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## **Economic Reforms in India: Perpetuating Policy Paralysis**

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### **Abstract**

*This paper examines the current state of economic reforms in India and the phenomenon of policy paralysis leading to almost complete lack of progress on reforms. It studies the qualitative aspects of reforms in India over the last couple of decades and explains how these have changed over time. It discusses the role of coalition governments, an increasingly regressive political economy and lack of strong political leadership in fostering the policy paralysis and expects the latter to prevail in the foreseeable future.*

Two decades have passed since India announced its New Industrial Policy on 24 July 1991. The policy marked India's intention to break free from an inward-looking economic strategy focusing on import substitution and an overarching presence of the state sector in production to encouraging greater private initiative, market-oriented economic principles and closer integration with the world economy. More policies announcing radical changes in economic rules and functions followed. As a result, the structure of the Indian economy has changed considerably during the last 20 years. The most visible outcome of the policy changes, or economic reforms, has been a decisive upward shift in the trajectory of India's economic growth. With a trend rate of 8.5 per cent annual GDP growth recorded during a major part of the last decade, India has been recognised as one of the fastest-growing emerging market economies. The rapid growth made possible by reforms has also resulted in India becoming one of the 10 largest economies in the world<sup>2</sup>.

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<sup>2</sup> India was ranked the 9<sup>th</sup> largest economy in the world for the year 2010 measured in nominal GDP. India's nominal GDP was estimated at US\$1.6 trillion for the year. See *World Economic Outlook (WEO) Database*

Notwithstanding the impressive growth, of late, concerns are mounting over several pending reforms. During the last couple of years, many legislations aiming to introduce fundamental changes in different economic policies have got stuck in the Parliament. It appears that an intriguing ‘policy paralysis’ has afflicted the Indian economy. The affliction is manifesting in the inability of the government to clear major economic bills. The malaise has spread deep within the executive and legislatures making the future of economic reforms in India appear distinctly bleak.

At the last annual India Economic Summit organised by the World Economic Forum (WEF) in Delhi in November 2011, businesses expressed their frustration over the almost complete lack of movement on economic policies<sup>3</sup>. Two main reasons were attributed to the lack of progress on reforms. The first was the government’s preoccupation in warding off various allegations of corruption against its functionaries such as in the allocation of 2G spectrum for telecom service providers and the misappropriation of public resources during the 19<sup>th</sup> Commonwealth Games held in Delhi in October 2010. Social activist Anna Hazare’s success in mobilising large public support last year for an anti-corruption crusade also pushed the government further on the back foot. While these were visibly enough to put economic reforms on the backburner by engaging the government’s attention elsewhere, political differences, within the ruling coalition as well as between the ruling coalition and the opposition have ensured that bills proposing major economic changes have got stuck in the Parliament. Even the Finance Minister has pointed to differences in political opinion in the Parliament as the main hurdle in implementing policy reforms<sup>4</sup>.

This paper examines the current state of reforms in India for obtaining clearer insights on the lack of progress on economic reforms and the phenomenon of policy paralysis. It studies the qualitative aspects of reforms introduced in India over the last couple of decades and explains how these have changed over time. It deliberates on whether coalition governments are the main reason behind the policy paralysis and tries to determine the future prospects of economic reforms in India.

## **Economic Reforms in India: Past and Present**

India’s economic policy reforms, till now, can be grouped into four periods according to their distinct characteristics. These are: 1) 1991-1994 2) 1995-2000 3) 2001-2003 and 4) 2004-2011.

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September 2011, International Monetary Fund (IMF). <http://www.imf.org/external/pubs/ft/weo/2011>. Accessed on 9 March 2012.

<sup>3</sup> ‘End Policy Paralysis: India Inc’, The Times of India, 14 November 2011; <http://timesofindia.indiatimes.com/business/india-business/End-policy-paralysis-India-Inc>. Accessed on 7 March 2012.

<sup>4</sup> ‘Policy Paralysis in South Asia; Indian growth to slow: World Bank’, DNA, 18 January, 2012; [http://www.dnaindia.com/money/report\\_policy-paralysis-in-south-asia-indian-growth-to-slow-world-bank\\_1639240](http://www.dnaindia.com/money/report_policy-paralysis-in-south-asia-indian-growth-to-slow-world-bank_1639240). Accessed on 9 March 2012.

