WP-2013-001

Sustaining growth: Interests versus institutions

Ashima Goyal

Indira Gandhi Institute of Development Research, Mumbai
January 2013
http://www.igidr.ac.in/pdf/publication/WP-2013-001.pdf

Sustaining growth: Interests versus institutions

Ashima Goyal
Indira Gandhi Institute of Development Research (IGIDR)
General Arun Kumar Vaidya Marg
Goregaon (E), Mumbai- 400065, INDIA
Email (corresponding author): ashima@igidr.ac.in

Abstract

Nations that were able to sustain high catch-up growth followed flexible and contextual policies. Inclusive institutions make correct policy choices more likely. India started out with highly inclusive political institutions since it adopted democracy with universal suffrage at independence. But extractive economic institutions, inherited from the British, were made more so by economic controls. In addition, a heterogeneous electorate allowed politicians to cultivate vote-banks and populist schemes instead of delivering better public services and governance. India's opening out was adequately nuanced and flexible but was sometimes used as a substitute for harder domestic reforms. It, however, added to the growing constituencies that benefit from growth, and are pushing for more inclusive economic institutions, that enable productivity, not just redistribution. Broader interest groups create better institutions and incentives. Examples from general governance, the regulation of industry, and agricultural marketing show the process, although messy and prolonged, is in the right direction.

Keywords: catch-up growth, institutions: political and economic, democracy, vote-banks, governance, active inclusion

JEL Code: O43, D78, F54

Acknowledgements:

Acknowledgement: This is a revised version of a paper presented at the 2012 CDS-NMML conference on 'The Indian Economy: a longer and broader view' in New Delhi. I thank my discussant, E. Shridharan, and other participants for very useful discussions.

Sustaining growth: Interests versus institutions

Introduction

The Indian growth slowdown, even after a smart recovery from the fallout of the global financial crisis (GFC), raises the question of what are Indian growth drivers and how growth can be sustained.

In the view that liberalizing reforms alone drive growth, external shocks and continuing restraints on markets are responsible for the 2012 slowdown. Extreme versions of this view regard domestic institutions as so dysfunctional only external forces can make a difference. But overdependence on external drivers also creates risk, and a large country like India cannot be driven only by external factors. Moreover, the Spence commission (2008) showed nations that successfully sustained high growth embraced openness but did not blindly apply market friendly reforms. Therefore India's nuanced reforms are not necessarily a drawback.

Acemoglu and Robinson (AR) (2011) argue that only countries with broadly inclusive political and economic institutions succeed in the long run. Without that they fail despite openness. In their view, Indian failures are due to the extractive institutions the British left it with. But the British also left India with legal and democratic institutions, and sixty years is long enough for institutions to change. Why should a broad inclusive democracy like India create dysfunctional economic institutions? The answer may lie in the contribution of ideas and of structure.

The dominant development ideas of the time favoured a closed economy with government led growth and re-distribution. Democracy was broad-based but politicians could exploit divisions of caste, religion and region to maintain a stagnant equilibrium that delivered neither growth nor equity. Economic controls gave additional power to elites to enrich themselves, with minimal doles to the groups that kept them in power. Continuing poverty created dependence through a need for further doles.

Institutions are congealed structure and ideas as well as interests[1]. Thus post-independence dominant development ideas imposed on inherited heterogeneous structure and colonial institutions created stagnancy. Institutions weakened by ideas and structure could be hijacked by interests. But a change in ideas and a rise in the proportion that benefit from growth are strengthening institutions. There is a steady deepening of horizontal democracy, but critical changes in the institutions of governance are slow. Even so, they are happening and are illustrated through Centre-State relations, contestations in the telecom story and in agricultural intervention. Since the process is messy and prolonged growth is volatile, but to the extent appropriate institutional change is occurring, growth could be more long-lasting.

The paper starts with the ideas that influenced India's development pattern, then goes on to an analysis of reform in the context of nations that succeeded, before analyzing institutions, their weakening and their subsequent strengthening in India. In the concluding section, insights from the analysis give pointers to the social inputs required.

Ideas

India may have become a closed economy for much of the post independence period, but it has always been open to global academic ideas. The government led big-push and control of the economic heights were the frontier development ideas at the time of independence. Rath (2012) argues that the focus on planning made the government persuade a constitutional body, charged with making grants-in-aid to bring States to a uniform level of public services, to cede grant making powers to the Planning Commission. But the latter made transfers according to the Plans, to build industry, not to provide public services to the people.

As the many failures of a government-led approach, in the socialist bloc and in other stagnating economies, became obvious, the weight of Indian policy opinion began to favour markets[2]. But the committee mode of functioning, and the repeated global financial crises, made the flaws of markets obvious so the reforms adopted were nuanced. So although the current Indian policy elite are largely those with a tendency to rely too much on free markets, richer domestic debate combined with current frontier thinking both give India a chance to

[1] The SIIO paradigm (Goyal 2011), which examines how 'structure and ideas become engraved in institutions that affect outcomes (pg. 1)', is a useful way to analyze this interaction. The domestic structure relevant to the analysis in this paper was the heterogeneous electorate.

[2] At 2011 Skoch function to felicitate his contributions to reforms Montek Singh Ahluwalia named his many superiors in government who supported reforms, and said that without that support he would not have dared to act.

design policies that bring out the best of both governments and markets while suiting conditions on the ground. A 'longer and broader[3]' view of the changes India is undergoing is part of this process.

For such a process it is necessary to move away both from an extreme rightist viewpoint for which all problems are due to not opening out and liberalizing enough, and from an extreme leftist viewpoint from which the opening out and the growing role of the private sector have increased inequality and stressed the social fabric. Liberalization was easier to do than improving domestic governance but foreign capital will not continue to finance an economy where the appropriate domestic infrastructure is not created. Neither the government nor the people can directly run the economy, so firms and markets must play a role, but with competition and appropriate regulation.

Why nations succeed

The Spence Commission (2008) examined 13 economies that, in the period after 1950, grew at above 7 percent for more than 25 years. Nine of these were from Asia. Their common characteristics included openness, macroeconomic stability, high savings and investment rates, and market allocation of resources. Governments were capable—pragmatic and flexible rather than ideological. While willing to intervene in markets to promote exports through industrial policies, and to manage exchange rates (with the use of selected capital controls and reserve accumulation) they were flexible enough not to get locked into distorting policies, to anticipate and change policies as required for growth. Resource mobility and urbanization was supported. Public investment in infrastructure accounted for 5 to 7 percent of GDP or more. Specific contextual interventions and the microeconomic incentives created were important. External drivers and opening out alone did not create growth.

World Bank studies based on the purchasing power parity (PPP) method characterize low income countries as those with a per capita Gross National Income (GNI) of less than USD 975 in PPP terms. In the lower middle-income group GNI lies between USD 976 and 3855, in the upper middle income group it is between 3856 and 11905. Above that are the high income groups. After crossing a minimum threshold, normally low income countries grow rapidly, provided they have the flexibilities mentioned above. China had its fastest rate of

[3] This phrase appears in the title of the conference for which this paper was first written.

growth after its (PPP) GDP per capita crossed $1747 in 1992. The experience of Japan and the US was similar. India crossed $ 1800 in 1999.

