

# BTI 2010 | India Country Report

<b>Status Index</b>	1-10	<b>7.33</b>	# 26 of 128	
Democracy	1-10	8.20	# 20 of 128	➔
Market Economy	1-10	6.46	# 42 of 128	➔
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scale: 1 (lowest) to 10 (highest)    score    rank    trend

This report is part of the Transformation Index (BTI) 2010. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 128 transformation and developing countries are evaluated.

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## Key Indicators

Population	mn.	1124.8	HDI	0.61	GDP p.c.	\$	2753
Pop. growth	% p.a.	1.3	HDI rank of 182	134	Gini Index		36.8
Life expectancy	years	65	UN Education Index	0.64	Poverty <sup>2</sup>	%	75.6
Urban population	%	29.3	Gender equality <sup>1</sup>	-	Aid per capita	\$	1.2

Sources: UNDP, Human Development Report 2009 | The World Bank, World Development Indicators 2009.

Footnotes: (1) Gender Empowerment Measure (GEM). (2) Percentage of population living on less than \$2 a day.

## Executive Summary

India can be regarded as a consolidated, inclusive democracy with no extra-constitutional veto players. The most glaring deficits in this relatively bright picture include an understaffed and therefore sluggish judicial system, corruption, politically partial police forces, and the weak protection of civil rights in tension-prone areas. Since 1991, India has seen a far-reaching, rapid and successful transformation of its economic order, making the country one of the most dynamic in the world. This process was driven by high levels of productivity in services and growing pockets of manufacturing. Agriculture, however, is still lagging behind. There are quite a few areas in need of reform, including most prominently public deficits, unproductive subsidies, a massive infrastructural backlog and the need to bring labor, land and bankruptcy laws in line with international standards.

The Indian government should be lauded for the progress it has made in enhancing democratic governance, especially in terms of securing a monopoly on the legitimate use of power, administrative and bureaucratic efficiency, ensuring an independent judiciary, and facilitating the high esteem of democratic procedures among the population. The government successfully made political and economic processes more inclusive by increasing expenditures for basic education and health, investing in rural infrastructure, and launching a massive employment program in rural districts. Care was also taken to accommodate the grievances of minorities (tribals, Muslims) and to find a negotiated solution for long-standing regional conflicts (Kashmir, North-East India). These efforts were made in parallel with efforts to improve relations with neighbors, especially Pakistan. The Indian government also took the lead in bringing forward regional cooperation by making unilateral concessions. On the economic front, however, there appears to be a stalemate. On the one hand, some economic reforms were not advanced, particularly those regarding privatization, the opening-up of special economic zones, the liberalization of foreign investment and making the currency fully convertible. On the other hand, the government continued to prune fiscal deficits, introduced a non-distorting value-added

tax, reduced tariff rates and pursued conservative monetary policies. Despite these measures, the Indian economy has been hit hard by the global financial crisis. Whereas the state apparatus has been effectively decentralized, the sphere of inclusion in the political process has been expanded, and the elites of formerly disadvantaged groups have been empowered, class and gender gaps nonetheless persist, and regional and personal income distribution has continued to diverge somewhat.

## History and Characteristics of Transformation

India's transformation toward democracy dates back to the introduction of self-governance and suffrage rights during British colonial rule. Nurtured and expanded in independent India, this tradition has been interrupted only once, during the declaration of a state of emergency from 1975 to 1977.

Electoral democracy has long since become the only game in town; even radical political forces abide by its rules and do not seek power through extra-parliamentarian means. Elections are free and fair, civil rights are guaranteed (but circumscribed under certain circumstances), extra-constitutional veto powers are nonexistent, the military is under strict civilian control, the media enjoy considerable freedom of expression and civil society is lively, though it lacks deep roots. Substantive democracy has suffered since independence from limited electoral choices; the Congress Party (INC) dominates at every political level and is able to mobilize and recruit local notables into the party machine. This has come at the expense of those less-privileged and wide-ranging social reforms. India, however, has undergone a dramatic (second) democratic upsurge in the last two decades, as regional organizations have emerged and the lower castes in the follow-up to the Green Revolution. These organizations have been economically empowered and assume positions in the leadership of traditional parties. This democratic growth has, however, led to unstable coalition governments and weakened federal control over the states. It has also meant that secondary powers, such as the Supreme and High Courts, the election commission and the president have become more proactive in carrying out their duties.

After decades of import substitution and state-led industrialization that left considerable room for private enterprises to act as junior partners of the state, India's transformation to a full-fledged market economy is of a more recent origin. A first, hesitant liberalization came into effect in 1985; the severe balance of payments crisis of 1990 – 1991 propelled a complete market-friendly turnaround. The reforms enacted after this crisis have transformed India into a vibrant and dynamic market economy, where only a few sectors are closed to private enterprise and international investment and which has been driven by considerable improvement in factor productivity and the rise of world-class enterprises. There are, however, still considerable reform deficits, most notably outdated labor, land and bankruptcy regulations, lack of progress in

privatization, stubbornly high but slowly declining budget deficits, a low level of public investments, and the consequently unsatisfactory state of public economic and social services.