- 1) 1991-1994: The first 'burst' of economic reforms in India saw sweeping changes in industrial, external sector and financial market policies. There were also moves to introduce fiscal consolidation in central government finances by cutting subsidies, selling equities of public sector enterprises and introducing voluntary retirement schemes for retrenching labour. The economy acquired a marked outward-oriented look with foreign investment policies becoming more liberal, tariffs being slashed on imports, the exchange rate becoming more market-determined and the Indian Rupee becoming fully convertible in current account transactions. The external sector crisis of 1991 provided a strong ground for initiating several radical measures. It is noticeable that most of the reforms initiated involved changes in economic policies in areas exclusively within the domain of the Central government. There were hardly any reforms in areas that are 'state' subjects as mandated by the Indian constitution or 'concurrent' subjects that are joint responsibilities of the Centre and states. The early reforms did not extend to land, labour, education, health or even management of infrastructure, which involve a bigger role of states.
- 2) 1995-2000: Reforms ran out of steam after the first three years from their introduction with several factors contributing to the halt. The initial euphoria following relaxation of controls on production, trade and financial transactions resulted in sharp buoyancy in the stock market. Soon after, outbreak of manipulative practices led to heavy decline in market capitalisation and large losses of investor wealth highlighting the lack of effective regulation<sup>5</sup>. From 1996 onward, the Indian economy moved into a moderate growth phase as investments suffered from excess capacity created earlier and high interest rates. Matters were complicated by a series of exogenous shocks including the catastrophic cyclone in Odisha (1997), imposition of sanctions following India's nuclear weapon tests at Pokhran (1998), the Kargil conflict (1999) and the Gujarat earthquake (2000). The sluggish pace of reforms during this period can be attributed to these shocks as well as frequent changes in government produced by short-lived regimes<sup>6</sup>. Nonetheless, there were still some attempts at introducing major economic changes. Notable among these were direct and indirect tax restructuring and fiscal consolidation measures announced in the 'Dream Budget' for 1997-98 and the repeal of the Urban Land Ceiling & Regulation Act (ULCRA),

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<sup>5</sup> The infamous stock market scandal triggered by 'big bull' Harshad Mehta broke out in late 1992 and dampened the markets heavily from late 1993/early 1994 onward.

<sup>6</sup> The 1996 Parliament elections produced a fractured mandate which saw the Bharatiya Janata Party (BJP) led by Atal Bihari Vajpayee coming to office for barely a fortnight in May 1996. The failure of the government to mobilize requisite majority in the Lower House of the Parliament (Lok Sabha) led to entry of the United Front government under H.D. Deve Gowda. This government lasted for only 10 months and was replaced by another edition of the United Front coalition headed by I.K.Gujral in April 1997. This government too could not last for a year forcing fresh elections in early 1998. The elections led to the BJP-led National Democratic Alliance (NDA) assuming power with Vajpayee as the Prime Minister. The NDA lost majority after the withdrawal of support by one of the coalition members forcing elections in September 1999. The latter returned the NDA to power and the coalition continued in office till May 2004.

introduction of a new Competition Law, establishing an Expenditure Reforms Commission (ERC) and bringing down government equity in non-strategic public enterprises to 26 per cent, which were announced in the Union Budgets of 1998-99, 1999-2000 and 2000-01 respectively<sup>7</sup>. Another notable development was the establishment of the Telecom Regulatory Authority of India (TRAI) in 1997.

- 3) 2001-2003: Exactly a decade after the first burst of reforms, followed the second. This period was characterised by introduction of several policies that could be called the 'second generation' of economic reforms in India. Reforms during this period addressed many policies in areas involving coordination between the Centre and states. Two of the most notable reforms were the introduction of the state value added tax (VAT) and enactment of the Fiscal Responsibility and Budget Management (FRBM) legislations, both for the Centre and individual states. At the same time, efforts were made to introduce important regulatory changes in critical infrastructure services like electricity and telecommunications. The period witnessed the beginning of privatisation of electricity distribution services in states through establishment of state electricity regulatory commissions (SERC) authorised to set electricity tariffs. These reforms were consistent with a similar regulatory structure for telecom established through the TRAI. Fiscal consolidation was given a further boost through introduction of pension reforms. At the same time, economic growth was actively encouraged by sweeping liberalisation of the foreign direct investment (FDI) regime. Several public sector enterprises were taken up for strategic sales, which not only implied dilution of government equity, but also surrender of state ownership.
- 4) 2004-2011: The latest and on-going phase of economic reforms in India has gradually seen the process running into considerable difficulties and long delays in implementation. The current period has tended to impart a qualitatively different approach to reforms by focusing on inclusive growth and a rights-based approach. Recognising that reforms need to address priorities of all sections of the society for making India's growth broad-based and economic changes politically acceptable<sup>8</sup>, the emphasis has been on empowering rights holders by enacting appropriate legislations and ensuring that institutions providing public goods fulfil rights of individuals. This has led to enactment of landmark legislations such as the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA), the Right to Information (RTI) Act