But once a country crosses into the upper-middle income group, a number of studies show, growth rates tend to decline by about two percent points. This threshold varies between USD 7000 and 17000. There is a 50 percent chance that a middle income country will stay in that group, caught in the 'middle income trap'. By 2015 China is expected to cross the USD 17000 mark[4]. Most analysts expect a slowdown in its rate of growth. East Asian high growth economies are also concerned about being caught in the middle income trap. The slowdown comes from a fall in productivity growth and is less in more open economies with higher consumption shares.

India and China, the countries currently growing at the highest rates, also followed pragmatic policies far from standard reform prescriptions. As China hits the middle income mark, India which is far below, should have many years of robust growth left. But compared to China's performance, India's catch-up growth has been volatile. Why?

Although it persisted in an increasingly inappropriate path for a long time, certain strengths were built up. For example, its skilled English educated labour allowed it to catch the outsourcing wave. The planning process did create a diverse economy—a major current strength that reforms enhanced. They added export demand to strong domestic demand, as manufacturing became globally competitive. The changes added up to a critical mass. Networks of markets and associations became dense, reducing transaction costs, as learning occurred and quality improved. It was no longer only the government undertaking initiatives for society. NGOs and corporates[5] became active as well. Other positive factors include the demographic profile and investment in infrastructure that has reached 7 percent of GDP.

The gradual growth oriented approach both countries followed did give useful degrees of flexibility to respond to outcomes—like the conscious Chinese strategy of 'crossing the river while feeling the stones'. The public sector could shrink as the private grew, thus avoiding the wrenching social tensions of the sudden Russian privatization. Both countries continued

[4] This literature is surveyed in Cai (2012). For a discussion of the minimum threshold see Goyal (2004, 2001).
[5] See Bhattacharya (2012) for dynamic CSR and business-model based private initiatives that are improving the delivery of essential services such as water and health, which the Government has failed to provide.

with capital account controls, but since China, had little domestic industry or trade unions, foreign direct investment (FDI) could drive its opening and focus on manufacturing exports. Since India had more private local industry, and rigid labour laws, some restrictions remained on FDI. The largest foreign inflows it attracted were portfolio flows (FPI) that contributed to the development and reform of capital markets. Liberalization favoured equity over debt flows—FPI may be volatile but it is at least risk sharing, so that outflows during adverse shocks are reduced.

But still openness, despite its contribution to diversification and catch-up, was also a source of shocks—the reform years saw major oil and food price shocks, the East Asian and global financial crisis. Volatile risk-on risk-off portfolio flows made financing the current account deficit difficult. Catch-up growth is normally faster than industrial country growth but it only defines a potential or trend growth rate. Savings generally rise with growth as firms get cash rich and tax revenues boom. China's savings rate reached the fifties. India's savings rate reached the thirties, and together with an incremental capital output ratio of four, and a sustainable current account deficit of 3 percent, peak savings define a potential growth rate of nine to ten percent[6]. Annual entrants to the labour force and the transition to higher productivity jobs provide required labour inputs. But countercyclical macroeconomic policy has to maintain the actual rate of growth in the face of shocks, even while reforms continue to sustain the potential rate. Policy failures on the supply-side and in smoothing shocks explain why growth fell below potential, and inflation rose, even after the threshold per capita level was crossed (Goyal and Arora, 2012).

Policy did not address structural features, such as short-term supply bottlenecks, and the necessity of improving agricultural productivity to reduce food inflation which raised wages and general inflation given the high share of food consumption. Government spending sustained demand for food. But in this sector structural rigidities prevented an expansion of supply, while monetary tightening reduced demand and raised costs for industry.

Chinese domestic savings were high and the Government could leverage these for large infrastructure spending from the nineties. This constituted a large fiscal stimulus that

[6] If a trillion dollars are required for infrastructure financing, $ 250 billion can possibly come from foreign savings if the CAD is pegged at about 3 percent.

maintained Chinese growth during the GFC. A country of one billion plus undergoing rapid catch-up growth requires a lot of infrastructure. India, which is 10 years behind China, was expected to go into a similar infrastructure cycle in the 2000s.

But low returns on past Government investments, and many leakage-ridden populist schemes, left the Government with positive deficits and a debt/GDP ratio which was not low. The fiscal consolidation necessary to reassure mobile capital in a more open economy was achieved through a reduction in public investment all through the first reform decade, especially since reduction of import tariffs reduced the tax/GDP ratio. The government was borrowing even for consumption—there was a revenue as well as a fiscal deficit. The neglect of investment in infrastructure further raised costs and created bottlenecks.

When the private sector did not adequately fill the gap and infrastructure constraints became pressing, the government did become more active in trying to push through public private partnerships in infrastructure. Some tax reform raised revenue but innovative forms of private participation and financing were still required to get around the finance constraint. Poor financial intermediation of savings, despite two decades of reform, prevented high domestic savings from funding infrastructure. Instead inadequate domestic inflation hedges increased demand for gold imports and widened the current account deficit.

Although there are ambitious plans to raise spending on infrastructure to one trillion dollars over the 12th Plan (2012-2017), about half will have to come from the private sector. The private sector did participate and targets for it were exceeded through the boom years, but investment collapsed below target in 2009-10 helping precipitate an overall slowdown. The cause was policy inconsistency and a failure of the government apparatus to gear up to providing the clearances required. The new scale of investment exceeded Government capacity. Private participation is difficult without a drastic improvement in procedures, since delays impact the balance sheets of private sector infrastructure firms.

Political constraints on policymaking explain the Indian government's neglect of investment and governance in the post-reform period. Inadequate policies are followed not out of ignorance, but because of political considerations. Poor governance and failures in education systems and in health care delivery may be symptoms of deeper problems that must first be resolved.

Why nations fail

AR illustrate how policy advice that does not recognize constraints was implemented in letter but not in spirit in Latin America:

> In Argentina and Colombia, central banks were also made independent in the 1990s, and they actually did their job of reducing inflation. But since in neither country was politics changed, political elites could use other ways to buy votes, maintain their interests, and reward themselves and their followers. Since they couldn't do this by printing money anymore, they had to use a different way. In both countries the introduction of central bank independence coincided with a big expansion in government expenditures, financed largely by borrowing (Pg.448).

The fiscal consolidation liberalizing reforms forced on India was achieved by reducing public investment and relying on foreign inflows to make way for subsidies. There was also a big expansion in Government borrowing.

AR argue for a State to create wealth for society as a whole, inclusive institutions must temper its power. Such institutions are the surest warranty for the success of a nation. They generate the creative destruction and innovation that sustains wealth. A State must be strong to be effective, but strength can imply a coercive pursuit of own interest[7]. For example, strong political centralization, which allowed the Soviet or Chinese State to coordinate resource allocation, explains their growth. But the authors expect such growth to be limited because a dominant State blocks innovation for fear of a loss of power. 'Extractive economic and political institutions' tend to be persistent, since even if newcomers take power they face few constraints and gain from maintaining extractive institutions.

