economic Growth in India, 1980-2005, Part II: The 1990s and Beyond' in Atul Kohli, *Democracy and Development in India, From Socialism to Pro-Business.* New Delhi: Oxford University Press, 164-185.

Mani, Sunil (2009) 'Is India Becoming More Innovative since 1991? Some Disquieting Features', *Economic and Political Weekly* 44(46): 41-51.

Mazumdar, Surajit (2008a) 'The Corporate Sector and Indian Industrialization: A Historical Perspective', in S. R. Hashim, K. S. Chalapati Rao, K. V. K. Ranganathan and M.R. Murthy (eds.), *Industrial Development and Globalisation* New Delhi: Academic Foundation: 193-236.

Mazumdar, Surajit (2008b) 'Investment and Growth in India under Liberalization: Asymmetries and Instabilities', *Economic and Political Weekly*, 43 (49): 68-77.

Mazumdar, Surajit (2010) 'Industry and Services in Growth and Structural Change in India', Working Paper No: 2010/02 New Delhi: Institute for Studies in industrial Development.

Mazumdar, Surajit (2011) The State, Industrialisation and Competition: A Reassessment of India's Leading Business Enterprises Under Dirigisme, *Economic History of Developing Regions*, 26 (2): 33-54

Nayyar, Deepak (1998) 'Economic Development and Political Democracy: Interaction of Economics and Politics in Independent India', *Economic and Political Weekly*, 33 (49): 3121-3131.

Nayyar, Deepak (2008) 'The Internationalization of Firms From India: Investment, Mergers and Acquisitions', *Oxford Development Studies* 36(1): 111 – 31.

Papola, T.S. and Alakh N. Sharma (2004) 'Labour: Down and Out?', *Seminar* 537, Special Issue on India Shining, May.

Patnaik, Prabhat (1999): "Some Indian Debates on Planning", in Terence J. Byres (ed.) *The Indian Economy: Major Debates Since Independence*, New Delhi: Oxford University Press, 159-192.

Patnaik, Utsa (1994), 'India's Agricultural Development in the Light of Historical Experience', in Terence J. Byres (ed.) *The State and Development Planning in India*, Delhi: Oxford University Press, 265-290.

Patnaik, Utsa (2003), "Food Stocks and Hunger: The Causes of Agrarian Distress", *Social Scientist*, 31 (7/8), 15-41

Patnaik, Utsa (2007), "Neoliberalism and Rural Poverty in India", *Economic and Political Weekly*, 42 (30), 3132-50

Pedersen, Jorgen Dige (2007) 'The transformation of Indian business: from passive resisters to active promoters of globalization', Paper prepared for Sixth Pan-European Conference on International Relations, University of Turin, Italy, 12 -15. September 2007.

Rao, J. Mohan (1994), 'Agricultural Development under State Planning', in Terence J. Byres (ed.) *The State and Development Planning in India*, Delhi: Oxford University Press, 220-264.

Ray, Rajat K. (1985) *Industrialisation in India, Growth and Conflict in the Private Corporate Sector: 1914-47*. Paperback Edition, 2nd Impression. Delhi: Oxford University Press.

Reddy, D. Narasimha and Srijit Mishra (2008) 'Crisis in Agriculture and Rural Distress in Post-Reform India', in R. Radhakrishna (ed) *India Development Report 2008*, New Delhi, Oxford University Press, 40-53.

Roy Chowdhury, Supriya (2005) 'Labour and Economic Reforms: Disjointed Critiques', in Jos Mooij (ed.) *Politics of Economic Reforms in India*, New Delhi, Sage, 264-290.

Sengupta, Arjun, K P Kannan , and G Raveendran (2008), 'India's Common People: Who Are They, How Many Are They and How Do They Live?', *Economic and Political Weekly*, 43 (11): 49-63.

Sengupta, Mitu (2008) 'How the State Changed Its Mind: Power, Politics and the Origins of India's Market Reforms', *Economic and Political Weekly*, 43 (21):35-42

Sivasubramonian, S. (2000) *The National Income of India in the Twentieth Century,* New Delhi: Oxford University Press

Srinivasan, T.N. (2002) "Foreign Trade Policies and India's Development", in Uma Kapila, (ed.) *Indian Economy Since Independence*, Fourteenth Edition, New Delhi: Academic Foundation, [Originally published as Chapter 5 in *Agriculture and Trade in India and China,* San Francisco: International Centre for Economic Growth, 1994].

Thorner, Daniel (1956), *The Agrarian Prospect in India*: Five Lectures on Land Reform delivered in 1955 at the Delhi School of Economics, Delhi: University Press.

Tripathi, Dwijendra (ed.) (1991) *Business and Politics in India, A Historical Perspective*, Delhi: Manohar Publications.

Tyabji, Nasir (2000) *Industrialisation and Innovation: The Indian Experience*, New Delhi: Sage Publications.

Vakulabharanam, Vamsi (2010), 'Does Class Matter? Class Structure and Worsening Inequality in India', *Economic and Political Weekly*, 45 (29), 67-76.

Virmani, Arvind (2004), "India's Economic Growth: From Socialist Rate of Growth to Bharatiya Rate of Growth", Working Paper No. 122, Indian Council for Research on International Economic Relations (ICRIER).