India in a Changing World

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By

Govind Bhattacharjee

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Preface

India made its first tryst with destiny seven decades ago on August 15th 1947, when it freed itself from nearly two centuries of colonial rule and became independent, but the fruits of independence eluded and disillusioned her people for a long time afterwards. For the first 50 years or so after independence, a large number of Indian people remained poor, malnourished and illiterate, deprived of the benefits of health, education and sanitation and a standard of living that could even remotely be called decent. The public delivery system crumbled and became completely dysfunctional and the administrative bureaucracy became completely insensate, close-minded and inward-looking, while the political system remained mired in endemic corruption and cronyism. Guided by the dated socialistic ideas of the first Prime Minister, Jawaharlal Nehru, the party that ruled for the majority of independent India's history, the Congress, followed a disastrous policy of squandering national resources through economically unsustainable welfare programs–basically by distributing dole to the marginalised sections of the electorate to ensure their continuance in power–without creating much capital. The presence of the State became overwhelming, guiding and interfering in every aspect of the life of citizens and businesses. The unlimited creative potential of its people remained shackled under the stifling command and control structure of a corrupt License-Permit Raj regime that was killing all initiative and entrepreneurial spirit. The nation came very close to becoming a failed state, both economically and socially.

However, destiny made another tryst with India in 1991 to rescue the nation from the brink of an impending collapse. The command-control structure was dismantled and India found a new freedom hitherto unknown. As this liberation asserted itself, the new-found energy of the youthful nation soon translated into much higher economic growth with a consequent reduction in poverty. It looked as if the nation had found wings with which to soar, and the sky was the limit. However, this growth story would soon end. The fruits of growth were not recycled into the economy but pilfered away through corruption which became ever more rampant. As scam after scam of ever larger proportions started rocking the government, the economy started failing again, and dole politics was resorted to in a big way to woo the electorate, along with the usual appeals to caste and religion. Hope gave way to pessimism and the country's future again looked uncertain. Another tryst with destiny was badly needed and a new government was elected to power with an overwhelming majority. The new government launched some path-breaking and disruptive reforms, but seems unable to control the social conflicts and tensions engineered by the extremist elements in society who are increasingly becoming more powerful and are trying to create further divisions in an already divided society by raking up the past.

India is currently passing through a period of great churning – socially and economically, as well as politically. It is making a complete break with its past to redefine its priorities and rediscover itself. This churning is something like the primeval *manthan*–the mythological struggle between gods and demons for the eternal nectar that brought the promise of immortality. The nation's future depends on the outcome of this *manthan*, whether it will throw up the nectar of social harmony or increase the polarisation of society; whether it will bring economic prosperity or keep the country permanently trapped in a lower middle-income bracket. Social transformation is a prerequisite for economic prosperity; they usually go together providing positive feedback to each other and altering the nature of socio-economic and political institutions, promoting pluralistic polity and participative decision making and removing the impediments to inclusive growth. Whether the events, initiatives, reforms and ideas of today will usher in such a transformation, only time can tell, but it is up to us to reflect upon the events of today to identify the sign of changing times that can mould and shape our future, and to adjust our strategy and direct our development accordingly. At the same time, we are a part of the larger world and cannot ignore what is taking place outside the country and the ideas that are transforming the future of this fast-changing world.

In this book, I have tried to capture the essence of these remarkably changing times which have the potential to transform the socioeconomic landscape of the country against the backdrop of a globally connected, but changing world, by releasing the energy and creative potential of the billion-plus population of a youthful nation, while drawing attention to the flaws that have seriously bedevilled its development and growth. The book is a collection of 50 essays published in several national newspapers and academic journals on recent events and the landmark reform initiatives undertaken during the last 3-4 years. In that sense, it chronicles the changing times in India so that the reader gets a sense of history, while appreciating the results and shortcomings of these reforms and how they are transforming the nation's economy and society.

The essays are organised in seven sections: (1) Breaking with the Past; (2) Shaping the Future: Disruptive Reforms; (3) Suboptimal Delivery; (4) India and the World; (5) The Churning of Society; (6) Tumult in the States; and (7) The World Around. Each section contains a few essays dealing with its respective topic. Major events that have influenced geo-political developments in our world in recent times and ideas that are shaping its future with consequent impact in India have also been covered here. Each essay is self-contained and narrated in a simple manner to allow the lay reader to understand and appreciate the essence of the topic discussed. There is a short summary at the beginning of each essay to introduce the topic to the reader. With society being dynamic, sometimes new events have overtaken those described in an essay, and wherever this has happened, an endnote has been appended by suitably updating the contents.

The ideas and events described in this book are recent; they have impacted our lives in some way or another, and we have not yet forgotten the excitement, and sometimes also the disappointment, that these have brought to our lives. I wish to re-engage the reader who has lived through these interesting developments and has witnessed the unfolding of these events. These are not events that have happened outside our world or ideas that are alien to us; they are still vibrant and forceful. Being intensely involved with these in a personal way, the reader may immediately relate to and reflect upon them, and contribute to the process of growth by providing useful feedback to the appropriate persons.