AR regard India's failures as due the extractive institutions the British left it with, despite the democracy it also inherited from them. 'India was the largest producer and exporter of textiles in the world in the eighteenth century… The East India Company looted local wealth and took over, and perhaps even intensified, the extractive taxation institutions of the Mughal rulers of India,… initiated a long period of reversed development in India. (Pg. 272)'

[7] AR use Max Weber's famous definition: the State has a 'monopoly of legitimate violence' in any society.

But theirs is a geography based argument—institutions tended to be extractive when colonial powers did not intend to settle in a country, perhaps because of the climate. But the British did stay in India for hundreds of years and built courts, railways, and universities. It was probably the desire, in a country of large size and heterogeneous provinces, for strong central control that led them to establish a centralized Indian administrative service. No other country has such a service. It has retained the ethos of superiority and the distance of ruling elites. Together with multiple levels of government and agencies, it lowered accountability to the local populace. Reforms do not work when bureaucratic institutions are the cause of the problems. AR's example from India is of health administrators sabotaging a simple incentive scheme a NGO had designed in Rajasthan, which required nurses to stamp a time clock three times a day to reduce endemic absenteeism.

At independence, the prevailing philosophy of economic controls allowed the indigenous government to use and further increase the extractive power of the institutions they inherited, despite very inclusive political institutions.

Unlike Britain where universal suffrage took a long time in coming, India started with it. The West was very skeptical about the survival of Indian democracy, partly because of the 'unwashed hordes' invading the hallowed precincts of parliament (Guha, 2007). Their own history was one of a very careful extension of suffrage. The issue of extending voting rights dominated the 1831 British election, but even so universal suffrage was not considered even for men. The motive for reform was to preserve as much as possible of the status quo by forestalling a possible revolution. Moreover, preserving power had become less valuable since earlier reforms meant there were few monopolies and little power over labour left by then. Other reforms included introducing a secret ballot, eliminating vote buying or 'treating'. By1884 the electorate doubled again—now 60 percent of adult males could vote.

In contrast Indian democracy began with universal suffrage, but the possibility of clearly identifying vote blocks in a heterogeneous electorate, without thick institutions to eliminate corrupt practices, led to vote buying and populist policies that targeted specific groups.

The caste system, whose origin and rationale was economic, was widely expected to die out with modern economic development. Gupta (2000) shows how castes were never static. Through history the caste system had evolved in response to economic pressures:

> "The evolution to jatis was on account of the social transition to a closed village economy. With the level of productive forces remaining stagnant, any rise in population was accommodated in the feudal structure of medieval India at the cost of greater rigidification and further stratification of the jatis (pp 222)."

So economic stagnation had led to a proliferation and strengthening of caste hierarchies. Similarly, after independence caste-based vote banks sustained the caste system. Castes were organized to fight for rights (Béteille 2008). Letain (1994) shows the role of caste and communalism in UP elections. In the post-independence stagnation, caste-based policies to create vote banks sustained the caste system. Extractive institutions that lowered growth strengthened castes[8]. Thus caste allowed politicians to get away with stagnation, and stagnation further strengthened caste, but it was no longer a system of economic organization but a political identity[9].

Authors like Roy (2012) argue against AR that the British left strong legal institutions but caste interests weakened them. For example, laws the British made were subverted by loopholes left for caste. However, the causality may be the opposite. Extractive institutions made more so by economic controls lowered growth. Since politicians could base handouts on groups such as caste, they could avoid improving public services more generally. Low growth reduced democratic pressures for more growth. Institutions strengthened caste interests.

Creation of inclusive economic institutions

AR argue against historical determinism. Rapid change is possible at critical junctures that disrupt the existing economic or political balance. The change can be in the direction of more extraction or more inclusion. Inclusive ground conditions raise the probability that the path

[8] There are signs higher post reform growth is reducing caste distinctions. Kapur et. al.(2010) found that lower castes were now eating ritual upper caste foods in festivals in villages they studied. Prasad and Kamble (2012) report on research that finds dalits succeed most in new and caste-neutral occupations—reform opportunities suit dalit entrepreneurs. They found Delhi's Azadpur fruit and vegetable mandi did not have a single dalit adhatiya or middleman, since traditional castes dominate these occupations.

[9] Dipankar Gupta made the latter point. I thank him and Satish Deshpande for useful discussion on this topic.

taken will be in the right direction. An example AR give is the Black Death that led to the Second Serfdom in Eastern Europe, but had the opposite effect in England. It is useful to examine the historical process of building inclusive economic institutions in the UK in order to benchmark changes in Indian institutions.

The Glorious[10] and the French Revolutions succeeded because broad and diverse political groupings had emerged, such as the gentry, different types of manufacturers, and Atlantic traders, who could benefit from creative destruction. The gentry were a new class of commercial and upwardly mobile farmers that had appeared in the Tudor period. Both countries had a history of parliaments, rule of law and power sharing that had already weakened absolutist regimes. Especially by the standards of the time, the Parliament empowered a broad and strong coalition against Stuart absolutism.

The rule of law is different from much of history in that it removes special privileges elites routinely enjoyed, and safeguards rights that apply equally to all. AR give examples from the UK and the US to illustrate how this contributed towards restraining absolute power and creating more inclusive economic institutions and policy.

> "In 1689 the Company seized the cargo of an interloper, one Nightingale. Nightingale sued the Company for illegal seizure of goods, and Chief Justice Holt ruled that the Company's seizure was unlawful because it was exercising a monopoly right created by royal prerogative. Holt reasoned that monopoly privileges could be created only by statute, and this had to be done by Parliament. So Holt pushed all future monopolies, not just of the Royal Africa Company, into the hands of Parliament. Before 1688 James II would quickly have removed any judge who made such a ruling. After 1688 things were different. (Pg. 194)"

Power sharing under pluralistic political institutions prevents any one element from trying to get more power. Roosevelt encountering constraints on his power from the Supreme Court charged it with trying to make policy. He argued his electoral mandate gave him the right to infuse new blood into the courts in order to change this situation. But the U.S. Congress

---

[10] In 1688 the British Parliament won various privileges in the overthrow of the catholic King James II of England. His protestant half sister Mary and her husband William replaced him. England became a constitutional not an absolutist monarchy.

defeated Roosevelt's court packing plan. Broad segments of society were willing to push back attempts to vitiate the Court's independence, because under more inclusion the potential benefits of monopoly power were not worth the risks.

More inclusive political institutions made economic institutions more inclusive and eventually led to the Industrial Revolution. Domestic monopolies were abolished in 1640. After 1688 parliament strengthened property rights eroded under the Stuarts. It prevented arbitrary taking away of rights. Obscure property rights were simplified and made secure, encouraging private participation in infrastructure building[11].

> 'In 1962 Parliament passed an act to encourage investment to make the Salwerpe navigable, and the Baldwyn family invested 6000 pounds to this end. In return they got the right to charge people for navigation on the river. In 1693 a bill was introduced in Parliament to transfer the rights to charge for navigation to the Earl of Shrewsbury and Lord Coventry. This act was challenged by Sir Timothy Baldwyn.
> …the new act failed, and Baldwyn's rights were upheld. (AR pp.198)'

Parliament began to promote manufacturing, rather than taxing and restricting it. The hated "hearth tax (AR, pp. 194)", which fell largely on industry, was abolished in 1689. New parliamentarians from Manchester and Birmingham wanted cheap food and low wages so the Corn Laws which banned grain import, keeping prices high and benefitting large landowners, were repealed in 1846. Parliament could be petitioned and was likely to implement petitions that collected many signatures.