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<sup>7</sup> The Union Budget for 1997-98 was presented by Mr P Chidambaram, the then Finance Minister in the United Front government. It was hailed as a 'dream budget' for outlining a road map for future economic reforms and the progressive fiscal restructuring measures. The budgets for 1998-99, 1999-00 and 2000-01 were presented by Mr Yashwant Sinha, the then Finance Minister in the NDA government.

<sup>8</sup> The NDA's poor show in the 2004 general elections was explained by many as a result of its overt emphasis on 'India Shining' – a media campaign projecting India as a robust and vibrant economy due to reforms. It was felt that only selected communities had benefitted from reforms and the campaign aroused the angst of those who had not and whose ire translated into votes against the NDA. The incumbent United Progressive Alliance (UPA) government, right from the beginning of its tenure, focused on reforms with a 'human face' for selling reforms in as politically palatable a manner as possible.

and the Forest Rights Act. Other economic legislations inspired by the rights-based approach like the Food Subsidy Bill, the Land Acquisition, Resettlement and Rehabilitation (LARR) Bill, the Right of Children to Free and Compulsory Education Bill, and the National Identification Authority of India Bill, have been introduced in the Parliament. Most of these legislations are facing delays in passage. There are also other legislations proposing major economic changes such as the Insurance Laws Bill, The Companies Bill, The Foreign Educational Institutions Bill, The Direct Taxes Code Bill, The Mines and Minerals (Development and Regulation) Bill, The Prevention of Money Laundering Bill, The Pension Fund Regulatory and Development Authority Bill and The Banking Laws Bill. These bills are also stuck in the Parliament. While it is expected that legislations emphasising squarely on the rights-based approach such as the food security and land acquisition bills will be debated more extensively by the legislature and thereby face delays, it is not clear why less controversial and more techno-economic legislations like insurance, direct taxes and prevention of money laundering bills are getting stuck.

A close look at the nature of economic reforms introduced during the early and later parts of the last two decades shows that those undertaken in the early 1990s focused more on policies in final product markets as opposed to policies governing factors of production. Industrial policy reforms reduced the scope of industrial licenses, freed industries reserved exclusively for the public sector, slashed the list of manufactures reserved for small scale producers, reduced tariffs on imports and allowed entry of foreign capital in domestic production. These were all aimed at augmenting capacities in production of final goods. Scant reforms were directed at factor markets like land and labour. Indeed, capital market was the only factor market to benefit from India's early reforms. This was because it was expected to help India's new entrepreneurs in mobilizing resources. It was also expected to serve as a conduit for channelizing idle physical savings of households into financial savings, which could be utilized for investment purposes. It must be noted though that the more far-reaching reforms in capital markets, particularly for institutionalizing effective regulations, occurred in the late 1990s. Though the Securities and Exchange Board of India (SEBI) was set up in 1992, it obtained statutory powers and became the regulator of capital markets only in 1998.

An implication of targeting reforms towards product markets was that the emphasis was on changing policies pertaining mostly to economic subjects within the administrative domain of the Centre rather than states. Part XI of the Indian Constitution divides subjects between the Centre and States in terms of their exclusive responsibilities to legislate. The Union List has 96 subjects on which the Parliament can exclusively legislate, while the State List has 61 items. There is also a Concurrent list of 47 items where the Centre and states can legislate jointly<sup>9</sup>. Subjects like external trade and commerce, stock exchanges and futures markets,