I am grateful to the Editor, The Statesman, and editors of all other journals, web portals and blogs where these essays have originally appeared for kindly permitting me to reproduce these essays in this book. I am also deeply grateful to the publication team at Cambridge Scholars Publishing, especially to Mr. Adam Rummens, Ms. Sophie Edminson, Ms. Courtney Blades and Ms. Amanda Millar, for making this book see the light of the day. I am grateful to Dr Shaibal Gupta and Dr P P Ghosh of the Asian Development Research Institute, Patna, and my senior colleagues at the Office of the Comptroller & Auditor General of India, Dr P Mukherjee and Shri Anupam Kulshreshtha, for reviewing the manuscript, besides providing me encouragement and support throughout.

Govind Bhattacharjee
June 21 2019

LIST OF ABBREVIATIONS USED

Most of the abbreviations used in this book have been explained wherever they appear in this book; however, there are still some commonly used abbreviations which have been frequently used. A list of these abbreviations is as follows:

AAP	Aam Admi Party
ASSOCHAM	Associated Chambers of Commerce and Industry in India
CAG	Comptroller and Auditor General of India
CBI	Central Bureau of Investigation
CBSE	Central Board of Secondary Education
CCT	Conditional Cash Transfer
CM	Chief Minister
CSO	Central Statistical Office
DBT	Direct Benefit Transfer
DISCOM	Distribution Company
FRBMA	Fiscal Responsibility and Budget Management Act
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GFD	Gross Fiscal Deficit
GSDP	Gross State Domestic Product
GST	Goods and Services Tax
ISIS	Islamic State of Iraq and Syria
JD(U)	Janata Dal (Unity)
LPG	Liquefied Petroleum Gas
MGNREGA	Mahatma Gandhi National Rural Employment Guarantee Act
MODVAT	Modified Value Added Tax
MP	Member of Parliament

MRTP	Monopolies and Restrictive Trade Practices
NATO	North Atlantic Treaty Organisation
NDA	National Democratic Alliance
NGO	Non-Governmental Organisation
NPA	Non- Productive Asset
NREGA	National Rural Employment Guarantee Act
NSG	Nuclear Suppliers Group
OBC	Other Backward Castes
OPEC	Organisation of Petroleum Exporting Countries
PWD	Public Works Department
RBI	Reserve Bank of India
RJD	Rashtriya Janata Dal
RTI	Right To Information
UDAY	Ujjwal DISCOM Assurance Yojana
UPA	United Progressive Alliance
VAT	Value Added Tax

SECTION 1

BREAKING WITH THE PAST

1. Twenty-Five Years of Reform
2. Disband the Planning Commission
3. Choice of Institution
4. Expenditure Reform
5. Will Federalism at Work Let Populism Thrive?
6. Management of Public Debt
7. Taxing Agricultural Income

1. TWENTY-FIVE YEARS OF REFORM[1]

(The economic reforms of 1991 have transformed the country from a poor one to a lower middle-income one. India has already left her dismal past way behind. We now need a second wave of reforms to transform the country into a global powerhouse.)

Three decades are but a speck of time in the history of a nation, yet the last three decades have been truly momentous for India's transformation from a poor underdeveloped country to an economic powerhouse to be reckoned with. The fiscal landscape of India today is unrecognisably different from that of 1986, when V. P. Singh, Finance Minister in the Rajiv Gandhi Government, rose to present his budget on February 28th. The then economic growth rate of 4.5 percent was little better than the Hindu rate of growth, and the fiscal deficit was nearly 12 percent of the country's Gross Domestic Product (GDP).

While attempting "to create a dynamic country that is equal to any other country in the world", Mr Singh reduced the number of income tax brackets from 8 to 4, and the marginal tax rate from 66 to 50 percent. Alongside this, to reduce the cascading effect of taxes on the final price of goods, MODVAT was introduced, allowing duty paid on raw materials to be set-off against the duty on final products. These were probably the first major tax reforms after independence. However, this was still the era of the dictatorship of the Planning Commission, the extra-constitutional, politically-appointed body of so-called 'experts' that decided how resources were to be deployed for development. The License Permit Raj architecture of the command and control economy was in full bloom, and, under its tyranny, the economy was getting throttled by extensive regulations, protectionism and a public sector supposed to dominate the 'commanding heights of the economy', but which was actually defined by cronyism, patronage, pilferage and inefficiency. In such a centralised planned economy, growth and productivity were the ultimate casualties, and the market–the driver of growth in any modern economy–was not allowed to flourish. The result was a forced impoverishment of the nation that earned India the

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[1] Originally published in *The Statesman as* "Twenty-Five Years After", 3rd August, 2016.

nickname the "Sick Man of Asia". Even though Mr Singh ended by asserting "his faith in [the] new India", that faith would be short-lived. Crisis was already knocking at the door, and would take the nation perilously close to becoming a failed state only five years later when it would have to be brought back from the brink of an impending disaster.

In the history of independent India, July 1991 was perhaps the most eventful month in terms of significance and profundity of impact. While we had attained our political independence in August 1947, it was only in July 1991 that we could finally make an irrevocable break with the past and take active steps to attain our economic independence from the stifling state controls that had stymied the nation's growth for decades. It was in this month that we had finally buried the disastrous legacy of Nehruvian socialism that had restricted the nation to a Hindu rate of growth since independence and kept its people in endemic and abject poverty while flaunting a socialistic pattern of society. We really came back from the brink of disaster, from being perilously close to becoming a failed state.