The education system was made more accessible to the masses. The Education Act of 1870 made the government responsible for the systematic provision of universal education, which was made free of charge in 1891. The school-leaving age was raised and special provisions made for children of poor families. The Liberal Party, in the early years of the twentieth century, began to provide public services, such as health and unemployment insurance, government-financed pensions, and minimum wages. As a result taxes rose many times and fell more on the wealthy.

---

[11] Property rights are multidimensional. Unclear definitions can limit certain kinds of commercial activities. There is the example of problems in conversion of agricultural land for industrial purposes in India.

Thus the characteristics of inclusive economic institutions are competitive entry, low broad based taxes, absence of arbitrariness in policy, and public services that enhance human capital equitably. Can latecomers accomplish all this faster? Leaders can choose to implement some of this policy set early, like many Asian countries focused on primary education even at low per capita income levels.

Economic Inclusion in India

The above process of inclusive political institutions leading to inclusive economic institutions, that allow productivity to rise, remains inadequate in India. But the country has long had the rule of law and private property even though implementation is poor. Interests were not the primary cause of Indian stagnation[12]. It was the ideas of government control and structural aspects such as castes that strengthened extractive institutions.

As the executive failed to deliver good governance, India saw increasing court activism. For example, Supreme Court orders sought to improve air quality in New Delhi and to investigate corruption in the allocation of natural resources. Legal changes also furthered more inclusion. NGOs and the middle class acquired clout through the mechanism of public interest litigation (PILs) and the Right to Information Act (RTI). The Right to Education Act was part of more rights based activism. Fiscal Responsibility and Budget Management (FRBM) legislation restrained the government's ability to spend.

Popular protest against corruption sought to reduce the government's discretion over resources—a major source of kickbacks. Independent constitutional bodies such as the Election Commission, the Finance Commission, and the Controller and Auditor General (CAG), became more active in preventing misuse of political power. This deepening horizontal democracy is pushing for better governance[13].

Broad-based political empowerment, a slow process of institutional strengthening, and the growing weight of ideas favoring change were sufficient for course corrections in critical junctures such as the crises in 1991.The coalition that gained from government-led

---

[12] Bardhan (1984) first made the argument that multiple interests the government had to placate kept Indian growth low.

[13] Organizations like Association for Democratic Reform and Praja are getting politicians to disclose their assets and police records and making report cards on elected representatives' performance.

redistribution dominated for a long time, because of heterogeneity and poverty. Opening out perhaps occurred as the forces that gained from growth strengthened, and the reforms strengthened them further.

So India in 2013 meets many of the ground conditions AR identify for institutional change, including pluralism of interests, a vibrant business class, and gradualism of reform. The markets that induce a virtuous cycle of more efficient allocation of resources, acquisition of education and skills, and technological innovations, are all there. As a result economic institutions are also slowly becoming more inclusive. The demand for better public services in health, education and infrastructure is rising since these enable more to make use of new opportunities growth creates. And the opportunities are now available to more. These pressures make 'active inclusion', defined as inclusion which creates conditions for the many to contribute to and participate in growth (Goyal 2012b), more acceptable politically. Government intervention remains essential, since there are externalities that limit private investment. But the intervention should lead to provision of better public services, thus increasing rewards to work[14]. This is uniquely suited to Indian catch-up growth and increasingly youthful demographic profile.

Poor governance and failures in education systems and in health care delivery are symptoms of deeper fault lines that have subverted productive inclusion. For change to occur internal political and external pressures must gradually make economic institutions more inclusive. Although growth does reduce poverty, since an expanding cake can accommodate more claims, without the correct interventions, inequality can rise. China reached LA levels of inequality starting from a system without divergence in private wealth. Democratic pressures for inclusive growth may help India avoid such an outcome if that inclusion becomes effective.

Since public investment is now too low to be further cut, the way towards fiscal consolidation is organizational efficiency, better targeting and composition of subsidies. Technology enabled direct distribution to the poor has the potential to reduce leakages, and free resources for provision of general public goods. The reforms made government more business friendly although the balance between extraction of revenue and encouraging business growth is yet

[14] Chatterjee (2011) argues that various government schemes have co-opted the peasant and made him less of a 'subaltern' who prefers to protest rather than to produce.

to be found. Table 1 shows India is more behind other countries in health, infrastructure and institutions than it does in financial market and business development. So it is clear where more attention is required. Else lagging sectors can choke others.

Table 1: India's world position on different criteria

Relative lags in:	***India's rank (highest is 1)***
Institutions	70
Infrastructure	84
Health and primary education	101
Higher education and training	86
Financial market development	21
Business sophistication	40

Source: The Global Competitiveness Report 2012–2013. World Economic Forum. http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2012-13.pdf

We illustrate the process of active inclusion at work in general governance, the telecommunication revolution, and in agricultural marketing. Institutions can be the most resistant to change where large numbers are affected. So change has been slowest in the institutions of general governance, and in the interventions in agriculture. But there is movement even in those areas.

Governance: overcoming institutional hysterises

Indian government administration performs very poorly. Cumbersome procedures hinder infrastructure investment, although inadequate infrastructure makes daily living hazardous. The criminal justice system is in shambles—with the number of policemen and judges ratio to population much below world averages—as 2012 protests against a gang rape have highlighted. The death in 2012 of Mahi, a 5 year old girl, after she fell into a drain because a manhole cover was missing, created country wide outrage. J Sinha, of the Boston Consulting Group, got a large reader response when he wrote about travails of providing an acceptable identity proof to a bank, given poorly thought through regulatory requirements[15]. Regulation of drugs in India comes under four government departments leading to delays in permissions that can range from 6 months to two years, compared to the practice in some countries that if permission does not come in 28 days it is regarded as given. There are also conflicts of

[15] Economic Times, Mumbai Edition,11 July 2012.

interest. Since the pharmaceuticals industry comes under the chemical ministry, the latter bats for the industry[16].

There is no shortage of potential improvements. Many stroke of the pen reforms can improve the Indian system. For example, the 5th pay commission suggested a structure for transfers of officials, and higher increments for those who perform. Successive expenditure reform commissions made useful suggestions for reorganizing administration, reducing multiple clearances, departmental overlaps and establishing clear accountability. These have been accepted by the Cabinet but not implemented. The problems with infrastructure clearances have clearly highlighted bottlenecks the current administrative structure creates.