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<sup>9</sup> Article 246 in the Seventh Schedule of the Indian Constitution illustrates the Union List, State List and the Concurrent List. See *The Constitution of India* (as modified up to the 1<sup>st</sup> December 2007), Government of

industries, customs duties, excise duties, corporation tax, and capital gains tax, which witnessed maximum reforms during the early years, are all in the Union list. Indeed, reforms were conspicuous by their absence in agriculture, land and mines, which are in the State list, and are also distinct in terms of relatively slow progress in education, electricity and industrial and commercial disputes, which belong to the Concurrent list. It must be noted that on subjects like agriculture, the Centre can only try to persuade, or at best engineer a consensus among states for taking appropriate policies. It cannot step in to design policies on behalf of the states. With critical factor markets such as labour and land figuring on the state list, there is little surprise in these having remained outside the scope of reforms in the early years. Clearly, consensus among India's Centre and states on reforms has not always been forthcoming, except in certain segments of government finance, as witnessed through the introduction of the VAT and state FRBMs.

Going by the two sub-phases most intensive in reforms, it is noticeable that both periods – 1991-1994 and 2001-2003 – were marked by relatively low economic growth and deceleration in economic activity. The year 1991-92 recorded GDP growth of only 1.4 per cent, which was not only an almost 10 percentage point drop from a high of 10.2 per cent in 1988-89, but was also the lowest GDP growth recorded since 1979-80. The low growth was due to the precarious circumstances in the economy, particularly the severe balance of payments (BOP) difficulties, which at a stage had brought down India's foreign exchange reserves to a level where it could afford barely a fortnight's imports. On the other hand, during early years of the last decade, there were two years – 2000-01 and 2002-03 – when GDP growth was as low as 4.4 per cent and 3.8 per cent respectively. Episodes of low economic growth or depressed economic activity could well be conducive to not only launching of economic reforms, but also hastening their pace. Indeed, in the Indian context, bad economic times could be good excuses for moving ahead on reforms without worrying much about their political fallout.

### **Policy Paralysis: Are Coalition Governments the Main Reason?**

On 29 February 2012, the Central Statistical Organisation (CSO) announced the latest GDP growth rate for the Indian economy. Estimated at 6.1 per cent for the October – December quarter of the financial year 2011-12, the third quarter GDP growth shows a marked decline from 7.7 per cent in first quarter (April-June) and 6.9 per cent in the second quarter (July-August)<sup>10</sup>. The number has raised concerns over whether the Indian economy is entering a period of moderate growth and economic activity. The latest GDP growth is more than a two percentage point drop from a robust 8.3 per cent recorded in the third quarter of 2010-11. The rather disappointing growth rate has reignited discussions on why the Indian economy is

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India, Ministry of Law and Justice; page no. 315-329; <http://lawmin.nic.in/coi/SEVENTH-SCHEDULE.pdf>. Accessed on 8 March 2012.

<sup>10</sup> 'Estimates of Gross Domestic Product for the Third Quarter (October-December) of 2011-12' Press Note, Press Information Bureau (PIB), Government of India; 29 February 2012; [http://mospi.nic.in/Mospi\\_New/upload/nad\\_pr\\_29feb11.pdf](http://mospi.nic.in/Mospi_New/upload/nad_pr_29feb11.pdf). Accessed on 6 March 2012.

gradually moving into low gear. In this regard, the inertia on economic policies being referred to as policy paralysis, is being held chiefly responsible.

Worries over policy paralysis have crossed India to figure in global discourses on the prospects of the Indian economy. Discussing South Asia's economic performance in its latest analysis of global economic prospects<sup>11</sup>, the World Bank attributes delays and uncertainty surrounding implementation of economic reforms as one of the key factors behind the decline in investment in India. In the same analysis, the World Bank projects a slowdown in South Asia's GDP growth for the year 2012 due to deceleration in investment produced by domestic policy paralysis and uncertainty about regulatory reforms, inter alia. South Asia's economic prospects are fundamentally determined by those of India's and there is little doubt over the reference being directed at India.

As mentioned earlier, the Finance Minister has indicated that divergence in political opinions in the Parliament is holding up progress on reforms by preventing passage of economic bills. This situation would probably not have arisen had the Congress – the single largest party in the ruling coalition – had majorities in both houses, which would have enabled it to pass bills easily. The fact that the Congress is repeatedly encountering opposition in passing bills has led to the belief that reforms are difficult to implement by coalition governments.