Since the mid-Eighties, the country had been sinking deeper and deeper into an economic quagmire, primarily because of the continued worsening of its balance of payments position, triggered by an overvalued currency. The Gulf War had exacerbated the crisis by swelling import bills and dwindling our scarce forex reserves. Nehruvian economics of deficit financing had led to escalating fiscal deficits which rose to 8.4 percent of the GDP by 1990-91. Inflation was over 12 percent, and internal debt alone rose to 53 percent of the GDP. India's external debt increased to US$72 billion from only US$20.5 billion in 1980, making India the third largest debtor nation after Brazil and Mexico. By June 1991, foreign exchange reserves fell to only $600 million, or only 2 weeks' equivalent of imports, and the prospect of defaulting on its external balance of payment obligations was looming ominously over the nation.

To escape the humiliating prospect of sovereign default, a desperate government had to secure an emergency loan of $2.2 billion from the IMF by pledging almost its entire stock of 67 tons of gold reserves as collateral. To complete the humiliation, the IMF insisted on the physical transfer of this gold, and the RBI had to airlift 47 tons of gold to mortgage the Bank of England and the remaining 20 tons to the Union Bank of Switzerland. While this gold was being transported to the airport, the carrier-van broke down, creating widespread panic. As a chartered plane ferried the precious cargo to London during the last 10 days of May 1991, an outraged nation and its hapless leaders were jolted out of their deep slumber after 44 years. The

Chandra Shekhar Government that presided over this crisis collapsed shortly afterwards, and on 21st June 1991, Mr P. V. Narasimha Rao took over as Prime Minister, with Dr Manmohan Singh as his Finance Minister. What followed has made the country what it is today. As the *New York Times* reported on June 29th, 1991, “Mr Rao, who was sworn in as Prime Minister last week, has already sent a signal to the nation—as well as the IMF—that India faced no “soft options”, and must open the door to foreign investment, reduce red tape that often cripples initiative and streamline industrial policy.”

It has been revealed that, irrespective of the government that was to assume power, the reforms would have nevertheless been launched. The then Chief Economic Advisor, Mr Deepak Nayyar, and Mr Singh’s predecessor, Mr Yashwant Sinha, both confirmed that any Finance Minister would have read the same budget speech in June 1991. Dr Singh was fortunate to have his name inscribed in golden letters in the annals of India’s destiny. In his budget speech that year, he quoted Victor Hugo, “no power on earth can stop an idea whose time has come”, asserting that “the emergence of India as a major economic power in the world happens to be one such idea. Let the whole world hear it loud and clear.”

In that momentous month of July of 1991, the rupee was devalued by 7 percent and again by 11 percent within the first three days. On 9th July, the Prime Minister addressed the nation, highlighting the need for reforms and promising to remove the cobwebs that had entangled the economy. A New Industrial Policy and a path-breaking Budget defining the course of reforms the country was to embrace were presented together on 24th July. In our universal eulogising of Dr Manmohan Singh as the architect of India’s economic reforms and the man who had brought the country from the brink, we often forget that it was actually Prime Minister Rao, also the Industry Minister, who was the real architect of India’s economic liberalisation. It was his industrial policy that had finally freed the economy from the suffocating License and Permit Raj architecture of the Nehruvian socioeconomic philosophy and polity, built around a complex labyrinth of licenses, permits and controls that dictated every facet of our production and distribution, setting up entry-barriers at every stage, and which built a strong bias towards state ownership of the means of production. It viewed all private enterprises with extreme suspicion, and believed in the domination of the public sector over every economic activity. It abhorred international trade and erected tariff barriers to prevent India’s integration into the global economy, which, in its myopic vision, was capitalist, and hence repugnant. It had infinite trust in the wisdom and ability of its redoubtable bureaucrats and Planning Commission Members to control and direct the market forces towards India's growth.

The defined objectives of the New Industrial Policy were to liberalise industry from all regulatory devices like licenses and controls, enhance support to the small-scale sector, increase competitiveness of industries, ensure the running of public enterprises on business lines, and ensure rapid industrial development in a competitive environment. The cornerstones of this policy were: (1) abolition of all industrial licensing, irrespective of the level of investment, except for certain industries related to security and strategic concerns; (2) de-reservation of industries for the public sector and allowing the private sector in all areas save three–arms and ammunition, atomic energy and rail transport (up until that point, the public sector had exclusive reservation over as many as seventeen sectors); (3) disinvestment of the public sector and its restructuring by giving it more autonomy, closing sick units and reducing the government's stake in it to 26 percent or less; (4) giving free entry to foreign direct investment (FDI) and foreign technology for modernisation, and providing products and services of international standards, through a new FDI policy; and (5) abolition of MRTP[2] clearance for large industries and liberalising industrial location approvals.