Since 2004, when a minority government was backed from outside by leftist parties, there has been hardly any progress made in second-generation economic reforms; on the other hand, a range of inclusive social policies were instituted (Education for All, National Rural Health Mission, National Rural Employment Guarantee Scheme, loan waiver for small and medium farmers), some of a more populist character but all intended to make development more broad-based.

## Transformation Status

### I. Democracy

#### 1 | Stateness

There are minor problems of stateness in India. However, the state's monopoly on the use of physical force is incomplete in some rural conflict zones in central India, areas of separatist activity in Kashmir and some small states in North-East India. In these regions, insurgent groups sometimes run a rather circumscribed kind of parallel administration. However, given that militants in these areas do not base their actions on a common perspective or agenda, their activities do not constitute a serious challenge to the polity as a whole.

Monopoly on the use of force

Identification with the nation and the definition of nationality pose problems only in zones of separatist activity where some groups do not consider themselves to be full citizens of India. Less radical groups in these regions would be content with the granting of a generous degree of regional autonomy or by their economic grievances being met. These groups have intermittently signaled that they are prepared to negotiate on these issues, and some have even entered into peace agreements with the government.

State identity

The secular credentials of the country were more or less restored at the national level after the new government took power in late 2004. However, religious groups have attempted to intervene in communal politics at the state level on issues such as "forced" conversions and the slaughtering of cows. Growing violence directed against Christian minorities has not been dealt with decisively. Muslims are often seen as responsible for the terrorist activities of some radical splinter groups. At the same time, the government moved forward in restoring the traditional land and forest rights of tribals. It also set up a commission to look into the social discrimination of Muslims, and earmarked a certain share of new programs for the benefit of scheduled tribes and castes.

No interference of religious dogmas

India inherited an efficient central administration from the colonial government that bases recruitment and promotion on merit. This heritage was undermined to a certain degree by a shift toward increasing reservation quotas for certain sections of

Basic administration

the population and the frequent, politically motivated transfers of officers. These tendencies are even more pronounced at the state level, where administrative organizations are practically colonized by specific political parties. Indian police forces are highly inefficient, politically dependent, prone to corruption, and misuse their power. Criminal conviction rates are therefore low, police atrocities against civilians are frequent, and the government often relies on the army to quell civil disturbances. Changes for the better have nonetheless been observed, as the Supreme Court has mandated that a police commission be established to investigate police corruption, and it has ruled that corrupt officers can be prosecuted without government consent.

## 2 | Political Participation

Since independence, India can boast of a nearly uninterrupted record of general, free and fair elections that have been accompanied by increasing voter turnout (especially among the poor and populations in underdeveloped areas). At the same time, voters have grown increasingly sophisticated and independent. As a consequence, there have been frequent and peaceful transfers of power at the center and in the states. Even in conflict-ridden areas (e.g., Punjab, Kashmir, North-East India) elections lead to political de-escalation, so much so that they have been used explicitly for this purpose. It must be noted, however, that electoral violence at the local level constitutes a significant phenomenon in some areas, but it does not diminish the meaningfulness of national elections.

Free and fair  
elections

There are no extra-constitutional veto powers or political enclaves. The military has always exhibited maximum political restraint; it is under strict civilian control and conceives its role purely in professional terms. The activities of private militia (hired by landowners or vigilant groups in areas of Naxalite activity), some of which were suspended after 2005 by order of the Supreme Court, constitute a minor problem. Civil associations (e.g., unions, employer federations) nearly always act as junior partners of the government. They are fragmented, politically affiliated and rather weak (their occasional militancy notwithstanding). As there are few intermediaries between the government, the parties in power and the people, elected rulers have a nearly unlimited power to govern at large.

Effective power to  
govern

The freedom of association is fully guaranteed, there are no legally complicated processes involved with forming interest groups. Associations, unions, NGOs and social movements proliferate (although association density is moderate). Most of them are politically fragmented, stand upon a weak institutional foundation or act as frontal organizations for specific parties and lack internal democracy. Social movements and NGOs abound and often act as democratic, social or environmental watchdogs, as advocacy agents for less privileged groups or even as intermediaries in communal conflicts. Not all of them are independent of political interference.

Association /  
assembly rights

Strikes and demonstrations are frequent and are only rarely repressed, dissolved or discouraged.

India can boast of a growing circulation of free, discerning and outspoken newspapers of different political shades in all national and regional languages. Nearly every political party, association or social movement is publishing its own mouthpiece. Citizens also have a broad choice among a multitude of state and private television channels reporting non-stop about political developments. If freedom of expression is undermined in rare instances, this has more to do with the influence of radical political or social movements than with state repression.