Costs of running coalition governments can certainly be high for the single largest party in the alliance. Both the Congress and the BJP have experienced this on several occasions. One of the biggest costs is satisfying the demand of smaller partners extracted in return for their support. Indeed, this has been identified as one of the biggest challenges facing political governance in modern India<sup>12</sup>. The dependence of the leading party in the coalition on smaller partners and this knowledge on part of the latter encourages them to pressurise the former in two ways. The first is in demanding key portfolios in the cabinet. Smaller parties try to make the most of the opportunity of being a part of the central government by maximising the political capital that can be derived from managing key ministries such as railways and telecommunications. In India, ministries like the railways and telecommunications have been held by the smaller members in the ruling coalition for several years now<sup>13</sup>. The railways –the largest departmental undertaking of the Indian state – have been used by the smaller parties for extending various services (e.g. new rail links, more

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<sup>11</sup> *Global Economic Prospects January 2012, South Asia Annex*; [http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1322593305595/8287139-1326374900917/GEP12a\\_SAR\\_Regional\\_Annex.pdf](http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1322593305595/8287139-1326374900917/GEP12a_SAR_Regional_Annex.pdf). Accessed on 7 March 2012.

<sup>12</sup> Instability and policy incoherence produced by multi-party governments is cited as a major reason behind India's likely failure to become a superpower. See 'Will India Become a Superpower?', Ramchandra Guha, London School of Economics, UK; <http://www2.lse.ac.uk/IDEAS/publications/reports/pdf/SR010/guha.pdf>. Accessed on 10 March 2012

<sup>13</sup> Incumbent railways ministers such as Rambilas Paswan, Nitish Kumar, Lalu Prasad Yadav, Mamata Banerjee, Dinesh Trivedi and Mukul Roy belong to small/regional parties like the Janata Dal (JD), Rashtriya Janata Dal (RJD) and the Trinamool Congress (TMC). The Dravida Munnetra Kazhagam (DMK), another critical part of the Congress-led UPA coalition, has held the telecommunications portfolio for a long time.

employment) to their regional constituencies. Operational efficiency and financial situation of the railways has progressively deteriorated over the years as none of the ministers from smaller parties have been keen on introducing corrective measures, which could be unpopular with people, such as revising passenger tariffs<sup>14</sup>. Telecommunications, another attractive portfolio for smaller parties, has turned from being India's most successful example of competition and reforms to one offering ample scope for rent-seeking<sup>15</sup>. The second way in which the smaller parties extract the price for preserving the coalition is by blocking legislations, which they suspect could be politically damaging, at least in the short term. Blocking these bills in the Parliament helps them to earn political mileage as they advertise to their local constituencies their sincerity and earnestness in preventing adoption of 'anti-people' policies. The Trinamool Congress (TMC)'s resistance to legislations on allowing majority foreign equity in domestic multi-brand retail operation and the pension bill are relevant examples.

There is no denying that the economic cost of coalition governments is becoming increasingly high given the wastage of key ministries and delays in implementing economic policies. But before attributing the policy paralysis entirely to coalition governments and divergence in political opinions, it is important to note that coalition governments are inevitable outcomes of the democratic process. Mandates in Indian elections have become increasingly fractured leading to outcomes where the large national parties – the Congress and the BJP – have no alternative to soliciting support of smaller regional partners. For almost two decades now, no national party in India has been returned to the Lok Sabha with a clear majority of 50 per cent of the total seats. As a result, coalitions revolving round the Congress and the BJP have become common structures of Central governments and would probably continue to be so in the foreseeable future.

While reforms might be difficult to push through coalitions, they are certainly not impossible either. During the period 2001-2003, several reforms occurred in spite of the ruling NDA regime being a coalition. Similarly, during the first couple of years of the current UPA government's first tenure, the momentum on economic policies was not lost. It is therefore incorrect to attribute the policy paralysis only to coalition governments.

A more realistic explanation of the slow progress of economic reforms probably lies in the fact that several stakeholders in the economy continue to remain unconvinced about the benefits of greater competition and integration with the world economy. These are typically the interest groups and industry lobbies that continue to benefit from absence of reforms. The enormous unorganised retail trade in the country is wary of greater competition and strongly opposed to entry of foreign retailers. So are the large numbers of small informal sector low-

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<sup>14</sup> Dinesh Trivedi was ousted by the TMC for proposing moderate hikes in passenger tariffs for the railway budget of 2012-13.