There were many other facets of the reform process, each of which contributed to the creation of a competitive industrial climate built around the private, and not the public, sector, by unleashing their immense energy, innovation and entrepreneurship to create wealth and jobs for millions, and by attracting financial capital from across the seven seas. The most pronounced and visible impacts of the economic reforms unleashed in July 1991 have been a drastic fall in our poverty ratio, a dramatic improvement in our growth rates, and a miraculous increase in the inflow of foreign capital, and the consequent build-up of our foreign exchange reserves. India's $356 billion forex reserves in May 2015 were way ahead of the $1.2 billion they had been June 1991, just as the nearly 9 percent growth achieved in 2010-11 was far above the Hindu rate of growth that we had been forced to live with for four decades after independence. But far more impressive is the fact that today the poverty rate by any measure ranges around 20 percent, compared to nearly 50 percent in 1991. That means at least 300 million people have escaped poverty because of the reforms. The India of 2016 is

[2] Under the Monopolies and Restrictive Trade Practices (MRTP) Act, 1969, government permission was needed by all firms with assets above a certain value for carrying out business in India. The Act was repealed finally in 2002.

far more integrated in the global economy and indeed is an economic force to be reckoned with in today's world. The stagnation and despair of the 1990s are things of the past; today it is aspiration and growth. We have indeed left our dismal past well behind us, and all political dispensations universally agree that the reform process that began in 1991 is irreversible.

A Tax Reforms Committee (Chelliah Committee) set up soon afterwards submitted its report in January 1993, recommending the radical simplification of the direct tax structure and the rationalisation of indirect taxes. Following its recommendation to widen the tax net, in the 1994-95 budget, a service tax was introduced on only three services, whose number increased to 119 by 2011-12. Today, barring only a few items on the "negative list", all services are taxable and their total contribution today is about 15 percent of the total tax revenue. The 1997 budget of Mr P. Chidambaram further brought the income tax rates down to 10, 20 and finally 30 percent, a level that has not changed since. The reforms boosted revenue, increased demand and accelerated growth. They also corrected the imbalance in the structure of revenue by raising the share of direct taxes in gross tax revenue from 19 percent in 1990-91 to 54 percent in 2015-16.

However, fiscal consolidation is not only about quantity; significant qualitative improvements were affected by the better management of deficits and debt, through the enactment of the Fiscal Responsibility and Budget Management Act (FRBMA) in 2003, imposing limits on government borrowing, debt and deficits, requiring the fiscal deficit to be reduced to 3 percent of the GDP by 2008-09 and forcing greater transparency of the fiscal operations of the government through statutory disclosures. The 12th Finance Commission (2005-10) forced states to enact their own FRBMAs, and reduce their own deficits and debt; all states had enacted these legislations by 2010. This brought the derailed state finances back on the rails and helped them emerge out of the vicious debt traps they were falling into almost irretrievably. Most states were thus able to generate revenue surpluses that financed their capital outlay, boosting significantly the productive capacities of their economies. The higher growth that we see today is a cumulative result of all these measures.

However, many of these gains were frittered away by short-sighted political decisions. The 5-year plans that allocated resources inefficiently were one; another was the unabated proliferation of the centrally sponsored welfare schemes whose number rose to 360 during the 9th plan (1997-2002). All these followed from the faulty Nehruvian economic model, which was perhaps singularly responsible for India's poverty. Fortunately, all these have now been corrected. The spectre of a Planning Commission no longer haunts the Indian economy, and the number of centrally sponsored schemes has also been slashed to only 28.

Reforms so far have penetrated all key economic areas from industry to fiscal and monetary policies, external trade, foreign investment, finance, and capital markets. However, there is still a whole lot of unfinished issues in education, health, labour, employment, land and agriculture. Agriculture employs 55 percent of our population, but generates only 16 percent of GDP; and nearly 660 million people are thus living on an average per capita income of about ₹30000–a meagre ₹2500 per month, far below the national average. Our Human Development Index is among the lowest in the world, as are our educational standards and health indicators. Delivery of public services remains abysmal in terms of quality and outreach. We need to address these areas now on a war footing, to take advantage of the demographic dividend to avoid a demographic disaster. We can no longer afford gradualism and incrementalism. With the prospects for growth accelerating, enacting a unified Goods and Service Tax (GST) to transform India into a single unified common market will indicate that we are keen on having another tryst with destiny, but the GST will be only the beginning of the second wave of reforms that will truly transform India into a global economic powerhouse.

As the 19th century philosopher, Pierre Joseph Proudhon, said, "The life of man is a battle, that of society a perpetual reformation." We have to continue to reform with ever-greater commitment.

(Afterword: A Goods and Service Tax (GST) was launched throughout India on 1st July 2017, replacing 17 indirect taxes and 13 cesses to which businesses were hitherto subjected. It is a landmark reform expected to transform the economic landscape of India in the next 3-5 years.)

2. DISBAND THE PLANNING COMMISSION[3]

(Whatever little we have achieved was not because, but in spite, of the Planning Commission. It is time to wind it up and bury the five-year plans once and for all.)