In China government coordinates well since officials are accountable to the party boss. In India re-election is important so voter priorities become crucial[17]. But if voters can be split into clearly identified vote banks, and government schemes and power used for patronage, performance is not crucial for re-election. Many laws, unchanged since colonial times, give too much power to the administration. Some of the laws are so unreasonable that no one can follow them. Since everyone can be found guilty, they give a tool to the corrupt or unreasonable official to extort or victimize using the laws. But ill defined laws victimize administrators themselves also. For example, a clause in the Prevention of Corruption Act (1988) defines criminal misconduct by a public servant to include obtaining a pecuniary advantage for anyone without public interest resulting. Ensuring this is difficult in a market economy. All these laws need to be re-drafted. Clearer responsibilities will enhance outcomes and reputations of public servants[18].

An ex-IAS officer responding to Mahi's death blamed the absence of accountability. The superior tells the inferior to do something, he tells line department, but there is no follow up. In his view, an individual officer can still achieve much if he were to use his many powers. As district magistrate, he got work done by a contractor when the line department did not do

[16] Economic Times, Mumbai Edition, 10 July, 2012.
[17] Uma Lele made this point at a 2012 ICRIER workshop comparing governance in India and China.
[18] For example, Mumbai's laws require a citizen to take permission before serving hard drinks. One police officer used this to terrorize those throwing parties, on moral grounds—it was christened the Dhoble effect after him.

it, and deducted the money from the engineers' payment. The latter appealed to the courts but the deduction was upheld[19].

Very few individuals are willing to fight a system, however. The latter has to change and institutional hysteresis overcome. Demand for better governance, as rising prosperity increases the numbers who stand to benefit from it, will be critical. Governments act when their own interests are involved[20]. Legal changes, such as the RTI Act, that give citizens more power and enforce more transparency[21] are helping. With these essential background changes more competition and better incentive structures can contribute. An example of competition is initiatives such as the two state of the art passport offices in Delhi that compete with each other in providing better services.

The most critical Indian policy initiatives require the Centre and the States to coordinate well together. Agriculture, health, education, policing, and making India one market are all on the concurrent list of the constitution. Excessive centralization under the British[22] was initially strengthened due to concerns for national integration. The constitution mandated an Inter-State Council but a strong central government in the early years and the emphasis on planning denied it the weight it required. As the political system fragmented and regional parties came up, the States obtained more political freedom but coordination between the Centre and the States became very poor. GST is held up for lack of support by some big consumer States who fear they will lose revenue. Decentralization needed to be strengthened in the constitution, and this was attempted with the nineties 73rd and 74th Amendments on direct local level democracy but implementation remains uneven with some States able to use clauses to resist effective devolution.

Policymakers in the Centre focused on more opening up, because this was something they could do without persuading the States to come along. But it was also required because India was too closed an economy. But in 2011 and 2012 foreign inflows slowed because of both

---

[19] Times of India, Sunday 30thJune, 2012.

[20] Analysis of panel data showed states that have less corruption and can reach targeted vote banks (e.g. rural poor), were the ones that implemented e-governance initiatives. Loss of political funding from more transparent e-governance can be a major impediment to change, also for coalition partners (Bussell, 2012).

[21] Pethe et. al. (2012) point to the importance of more information, politicians make money from buying property they know is going to appreciate. A possible solution is to make their special information available to all.

[22] Granville (2002) points out the centralized federalism of the British 1935 Government of India Act was largely adopted in the Constitution.

domestic policy bottlenecks and external risks. Financing the current account deficit proved difficult. So, the difficult task of motivating the States to improve the supply-side must receive priority. Nations that were able to sustain growth were the ones that successfully addressed emerging bottlenecks.

In India's fiscal union the constitution clearly demarcates taxation powers between the Centre and the State, and lays down revenue sharing criteria, which are revisited by periodic Finance Commissions. These meet equity criteria by mandating higher awards to weaker States so as to enable the provision of uniform public services through the country, and are an essential part of making it one country. But since such transfers can motivate States to remain weak, recent Finance Commissions have also given States incentives to improve their finances, and special grants conditional on better types of expenditure. States that signed the FRBM legislation were given special debt forgiveness. These initiatives, together with buoyancy in shared central revenues, led to remarkable improvement in State finances. A viable fiscal union needs transfers plus some discipline. Euro zone countries are in trouble because they are not a fiscal union and there is no mechanism for transfers[23].

Additional transfers are also possible under Article 282 of the constitution and these have become dominant, accounting for as much as one third of State spending. Multiple centrally sponsored schemes, administered through the Planning Commission, have undermined the authority of the Finance Commissions. The Gadgil formula applies to only a fraction of the transfers so they are increasingly discretionary. Indeed, as Rath (2012) argued the Plan schemes took attention away from general public services for the average citizen, on which the first Finance Commission had focused.

Central ministries, too, make large transfers to the States. Part of the transfers could be made conditional upon improved public services, to help convergence among the States, as recent finance commissions and the urban renewal mission have done. Incentives from non-

[23] Bordo et. al. (2011) point out fiscal unions where the Centre unconditionally bailed out States or provinces tended to have very poor macroeconomic outcomes. For example, in Argentina and Brazil sub national debt added on to national debt without adequate tax revenue, and serviced by printing money led to hyperinflation resulted. Foreign debt ended in default. In contrast in the US after the Centre bailed out States from their war of independence debt, States overspent. After bail outs were refused and States began to balance their budgets, the Centre did mandate transfers for State health and education programs. In Canada bailouts were available only on severe conditionality so provinces preferred to default. Market discipline worked to improve finances as risk premia rose for in high debt periods.

discretionary mechanisms work best when they are immune from political renegotiation. They will also work since voters have begun to reward State governments that deliver better governance.

Tight restrictions on end use and delays in sanctions reduce the utility of the transfers for State Governments. The latter are guilty of the same treatment of lower level bodies such as Municipalities and Panchayats. Transfers should be made more time-bound and outcome based. But dialogue must also complement incentives. Regular meetings should evolve new policy initiatives, not just communicate a policy decision.

Since they first have to get the Centre’s permission, scope for market borrowings by Indian States is limited, as is market discipline, with the centre absorbing the risk. Gradually this should change and States with higher debt should pay higher rates. Market borrowings have risen in the recent period, as they have increasingly substituted for loans from the Centre.

The Cabinet Committee on Economic Affairs’ (CCEA) 2012 decision to restructure the debt of state distribution utilities (discoms) has some of the required combinations of discipline and transfers. Therefore it is likely to work better than a package given ten years ago that did not prevent the discoms piling up debt again. The decision to take over 50 percent of the short-term debt of discoms in the next two to five years while providing grants for improvement over and above targets is similar to the debt consolidation and relief facility the Twelfth Finance Commission had given. The grants for improvement would encourage reform measures, while short-term debt restructuring improves discipline.

States are to notify the tariff order for a financial year by end-April, make upfront subsidy payment, meter and monitor the turnaround plan, convert state governments loans into equity, involve the private sector, and ensure punctual auditing of accounts. The carrot comes from a central government grant equal to the value of additional power saved from technical and commercial loss reduction above a limit proposed. There will also be capital reimbursement support for 25 percent of principal repayment by the state government on the liability undertaken under the new proposal.