<sup>15</sup> The scandal involving the allocation of 2G spectrum for telecom service providers is probably the biggest case of economic corruption in India in the post-reform period.



end manufacturers whose products are procured and marketed by the unorganised retail trade without stringent certification or quality requirements. Both the unorganised retailers as well as the small manufacturers enjoy considerable clout in influencing perceptions of political parties in opposing policies on foreign entry in retail. Similarly, employee federations affiliated to the mainstream political parties are averse to introduction of greater competition in the state-dominated banking and insurance industries. There are still many producer lobbies in India who clamour for protection from imports citing the 'infant industry' argument<sup>16</sup>. These groups have succeeded in drawing up large negative lists during India's external trade negotiations with other countries. All these groups and lobbies with interests aligned against market-based reforms find quick support from small parties in coalitions as they are able to plead their cases to these parties in a politically gainful manner. At the same time, the urge on part of opposition parties in the Parliament to secure quick political mileage encourages them to adopt postures on particular policies that are at variance with their earlier postures on these issues when they were in the government. For example, the BJP opposed foreign entry in retail though it had initiated the first moves in this respect in 2003. And finally the ruling parties are not committed to economic policies to the extent that they are unwilling to put additional efforts in forging consensus on major issues. This is particularly true of the Congress, which in recent months has been so low on political capital due to charges of corruption and inefficiency that it has refrained from achieving cross-party consensus on certain policies, if the initial efforts have been unsuccessful. The success of various lobbies with defensive interests in gaining support from an increasingly myopic spectrum of political parties focused on short-term political gains through populist measures has led to inertia and lack of movement on economic reforms.

Ironically, it was the Congress which ushered in economic reforms in India in the 1990s. It is paradoxical that the policy paralysis has set in at a time when the Congress is at the helm of affairs and Dr Manmohan Singh, the architect of India's reforms, is heading the government. It is becoming increasingly clear that the current leadership of the Congress party is incapable of taking a bullish posture on reforms by biting the political bullet as Mr P V Narasimha Rao had done in the early 1990s. The lack of political courage in pursuing reforms has made the opposition from smaller parties and defensive interest groups appear more herculean than it actually is.

### **Would Reforms Happen?**

There is little doubt that the Indian economy will continue to grow at 6-7 per cent per year unless affected by serious exogenous shocks. This trend rate of growth, while lower than the trajectory achieved during the earlier decade, will still be higher than that of most major

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<sup>16</sup> See 'India's Foreign Investment Policy : Achievements and Inadequacies', A Palit (2009), *Asie Visions* 18, The Institut Francais des Relations Internationales (IFRI), Paris, for more details on the nature of opposition to entry of foreign investment in India; [http://www.ifri.org/files/centre\\_asie/AV18\\_Palit\\_final.pdf](http://www.ifri.org/files/centre_asie/AV18_Palit_final.pdf). Accessed on 10 March 2012.

economies in the world. This might be taken by policymakers as a ‘comfortable’ growth trajectory, one which need not be upped further till the global economic situation corrects and creates favourable conditions for a step-up in India’s GDP growth. If that is so, then there is little possibility of the policy paralysis ending. The Central government is unlikely to push that ‘extra’ effort behind reforms given that the economy is as it is growing at almost seven per cent despite the delays in clearing legislations<sup>17</sup>. Indeed, the current GDP growth rate is not as low as those witnessed in the early 1990s, or the early years of the last decade, for motivating a ‘big push’ on reforms. Furthermore, with the latest assembly election results<sup>18</sup> being particularly favourable for the ruling Congress coalition and the next Parliament elections barely a couple of years away, the Congress is unlikely to antagonise current and potential political partners by making much noise on ‘difficult’ reforms. As it is, the Congress leadership has been exceptionally careful in heeding sentiments of alliance partners, irrespective of the economic costs it involves, as was again evident during the recent saga over removal of the Railway minister on hiking passenger tariffs after almost a decade.