Before denouncing the idea of winding up a 63-year old aging institution as preposterous and heretical, let's take a hard look at the facts. The Planning Commission was created by an executive resolution of the Government of India in March 1950. The Commission is not a constitutional body, but it enjoys the extra-constitutional authority to recommend the transfer of almost half of our annual budgetary allocations to states as plan grants every year. It is known to produce voluminous 5-year plans full of fantastic rhetoric and fancy jargon, besides generating a plethora of reports on every conceivable subject. It is also known to entertain the nation from time to time by generating astounding statistics, especially in relation to poverty numbers. Over the decades, the Commission has grown into a mammoth bureaucracy that needs about ₹100 crore of public funds annually to run its report-producing apparatus. For several decades, it has also become the major driving force behind doling out national resources in the form of ill-conceived and poorly-implemented Centrally Sponsored Schemes, through which the powers that be gain access to public funds, and are licensed to misuse these funds for political ends.

There is only one mechanism provided in the Constitution for the devolution of central resources to the states–under Article 275, through the agency of the Finance Commissions. However, the spirit of fiscal federalism in the Constitution was hideously defeated by the creation of the Planning Commission and by giving it exclusive powers, without any constitutional backing, to transfer huge amounts of central resources to states as plan transfers, while limiting the scope of the Finance Commission to only recommending non-plan transfers.

The creation of the Planning Commission necessitated classification of expenditure into "plan" and "non-plan" categories, which was done without

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[3] Originally published in *The Statesman as* "Disband Yojna Bhavan", 24th July, 2014.

any constitutional sanction. The device used for plan transfers is Article 282, meant for dealing with exceptional situations. These transfers are discretionary in nature, vulnerable to being influenced more by political than economic considerations and enabling the Centre to arm-twist any state, given the huge amounts at stake. When this arbitrary discretion of the Centre over the transfer of these plan funds was sought to be limited by making these transfers based on the so-called Gadgil formula, the Centrally Sponsored Scheme was the innovation introduced by the Centre to retain its hold over public funds, and to allow it to misuse these funds on cheap, wasteful and supposedly vote-catcher schemes. The numbers of such schemes have since proliferated unabated on political considerations, creating aberrations in our public finances all the way. Most of these transfers are also made outside the state budgets, so they bypass the usual budgetary, accounting and legislative controls. More than one lakh crore of rupees are thus transferred every year to states outside their budgets, often leading to huge waste and leakages. Plan transfers have now become tied to these fancy schemes and their allocations have taken quantum jumps in recent years. In the process, states' fiscal spaces have shrunk, their autonomy has suffered and their flexibility to launch schemes specific to their needs has almost completely vanished. Other distortions followed as private sector investment naturally went to states with better infrastructure, thereby widening the economic imbalance and disparity among them.

Debate on what the first four and a half decades of our planning since independence have achieved is already passé. Despite high sounding rhetoric like achieving a 'socialistic pattern of society', *'garibi hatao'*, 'growth with stability and distributive justice', 'planning from below', and adoption of fanciful models of growth borrowed from US textbooks, outputs fell, prices soared, unemployment increased, poverty remained undented and growth continued to languish within the Hindu rate of 3.5 percent until 1991 when the economy was poised precariously on the verge of failure. This was, in brief, the story of the first seven plans. However, through it all, as more and more ambitious plans were introduced with ever more allocation of public funds, the bureaucracy of Yojna Bhavan flourished, becoming ever more powerful by doing the bidding of its political masters. Its style of functioning, however, became curiouser and curiouser, increasingly falling out of sync with a modern economy.

It determined what was to be produced in the economy, how much and by what means. After surveying the available resources, a growth target for each sector of the economy was fixed and investments were allocated to each sector, specifying the type of projects and even the specific production techniques as well. Naturally, this led to an economy characterised by extensive regulation, protectionism and a public sector supposed to dominate the ‘commanding heights of the economy’. The government’s size also grew in tandem; under UPA II, we had 53 blessed ministries overseeing every aspect of our lives. The extensive control only fuelled pervasive corruption all around and stifled growth. Vital sectors of the economy were nationalised, and the rest regulated by an elaborate system of licenses and red-tape that inhibited private investment, making the economy reel under this License-Permit Raj. This tyranny of the state only benefited certain entrenched groups but smothered individual entrepreneurship.

In such a collectivised, centralised planned economy, economic democracy, growth and productivity became the ultimate casualties, and the market–the driver of growth in a modern economy–was not allowed to flourish. As Professor P. R. Brahmannda insightfully observed, instead of attacking poverty through a wage-goods model, the authorities chose a number of anti-poverty and pubic distribution measures that were simply fire-fighting exercises with large leakages. The result was a forced impoverishment of the nation that earned it the nickname the “sick man of Asia”. Add to this the growth of black money, an offshoot of corruption, and the heightened inequality and disparity, and the picture of an impending disaster was complete. *Time* magazine quoted a recent McKinsey Global Institute report suggesting that even in 2012, ‘as many as 56 percent of the Indians–some 680 million people– could not afford [the] most basic needs like food, water, housing, sanitation and health care’. The economic reforms came after realisation dawned that it is the market, not the government, that should drive the economy. In recognition of this fact, the 8th Plan stated in its preface that the plan was only “indicative” in nature and that the state could at best be a facilitator for investment by the private sector. However, despite the declining share of public investment post-reforms and promotion of the PPP mode of investment, the role and importance of the Planning Commission did not diminish.