If the Centre’s initiatives improve governance, its own transfers are better designed, delivered and targeted; an increasingly aware electorate would reward it just as it is rewarding better governance in States. Yardstick competition and convergence will take place across administrations. As some States allow FDI in retail, change labour laws, reform power distribution and do better, others will follow. This happened with the adoption of VAT. As States that implemented it gained revenue others followed. No one wants to be the last man standing. Witsoe's (2012) study of Bihar shows how large numbers of agents involved in corrupt activities quickly turned to more constructive activities with a regime change.

There are problems with decentralization also—it is not a panacea. It sometimes allows feudal local elites to usurp power. A study on Bengal village schools (Roy et.al, 2012) shows how local parent-teacher committees are run by CPM officials, who dictate policy. Scheduled Tribes who are aware of the poor quality of teaching do not dare to speak up. Apart from strengthening community participation and awareness, focusing on the district is a via media. Chidambaran argues this is the lowest sustainable unit of administration and is the appropriate level to introduce governance reforms. Empowering three district level officers to run the Integrated Action Plan introduced in 60 Naxal affected districts, worked well[24].

Preventing extortion: Telecom

The cellular mobile story is well known in India, but we shall touch on it briefly since it illustrates the institutional deepening required to encourage industry, yet prevent extortion of wealth through a combine of politicians and industrialists, especially as natural resources rise in value with growth.

In 1992 private operators were allowed in mobile telephony and licenses were granted over 1994-95. Foreign partners brought in the latest technology. From the beginning the government made sure there was competition by allotting licenses to more than one provider in a circle. But it was after the Telecom Regulatory Authority of India, set up in 1997 and reconstituted in 2000, moved from a fixed fee to a revenue sharing model that the sector really took off. License fees were lowered by the NDA government. The growth of the communication sector was in double digits after 2000 and its annual contribution to GDP growth around ten percent[25]. India moved from just 5 million telephone subscribers in 1991 to 37 million in 2001 and more than 900 million connections in 2012. Competition ensured

[24] Chidambaram's (2012) interview to Inclusion, available at http://www.inclusion.in/index.php?option=com_content&view=article&id=802

[25] Mani (2007) also http://www.nistads.res.in/indiasnt2008/t4industry/t4ind14.htm, and news reports.

India had one of the world's lowest tariffs. Millions of poor people benefitted from these services. Outcomes like these go against Kohli's (2012) argument that reforms were pro-business rather than pro-market. There was a decline in protection, and competitive entry led to many new businesses that did very well. It is true however, that poor business services favoured big business since small business is more dependent on public goods.

But great wealth brings with it both temptation and suspicion. In 2008 the UPA government minister A. Raja allocated more 2G mobile licenses on a first come first served basis. The Government auditor CAG alleged a large revenue loss to the Government. The figure gained credibility from the Rs 106,219 crores the government earned from 3 and 4G licenses allotted through auctions in 2010. In 2012 the Supreme Court (SC) cancelled the old allocation and ordered new 2G auctions. But when they were held in November of that year only 9,407.64 crs were raised against the 40,000 crs expected, casting doubt on the CAG figure that had triggered a series of corruption allegations[26].

The SC clarified, in response to a Presidential query, resource allocation was a policy decision and therefore a prerogative of the executive. While auction was not essential, the allocation should be in the 'common good'. The SC could intervene if an allocation did not satisfy the criteria of 'fairness and non-arbitrariness'[27], as in the case of Raja's allocations. Since judicial activism can easily result in judicial overreach, especially since the judiciary has no executive powers and little economic expertise, this judgment was a useful clarification of the constitutional separation of powers.

Industry leaders argue the rollout of 3G services has been minimal partly because of the large amounts paid for the licenses. The sector will see bankruptcies and takeovers and the earlier type of growth will no longer be possible. There are also complaints of too much competition and too little spectrum allocation compared to international norms. Industry will always lobby to minimize what it pays the government. Vodafone took advantage of loopholes in

[26] In that atmosphere Government could not go against the high reserve price TRAI set of Rs. 18,000 crs. Companies like Bharti and Vodafone that were given licenses in 1994 do not have to take part, but the auction price will determine what they have to pay when they renew their licenses in 2014. At the Government reserve price of Rs. 14,000 crs (many multiples of the 2008 price), there was little competitive bidding. Also 3G data services have more scope for revenue compared to 2G which carry only voice telephony. Even so, the reserve price set in the 3G auctions had been lower (about Rs. 3000 crs) but was raised by competitive bidding. Source: news reports.

[27] See news reports on the SC judgment, for example, Times of India, September 28, 2012.

Indian law to avoid taxes when it bought over Hutchison Essar, an earlier player. But indebted firms will pass on the cost to consumers, and invest less in providing the services, thus reducing growth rates. This in turn reduces future revenue to the Government, and the welfare of the subscriber.

Discretionary allocation of captive coal blocks to private companies by Government committees led to similar allegations of favouritism and kickbacks, and a backlash from civil society, while lack of consistency and clarity in policy discouraged investment. The Government's defense was that the allocation, made only to power and cement companies, meant to reduce costs and prices charged to the consumer and to quickly ramp up coal production in the country. Inadequate coal from the nationalized public sector was creating bottlenecks. De-nationalization would be a long-drawn out process.

The major gain from their natural resources, whether spectrum or coal, should go to people in the shape of low prices for the products they consume. Neither companies, nor government, should be able to grab a major share. Auctions have the desirable property of removing the government's discretion in allotting natural resources, which can be a major source of corruption. A single-step auction based allocation, with a low reserve price, and part of the payment to come from future royalties, could avoid both discretion in allocation and large upfront costs that reduce subsequent development. Apart from the contract, adequate competition can ensure prices remain low, and service quality improves.

As growth raised the value of natural resources, and potential extraction by any one group, the checks and balances of Indian democracy, and a more empowered public, exposed the corruption, held up the allocation and lowered the growth rate. Tainted ministers had to resign and faced court cases[28]. The price is worth paying as part of the process of building more robust inclusive institutions that prevent extortions by those in power. It is difficult to estimate how much of this happened in China, where power is absolute. The Bo Xilai case may have revealed only the tip of the iceberg. The issue of natural resource allocation

[28] These apart from A Raja, include Suresh Kalmadi, Chair of the 2010 Commonwealth Games, and in Maharastra Ashok Chavan Chief Minister in the Adarsh Housing Scam, and Ajit Pawar, who as water resources minister sanctioned a large number of irrigation projects with unprecedented cost escalation. Ajit Pawar's argument was he was unfairly blamed for speedy file clearance. Procedures have to be made faster yet more robust.

revealed inadequacies in Indian institutions, but they are responding to close gaps, and make extortion more difficult.

Reducing Monopoly: Agricultural marketing

During the reforms, areas where more competition was introduced did well. The two areas with minimal opening out, government and agriculture are the ones that are lagging. The structure of government interventions in agriculture established around the time of the major droughts in the mid sixties have continued, largely unchanged, since then. They were based on input subsidies, higher output prices supported by government set procurement prices, and a monopoly to State marketing boards, to develop markets and to support government procurement that fed a subsidized public distribution system. Together with new green revolution technology, these initiatives lead to a large rise in production, making the nation self-sufficient in foodgrains production. Food security is a pressing issue, given the numbers of poor, and justifies elaborate interventions.