For India’s dynamic modern entrepreneur class, continuation of policy paralysis is bad news. So it is for foreign investors influenced by major global investment confidence indices, which assign high ranks to India<sup>19</sup>. Foreign investors are clearly at a loss to figure out why a US\$1.6 trillion economy capable of growing at eight per cent or more annually, is unable to pass bills in its Parliament. For outsiders, the phenomenon is even more puzzling because the very fact that the government is introducing the legislations indicates that it believes in the changes it is proposing. Yet the changes remain proposed only on paper and fail to become rules and laws. Very rarely does one come across governments which can only propose and not dispose.

Business and industry is also becoming increasingly worried over the ‘costs’ that certain proposed legislations imply for them. The compensations suggested in the new land acquisition bill and the mines and minerals bill for displaced communities is high enough to discourage industries from fresh investments. The government’s emphasis on the rights-based approach to development and the effort to ensure that economic laws are drafted accordingly has probably created a situation where regulations have begun becoming disincentives for industry. Without disputing the virtues of the rights-based approach, the government needs to be careful in not scaring away investors. Indeed, many investors would not like the land acquisition and mining bills to be eventually passed in their proposed forms. To that extent, paradoxically, the policy paralysis offers them some momentary respite.

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<sup>17</sup> The latest Union Budget (2012-13) pegs GDP growth at 6.9 per cent for 2011-12.

<sup>18</sup> Elections were held in February-March 2012 in Uttar Pradesh, Punjab, Uttarakhand, Goa and Manipur. Congress fared poorly in Uttar Pradesh – India’s largest state – and also lost in Punjab, another key state in Northern India.

<sup>19</sup> The A.T. Kearney FDI Confidence Index measuring attractiveness of different locations from the perspective of long term FDI has continued to rank India as the second most attractive location since 2007. The 2012 index ranks India second again, after China, and ahead of Brazil, US, Germany, Australia, Singapore, United Kingdom, Malaysia and Indonesia; <http://www.atkearney.com/index.php/Publications/foreign-direct-investment-confidence-index.html>. Accessed on 11 March 2012.

The inherent contradiction between the rights-based approach and fiscal consolidation has begun looming large over India's economic prospects. These are reflected in concerns over fiscal implications of the MGNREGS (Mahatma Gandhi National Rural Employment Guarantee Scheme) and the proposed food subsidy bill. While the MGNREGS has ensured income growth for economically marginal rural households, both the quantity and quality of infrastructure assets created from such cash transfers in rural India are being debated. The programme is also being suspected to have cramped supply of labour for industrial enterprises since opportunity cost of migrating to urban areas for industrial employment is now being perceived as too high by rural households given their assured incomes. The food subsidy bill entails an aggregate outlay of around US\$29 billion, which is more than double the budgeted food subsidy for the financial year 2011-12<sup>20</sup>. One can hardly help sympathising with the Finance Minister who has to satiate the voracious appetites of these various schemes while still trying to adhere to the FRBM targets by pulling down an alarming fiscal deficit touching six per cent of GDP.

Finally, discussions on economic reforms in India often tend to focus on actions by the Central Government and miss out on reforms by individual states. In this respect, though, the situation in recent years has not been particularly promising. Most Indian states, like the Centre, appear to be following 'hands off' policies on reforms and are not showing vigour and foresight in implementing reforms. Perhaps, reforms by 'stealth' – an influential concept in the political economy literature on India's reforms that alludes to reforms being implemented skilfully and cautiously (like a stealth bomber) without affecting political sensitivities<sup>21</sup> – has become redundant in an era of pervasive populism shrouding the country's political economy. Virtues of economic reforms have become distinctly marginal to those of ad-hoc populism so much so that political parties and personalities are uninterested in pushing reforms even stealthily or surreptitiously. Given the circumstances, policy paralysis and stunted progress on economic reforms appears inevitable.

[Keywords: Economic reforms, reforms, India, economic policy, policy paralysis, reforms policy]

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<sup>20</sup> 'India's Food Subsidy Bill: A Sustainable Option', Rajiv Kumar and Soumya Kanti Ghosh, *East Asia Forum*, 7 March 2012; <http://www.eastasiaforum.org/2012/03/07/india-s-food-subsidy-bill-a-sustainable-option/>. Accessed on 28 March 2012.

<sup>21</sup> See 'Political skills: Introducing Reforms by Stealth', Chapter 6, *Democratic Politics and Economic Reforms in India*, Rob Jenkins (1999), Cambridge University Press, for a detailed analysis of reforms by stealth.