Its role as the most important extra-constitutional allocator of plan resources has long jeopardised centre-state relations. As the Commission on Centre-State Relations observed in its report (March 2010), “Following the introduction of economic reforms in the country, the role of Central planning seemed to have lost much of its relevance. There was a shrinking of the share of the public-sector investment. States saw an opportunity to regain ground lost to the Planning Commission. However, this hope was belied.” As such, the command and control mindset continued.

Command economies invariably tend to get corrupt as, by concentrating economic power and authority, the normal decision-making process is neglected. Plans drawn on the basis of insufficient information were approved and implemented with disastrous results. As growth slowed, inequality was amplified, the rural-urban divide widened, resource allocation to different sectors remained lopsided and ad-hocism reigned supreme. The evils that distress the common man –inflation, poverty and unemployment– remained uncontrolled and unfettered. One is reminded of what Frederick Hayek wrote in *The Road to Serfdom* in 1944: "There could hardly be a more unbearable and more irrational world than one in which the most eminent specialists in each field were allowed to proceed unchecked with the realisation of *their* ideals."

Our country certainly deserves better than to be led by a set of technocrats far removed from the ground realities but wielding unrestrained power and illegitimate authority. It is indeed time to realise that, in a diverse country such as ours, where skill, talent and entrepreneurship are abundantly available, centralised planning does not work. Whatever little we have achieved, it was not because, but in spite, of the Planning Commission. It is time to disband it and bury the 5-year plans once and for all. Responsibility for planning henceforth should be delegated to the elected representatives in respective states, where it logically and rightfully belongs.

(Afterword: The Planning Commission was wound up in August 2014, barely three weeks after this article was published. Subsequently the concept of 5-year plans was abandoned, and even the distinction between plan and non-plan expenditure was later removed. A new institution, the National Institution for Transforming India known as NITI Aayog, was set up under the Chairmanship of the Prime Minister, with the noted economist Dr Arvind Panagarya as Vice Chairman to advise the government on the developmental paths and programs, but without the power to allocate any resources.)

3. CHOICE OF INSTITUTION[4]

(Institutions have a life of their own, and once established, they cannot simply be wished away. If its replacement inherits any of the weaknesses that had made the Planning Commission such a dysfunctional and growth-obstructing institution, it will also continue to corrupt our governance system for a long time, like its predecessor. We ought to be very careful in resurrecting it in another form, without adequate thought and clarity about its intended role and purpose.)

"An institution is the lengthened shadow of one man", Emerson observed. Undoubtedly, the Planning Commission was nurtured under the overstretched shadows of the socialist ideals of Nehru. While the Modi Government's decision to consign it to the dustbin of history was most welcome, one cannot but look with apprehension at the government's consideration to create a replacement institution. Institutions have a life of their own, and once established, they cannot simply be wished away. If its replacement inherits any of the weaknesses that had made the Planning Commission such a dysfunctional and growth-obstructing, institution, it will also continue to corrupt our governance system for a long time. We ought to be very careful in resurrecting it in another form, without adequate thought and clarity about its intended role and purpose.

With its unrestrained powers and authority, the Planning Commission was serving powerful interests that ensured its survival for such a long time. Its abolition is no guarantee that these interests will let go of their privileges so easily; they are more than likely to stage a come-back, albeit in a different guise. This chain needs to be broken irrevocably, before history repeats itself. History is replete with examples of new incarnations of old institutions having inherited the character and shortcomings of those they have replaced. As a nation with an abundance of talent and entrepreneurial capacity, we need to consider if we really need another institution in place of the Planning Commission to guide the nation.

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[4] Originally published in *The Statesman as* "Choice of Techniques", 6th October, 2014.

It may be interesting and instructive to draw from the experiences of other countries in this regard –for example, the BRICS countries India is often grouped with. In the erstwhile Soviet Union, the State Planning Committee, known as Gosplan, was responsible for central economic planning from its inception in 1923, until the dissolution of the Soviet Union in 1991. Gosplan was responsible for the creation and administration of a series of 5-year plans governing the economy of the USSR, much like the Planning Commission in India during 1950-2014, or the State Planning Commission in China during 1952-1998. However, after the break-up of the Soviet Union, the countries that rose from its debris have shifted determinedly from planned economies to market economies by adopting liberalisation, privatisation and globalisation as the only way forward, and some of these countries, like Estonia, have registered GDP growth exceeding 8 percent, transiting into advanced economies. Russia does not have a centralised planning system anymore; the state control that had marked six decades of overwhelming dominance of all investment, production and consumption decisions by the Communist Party is now a nightmare of the past. The country is grappling today with the decrepit legacy of its earlier centralised planning system.

Like the proverbial phoenix, China has risen from the ashes of the Cultural Revolution that ended in 1976. Chinese planning had initially followed the same Soviet model adopted by us. Before the economic reforms began under Deng Xiao-Ping in the late 1970s, private industry was virtually non-existent in China, and industry was dominated by state enterprises, and a rigid and coercive regulatory regime characterised by command and control. All resources–land, labour, raw materials and capital–were provided by the state, which determined the production and distribution plans and their final output. However, since the 1990s, as reforms heralding China's movement towards a market economy took firm hold, planning became more and more indicative, engaging only with projections, trends and bottlenecks, while allowing and encouraging private firms to grow and compete with each other and with state-run enterprises. As the state gradually withdrew from control of economic activities, in 1998, the State Planning Commission was restructured. It was merged with the Commission for Restructuring the Economic System, established in 1982, to direct economic reforms, and was renamed the State Development Planning Commission. In 2006, it was further rechristened the National Development and Reforms Commission (NDRC), omitting the word 'Planning'. This indicated a paradigm-shift to declare that China was no longer a centrally planned economy.