Although the idea was to help farmers by developing markets that did not yet exist, over time production stagnated as various types of monopolies developed and markets were segmented. India's experience with State marketing boards these illustrates how an institution set up to help can become extractive[29]. APMC Acts prohibits transactions in agricultural products outside the 'market yard' of regulated markets, of which there are around 8000. Thus direct marketing or contract farming is prevented, reducing corporate involvement and farmer and consumer options. About 15 per cent of the 22,221 rural periodical markets also come under the APMC regulation. Licenses for trade are issued by market committees, the average mandated fees to be paid to them are around 10 per cent, although there is a range. The fees are meant for developing infrastructure but most markets do not have cold storage and grading facilities. India is said to be the world's largest producer of fruit and vegetables but as much as 30-40 per cent are estimated to be lost due to poor post-harvest storage and transportation. Estimated value addition (7 per cent) and commercial processing (2 per cent)

[29] AR describe the Sierra Leone Produce Marketing Board set up in 1949 during the colonial period ostensibly to smooth coffee prices and help farmers. To meet costs of functioning it paid the farmers less. But soon it became a way of heavily taxing farmers. This got much worse after independence. Stevens's government extracted 90 percent of farmers' income. The revenue was used for personal enrichment and to buy political support, not to provide public services. The extraction by Indian marketing boards had similar aims but never reached such high levels. In countries with effective democracy such as Botswana, in contrast, administrative control of agricultural prices was relaxed. A system of more voluntary contracts took the place of mandatory state purchasing of grain.

are both low. Governance is poor, professionalism is lacking, and regular elections are not held for the agricultural produce market committees. Commission agents are said to be a source of political funding.

The trade in food products suffers from other distortions. The Essential Commodities Act (ECA), enacted in 1955 in response World War II scarcities, imposes limits on stocking foodgrains. State level differential tax regimes, policies and laws also artificially segment markets. Private traders require permits to transport foodgrains out of a state, or even a district. The National Permit System does not apply to trucks. Multiple clearances add to problems—environment laws and agricultural input interventions also sanction physical checks on trucks. The average time required to cross an inter-state border is two hours. Such checks are especially costly for perishable products. Adoption of the GST will remove many of these irritants. Even without that the Constitution allows market facilitating agreements between two or more States under Article 252 of the Constitution.

Estimates, from the Government's own committees, of gains from harmonization and unification of these markets are large[30]. As waste and transportation costs fall, farmers will get higher prices while consumers pay less. Agriculture and related activities will grow faster, raising exports and employment. That agricultural growth rates have fallen in the post-reform period suggests the government's agricultural interventions need rethink. Precision farming that scientifically measures inputs has been able to save precious water and other inputs yet yield large productivity gains in some areas (Bhattacharya, 2012). With the rise in per capita incomes and more effective minimum wages, there is a diversification of food basket. More demand for fruits and vegetables is making the public distribution scheme (PDS) less relevant since the PDS cannot cover all these. It was part of an intervention strategy based on foodgrains. Now general agricultural marketing has to improve. Rising productivity and employment in products, such as fruit, vegetables and protein items, for which demand rises with incomes, is the way to achieve sustainable growth.

[30] For example, post-harvest losses to fall 5-7% for grains and 25-30% for fruit and vegetables; static efficiency gains from disintermediation of distribution up to 20%; savings in compliance costs from fiscal unification 5-20%, depending on the stage, and revenue gains of 25% from a full GST.

Sustained high food inflation and its spillover into general inflation are forcing some action to improve productivity and marketing in agriculture, and give farmers more options[31]. There are proposals to introduce PPP to improve functioning, and to take perishables out of the ambit of the APMC Act, since raising time and transaction costs especially harm perishables. Some States, for example, Andhra Pradesh, Tamil Nadu, Maharashtra and Odisha have permitted direct marketing outside APMC. Weakening the APMC will also facilitate other innovations such as negotiable warehouse receipts, bank credit against such receipts, and support for construction of warehouses and storage facilities.

Better supply chains in turn would make possible more substitution of the costly and ineffective PDS with cash transfers or food coupons, thus ensuring better targeting with lower leakages and corruption. With less procurement required the government's need to force a monopolistic marketing structure to help its procurement will reduce. Economic institutions will become more inclusive. The large difference between Indian consumer and wholesale price indices is partly due to inefficiencies in retail. Retail absorbs unemployment and is a source of political corruption[32]. Fear of creative destruction that could upset existing power bases has prevented change, but it is beginning and gathering force.

FDI in retail would be an added change agent. The 2012 enabling policy allows States that want it, to allow it, subject to certain conditions such as back end processing. Others need not. As the gains become obvious more and more States will join. And as the numbers of those who stand to gain from better market integration rise, change in restricting laws will take place, setting in motion a virtuous cycle. FDI by itself is not sufficient—other legal and institutional impediments have to be reformed. But it can boost the strength of the forces making for change[33]. As suggested in the earlier section, some of the many transfers from the Centre can also be used to motivate faster change in the States.

---

[31] A large number of government committees and reports have addressed the issue. These include a 2010 Commission on Centre-State relations report, a Draft National Competition Policy, Working Group of the 12th Five Year Plan on Agriculture Marketing Infrastructure, http://planningcommission.nic.in/aboutus/committee/wrkgrp12/agri/weg_rep_market.pdf, Interministerial Group on Inflation, http://finmin.nic.in/workingpaper/IMG%20on%20Inflation.pdf, A National Academy of Agricultural Sciences (NAAS) 2011-12 report on agriculture http://www.indiawaterportal.org/sites/indiawaterportal.org/files/state-of-indian-agriculture-report-naas-2011-2012.pdf. See also Debroy (2012) and Khan (2012).

[32] Ashok Gulati estimates Azadpur Mandi in Delhi to have 45,000 commission agents.

[33] Nayar (2011) argues the forces of globalization are pushing India towards forming one market.

Conclusion

After opening out and crossing a threshold a nation's potential growth is high during the process of catch-up with the frontier. But growth can slow due to inadequate macroeconomic stabilization in response to internal and external shocks, and failure to address emerging bottlenecks. Nations that were able to sustain high growth were willing to intervene in markets as necessary but were flexible enough to change policies that began to create large distortions. They anticipated and adjusted policies as required for growth.

But political power and interest, as enshrined in institutions, drive policy choices. Inclusive political and economic institutions make it more likely the correct choices that empower broad sections of the population to contribute to and participate in growth are made.

India started out with highly inclusive political institutions since it adopted democracy with universal suffrage at independence. But extractive economic institutions, inherited from the British, were made more so by the dominant development ideas of the time, which strengthened the apparatus of controls over economic activities. The heterogeneous electorate, which could be divided by caste, class, community and region, and economic stagnation in the closed government led economy, allowed politicians to seek re-election through cultivated vote-banks and populist schemes instead of delivering better governance. An important lesson is caste based polices must give way to better general public services in a new India. Civil society must push for provision of better schools, roads and hospitals to service disadvantaged groups rather than for reservations. Since such groups account for more than half of the population, such a large percentage of reservations will destroy productivity. The solution is to equip them with better skills. This becomes easier since many intermediate occupations appear in a higher growth economy. The argument that reservations have not created equity so reservations are required in all types and hierarchies of activities is flawed. Reservations were originally introduced for ten years. They have lasted for sixty years but have still not delivered. Equality of opportunity, together with a move towards proportional representation rather than the current first past the post electoral system may do better. The latter has not delivered majority governments for quite some time. So political power based on population proportions and skill based access to jobs may deliver social justice and progress.