We may recollect that, at the end of the Seventies, India was ahead of China in terms of socioeconomic development. The early years of the present century saw India and China being bracketed together as 'Chindia', when our growth nearly matched China's. However, courtesy of the disastrous decade of UPA rule, China today is light-years ahead of us, and we are unlikely to catch up with it ever again. Nobody recalls 'Chindia' anymore, and comparison with China may be out of place. So, let us see how Brazil has fared.

Until the early 1990s, Brazil was mired in a web of crises, much like our own. About 40 percent of the population was poor, half of them sunk in absolute poverty characterised by severe deprivation of basic human needs. With a Gini coefficient measuring 0.6, it also had one of the highest income inequalities in the world. Poverty, exclusion and backwardness made the country a potential volcano, ready to erupt at any moment. Under its new Constitution of 1988, it undertook extensive reforms through the liberalisation of trade and financial sectors, decentralisation and deregulation, elimination of forex barriers, privatisation and enforcement of fiscal discipline. By bolstering the market to generate income and designing innovative social sector programs like Bolsa Família delivered through a system of conditional cash transfers, it had eliminated absolute poverty within just a decade. By 2012, its per capita income rose to $11690 and its poverty ratio shrunk to only 9 percent of the population. Today, the gap between India and Brazil is as wide as the distance that separates them. In 2012, India's per capita annual income was only $1440, and even at a much lesser poverty line drawn by our now-defunct Planning Commission, India's poor constituted 21.9 percent of the population.

South Africa, of course, was a different story because of its apartheid past that ended only in 1994, when its first democratic elections were held and the African National Congress came to power. It started with a Development and Reforms Program as the primary socioeconomic program, which ultimately was transformed into the New Growth Path (GNP) under the current President, Jacob Zuma. Under GNP, a National Planning Commission (NPC) was set up in 2009 to chart out a roadmap for development with a 20-year horizon. In 2013, it finally came up with the 'National Developmental Plans ~ 2030'. The NPC, however, is not a government entity, but a body of 26 experts from the outside appointed by the President to advise on matters impacting long-term development. It is perhaps too early to assess its impact and efficacy.

A central overarching body is thus not a necessary prerequisite for development. The 73rd Amendment to our Constitution provides for planning at the grassroots level of the villages, and for the consolidation of these plans all the way up. This way, a realistic plan can be made by considering the local needs and addressing the implementation bottlenecks, since people actually responsible for implementation will be involved in this bottom-up planning process. Planning must be a responsibility of states, and cannot be relegated to technocrats and experts on any pretext. It should be the priority and responsibility of the elected representatives who should drive the process through the consensus and involvement of all stakeholders, including experts. The process of consensus-based planning will ensure efficiency of the plan, and involvement of elected representatives will strengthen the accountability mechanism. If a think-tank is imposed upon the nation, the weight of the tank may sometimes become an obstruction, leading again to inertia and what can perhaps be called "fossilism". We need not cling to the old ways after life has completely departed from them.

(Afterword: NITI Aayog was set up in January 2015 in replacement of the Planning Commission. It was to replace the erstwhile one-way flow of policy from the centre states with 'a genuine and continuing partnership', while acknowledging that we need to find and adopt our own strategy for growth without depending on imported models. The stated objectives include providing a framework 'national agenda' to 'foster cooperative federalism through structured support initiatives and mechanisms with the States on a continuous basis, recognizing that strong States make a strong nation'. The Aayog is to develop mechanisms to formulate credible plans at the village level and aggregate these plans progressively at higher levels of government. The 13 objectives also include designing strategic and long-term policies and programs, monitoring and evaluating their implementation and progress, and the identification of required resources for strengthening delivery, while focusing on technology upgradation and capacity building for the implementation of programs and initiatives.

Chaired by the Prime Minister, it has a Governing Council comprising Chief Ministers of all states and Lt. Governors of all Union Territories; this will automatically render the existing National Development Council defunct. However, like its predecessor, NITI Aayog does not have any constitutional status and will therefore remain a think-tank of the government.)

4. EXPENDITURE REFORM[5]

(Niti Aayog should start its work by suggesting that it remove the distinction between plan and non-plan expenditure, and reduce drastically the number of centrally sponsored schemes.)

Hearty congratulations are due to Mr Arvind Panagariya for taking over the reins of Niti Aayog, the reincarnation of the Planning Commission of India, which had dominated and distorted the Indian public financial system for over six decades. As the newly appointed Vice Chairman of its new avatar, Mr Panagariya will have his hands full. We wish him good luck in first cleansing the system of the numerous aberrations that have crept into it over the decades and then driving it towards achieving real growth for the country. Thankfully, he comes with the belief that it is growth that has the potential to lift millions out of poverty by creating wealth and generating employment, as opposed to the sops and doles that formed the guiding philosophy of the previous regime.

The Union Budget 2014-15 had earmarked ₹575,000 crore as planned expenditure on various programs and schemes targeted towards the alleviation of poverty and the creation of employment, and for providing basic public services like education, healthcare, nutrition, drinking water and sanitation to the people of the country. These programs include the 17 flagship welfare schemes like NREGA, on which lakhs of crores of rupees are being spent every year without much visible improvement on the ground. Mr Panagariya will have to transform Niti Aayog into an effective instrument for monitoring and evaluating the implementation of these programs. On this will primarily depend whether NITI Aayog truly becomes what its name suggests: the **N**ational **I**nstitution for **T**ransforming **I**ndia.

Mr Panagariya would do well to begin by dusting off the "Report of the High Level Expert Committee on Efficient Management of Public Expenditure", which was appointed by the UPA government under the Chairmanship of Dr C. Rangarajan. The Committee had submitted its report in July 2011, but the Manmohan Singh Government had preferred to put it

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[5] Originally published in *The Statesman as* "Planning Technique", 31st January, 2015.

in cold-storage, obviously because acting on the report would have meant undoing and unravelling the welfarist agenda of the Congress Party. The most important recommendation in the report was to abolish the distinction between plan and non-plan expenditure. Acting on it would have meant reducing the importance of the Planning Commission by removing the emphasis on welfare-oriented plan schemes of the government. The Planning Commission then would have been rendered powerless to allocate national resources under the guise of these plan schemes and confined only to the task of formulating 5-year plans. The regime, which believed that its electoral fortunes depended entirely on its ability to extend the benefits of doles and subsidies to the widest possible sections of voters, would naturally be loath to act upon such heretical recommendations.

The Rangarajan Committee Report stated: “Over a period of time, several issues have cropped up from the distinction between plan and non-plan, making it dysfunctional and an obstacle in outcome-based budgeting. Therefore, this distinction should go for both union and state budgets. On removal of plan/non-plan distinction in the budget, there should be a fundamental shift in the approach of public expenditure management - from a segmented view of plan and non-plan to a holistic view of expenditure; from a one-year horizon to a multi-year horizon; and from input-based budgeting to the budgeting linked to outputs and outcomes. This shift to a holistic view of expenditure would require, *inter alia*, changes in organisational structure, mandates and processes.” These changes in the organisational structure of agencies concerned with the delivery of developmental programs and the necessary reengineering of the governmental processes and procedures have not yet been implemented.

In fact, the distinction between plan and non-plan expenditure has caused many more problems than mere segmentation of expenditure into the arbitrary ‘plan/non-plan’ classifications, fostering a rather limited and fragmented view of resource allocation. The Report noted that such classification has given rise to an inherent bias in favour of plan expenditure and against non-plan expenditure among the policy makers and officials across all levels, and enforced the notion that plan expenditure was good and non-plan expenditure was bad. This has led to a situation where the non-plan expenditure essential for the maintenance of valuable assets like roads, project assets, buildings and assets for the delivery of public goods and services created under the various plan schemes has systematically been neglected over the years, leading to a progressive deterioration in the quality of public services. “This has also led to a motivation for showing higher plan expenditure and higher plan sizes both at Central and State levels”, the Report observed.

In addition to the poor quality of information that went into the making of successive plans, other problems in budget and accounting classification, inadequate information on transfers of resources to the states, unreliable and dated information on costing of services and the far-from-perfect Central Plan Scheme Monitoring System (CPSMS) generated data have always plagued our system of resource allocation, appraisal and monitoring of expenditure on plan schemes. These problems still remain unresolved and, unless effectively addressed, will continue to cause the sub-optimal utilisation of resources and short-delivery of outcomes. Removing the plan/non-plan distinction and realigning the budget and accounting classification would be the first step towards restoring sanity in our public financial system.

Once this distinction is removed, many things will automatically fall into place, and some others will have to be corrected, like the rationalisation of the endless mechanisms devised to finance the plethora of plan projects. A bewildering variety of these exist now: Normal Central Assistance for central plans and state plans; Additional Central Assistance for centrally sponsored schemes; Additional Central Assistance for externally assisted projects; Additional Central Assistance for programs funded by the Ministry of Finance but implemented by other departments/ministries; Special Central Assistance for special programs; and Advance Central Assistance for special and exceptional situations. In fact, there are so many of these that the normal human brain would struggle to grasp their astounding numbers and complexities. Until 2013-14, there were *only* 137 centrally sponsored schemes. Some semblance of reason was later sought to be brought in by restructuring these into 66 schemes, including the 17 flagship programs with significant outlays, for the remaining years of the ongoing 12th Plan (2012-17). It was also decided to abolish the direct transfer of funds for centrally sponsored schemes to agencies that were implementing these schemes in the states without routing the funds through their budgets. However, much more needs to be done, in terms of further integrating and streamlining these programs by coordinating, monitoring and directing their deliveries towards specific, target-oriented and time-bound outcomes. A suitable accountability architecture also needs to be created.

The newly-formed NITI Aayog is supposed to replace the erstwhile one-way flow of policy from the centre to states by ‘[a] genuine and continuing partnership’. It has been created with 13 laudable objectives, while