As the world left India behind, and the dominant development ideas changed to favour more openness, India also adopted liberalizing reforms. Opening out was gradual and nuanced, and this was beneficial, since it helped mitigate the impact of the many external crises in this period. But even so, external liberalization was easier to do than many required internal changes, since the latter affected more domestic interest groups. But the temptation to use more opening out and inflows as a substitute for harder domestic reforms is a short-run policy that can dangerously increase dependency in the long-run. Since the only way to improve the fiscal deficit is to cut slack in the system and the only way to attract inflows to finance the current account deficit is to remove supply-side bottlenecks, the government is being pushed to tackle these issues.

Poor institutions generated interests that favoured stagnancy. A change in ideas and a rise in the proportion that benefit from growth have strengthened institutions. Interests are now pushing economic institutions towards more inclusion. Institutions no longer just serve elite interests. Systems and incentives are improving. Examples from general governance, the regulation of industry, and agricultural marketing show although the process is messy and prolonged, it is in the right direction. These improvements suggest that although catch-up growth has been volatile in India, it may be able to avoid the middle-income trap, as broader sections are systematically empowered for active inclusion.

References

Acemoglu, D. and Robinson, J.A. 2012. *Why Nations Fail: The Origins of Power, Prosperity and Poverty*. Crown: New York

Bardhan, P. 1984. *The Political Economy of Development in India*. Basil Blackwell: Oxford. Expanded edition, New Delhi: Oxford University Press, 1998.

Bhattacharya, A. 2012. ‘Quiet Revolutions’, *Business Today*, August 19.

Béteille, A. 2008. ‘Constitutional morality’. *Economic and Political Weekly*. 43 (40), pp. 35-42. October 4

Bordo, M., Jonung, L. and Markiewicz, A. 2011. ‘A fiscal union for the Euro: Some lessons from history’, *NBER working paper no. 17380*. September.

Bussell, J. 2012. ‘E-governance and corruption in the Sates: Can technology serve the aam admi?’. *Economic and Political Weekly*. 47 (23), pp. 77-85 June 23.

Cai, F. 2012. 'Is there a "middle-income trap"? Theories, experiences and relevance to China'. *China and World Economy*. 20 (1), pp. 49-61

Chatterjee, P. 2011. *'Lineages of Political Society: Studies in Postcolonial Democracy'*. Ranikhet: Permanent Black.

Bibek, D. 2012. 'The story of (un) competitive agriculture', in *No One Killed Agriculture, Special Issue Inclusion* http://www.inclusion.in/index.php?option=com_content&view=article&id=796

Goyal, A. and Arora, S. 2012. 'Deriving India's potential growth from theory and structure'. *IGIDR working paper no. WP-2012-018*. Available at http://www.igidr.ac.in/pdf/publication/WP-2012-018.pdf.

Goyal, A. 2012. 'An appraisal of five year plans and the future'. In *Yojana*, special issue on *An Approach to 12th Five Year Plan– Issues and Challenges*. January.

Goyal, A. 2011. 'History of monetary policy in India since independence'. *Report for 2010-11 first Professor P.B. Brahmananda Memorial Research Grant Award, 2011.*

Goyal, A. 2004. 'Puzzles in Indian performance: Deficits without disasters'. Chapter 12 in *India Development Report 2004-05*, Kirit S. Parikh and R. Radhakrishna (eds.), New Delhi: IGIDR and Oxford University Press, 2005.

Goyal, A. 2001. 'Reasoned optimism'. *The Economic Times*, June 19.

Goyal, A. 1999. 'The political economy of the revenue deficit'. In *India Development Report 1999-2000*, Kirit S. Parikh (ed.), New Delhi: IGIDR and Oxford University Press.

Granville, A. 2002. 'The expected and the unintended in working a democratic constitution', in Z. Hasan, E. Shridharan, and R. Sudarshan (eds.) *India's Living Constitution*, New Delhi: Permanent Black.

Guha, R. 2007. *India After Gandhi: The History of the World's Largest Democracy*. Macmillan: London.

Gupta, D. 2000. *Interrogating Caste: Understanding Hierarchy and Difference in Indian Society*, New Delhi: Penguin Books, India.

Kapur, D., Prasad, C. B., Pritchett, L. and Babu, D. S. 2010. 'Rethinking inequality: Dalits in Uttar Pradesh in the market reform era'. *Economic and Political Weekly*, Vol. 45 (35), pp. 39-49. Available at http://casi.ssc.upenn.edu/system/files/Rethinking+Inequality+DK,+CBP,+LP,+DSB_0.pdf.

Khan, H. 2012. 'Food inflation and agricultural supply chain management'. Deputy Governor, RBI, speech available at http://rbidocs.rbi.org.in/rdocs/Speeches/PDFs/FIASCM230912.pdf

Kohli, Atul. 2012. *Poverty Amid Plenty in the New India*, New Delhi: Cambridge University Press.

Leiten, G.K. 1994. ‘On caste and communalism in Uttar Pradesh’. *Economic and Political Weekly*, 29 (14), pp. 777-81. April 24.

Mani, S. 2007. ‘Revolution in India’s telecommunications industry’. *Economic and Political Weekly*, Vol. 42 (7), pp. 578-580. February 17.

Nayar. B.R. 2011. Globalization, the State, and India's halting march to common market: The political economy of tax reform under federalism', *India Review*, 10 (3), pp. 201-245

Pethe, A., Tandel, V. and Gandhi, S. 2012. ‘Unravelling the anatomy of legal corruption: Focusing on ‘honest graft’ by politicians’. *Economic and Political Weekly*. 47 (21), pp. 55-62. May 26.

Prasad, C.B., and M. Kamble. 2012. ‘To empower dalits do away with India’s antiquated retail trading system’, *Times of India,* Mumbai Edition, December, 5.

Rath, N. 2012. ‘Economic origin of regional and caste parties’. *Economic and Political Weekly*. 47 (30), pp. 24-28. July 28.

Roy, D. and Banerjee, P.S. 2012. ‘Decentralised governance reforms in primary education: Some reflections on West Bengal’. *Economic and Political Weekly*. 47 (24), pp. 67-74 June 16.

Roy, T. 2012. ‘Empire, law and economic growth’. *Economic and Political Weekly*. 47 (8), pp. 97-104. February 25.

Spence Commission on Growth and Development. 2008. ‘The Growth report: strategies for sustained growth and inclusive development’, Chair M. Spence. Available at http://go.worldbank.org/FC797ZNZP0.

Witsoe, J. 2012. ‘Everyday corruption and the political mediation of the Indian State: An ethnographic exploration of brokers in Bihar’. *Economic and Political Weekly*. 47 (6), pp. 47-54 February 11.