Freedom of  
expression

### 3 | Rule of Law

While horizontal separation of power is assured, vertical separation had previously been restricted by frequent politically motivated replacement or undermining of state governments. It has been restored in the wake of coalition governments coming to power since the mid-1990s and their dependence on smaller, regional parties. Federalism has also suffered from a multitude of central programs impinging on the sovereignty of state governments and recent efforts to force a reduction of state budget deficits. Control of the executive by the parliament suffers from modest professional competence of parliamentarians, extremely short session periods and lack of data gathering and research support. The judiciary has recently come under considerable attack from the legislative branch, which feels that the courts have been exceeding their authority in interpreting the law. This is, however, more a consequence of legislative “underreach” in defining civil rights.

Separation of  
powers

The Supreme Court enjoys considerable and broad-based competence in the examination of the constitutional correctness of laws and as an appellate body concerning violations of human rights. The court has become rather proactive in recent years in curbing violations of minority rights, upholding administrative accountability and safeguarding the rights of future generations. The independent election commission can boast of a similar record and is today tightly controlling the upkeep of stipulated election codes.

Independent  
judiciary

The courts remain institutionally autonomous, in spite of pressures by the executive, which interferes with judicial nominations and transfers politically unpopular judges. The upper courts recently made an effort to restore their independence in nominations by creating new committees filled predominantly by higher justice officials. The government has also restrained from forming a national justice commission which would have decided on failing or corrupt judges. Understaffing and sluggish judicial operations – which have resulted in a massive number of unfinished judicial proceedings and accused (but not convicted) individuals being held in custody – are the main culprits in restricting the rule of law in India. Laws

and regulations in India tend to be overly detailed and there are low thresholds for initiating and prolonging processes, all of which cause problems. Underprivileged sections of the population shy away from the courts not only because they are not fully aware of their rights, but also because of the high litigation costs.

The misuse of public office is frequent in India. During the review period, such misuse was only intermittently prosecuted, as ministerial consent is required before cases against a given ministry can be filed. In addition, administrative transactions are moderately transparent and public officers still hold considerable discretion in implementing government regulations. The culture of corruption is deeply entrenched in India and has not changed for the better in the last few years. Licenses and government posts are frequently awarded to the highest bidder. As a consequence, India is still listed in the upper/lower range by several international ranking institutions in regard to corrupt practices and regulatory quality. During the period under review, a substantial part of the political class was found to be involved in spectacular corruption cases. The often-cited nexus of politicians, bureaucrats and criminals in India weakened only slightly.

Prosecution of  
office abuse

Civil rights are ensured except in regions where emergency laws prevail. The rights of the underprivileged are, however, circumscribed by the existence of private security forces that act often with impunity, by the unsatisfactory enforcement of relevant protection laws, and a sluggish judicial system fraught with unreasonable delays in criminal cases, and the victimization of the accused during police custody. After the terrorist assaults in Mumbai, the government introduced new legislative proposals to create a National Investigation Agency, special courts for dealing with terrorist activities, and the authority to detain suspects without trial for six months.

Civil rights

#### 4 | Stability of Democratic Institutions

Democratic institutions in India are stable. Nevertheless, state governments are occasionally destabilized for political reasons, multiparty governments in the last decade have been rather unstable (a situation which granted political blackmail power even to minor parties), and parliamentarians often cross the floor to the opposition or to new parties so as to profit personally from new political equations. All of this has delayed or obstructed important constitutional and economic reform projects. Institutional efficiency is also hampered by the large number of tax rates and rebates, and by other provisions allowing discretionary leeway for government officials. Accountability is also hampered by the proliferation of ministries and agencies, a multitude of only modestly coordinated vertical programs implemented by Union states and the fact that financing is insufficiently decentralized to lower tiers. It must be mentioned that the government made a fair attempt to bring most government programs under one sectoral umbrella. It also sought to create model frameworks or agencies for regulating public services and to provide states with

Performance of  
democratic  
institutions

incentives to bring their household in order. With the anti-defection law promulgated in 2004, the rate of floor-crossing has declined somewhat.

Democratic institutions are accepted and held in high esteem by voters, although this does not extend to the police and the parties, both of which are trusted by only very few people.

Commitment to democratic institutions

Even poor people feel that their voting decision carries weight and take pains to register themselves. Democratic competition is the only game in town for most of the population, except for quite miniscule insurgent groups like the Naxalites or separatist groups in Kashmir and North-East India. However, sincere peace negotiations or offers of cultural autonomy could appease some of these splinter groups.

## 5 | Political and Social Integration

The Indian party system is relatively stable, volatility is low and a highly plural society means that the system rewards centrist tendencies. As a result, coalition-building for government is easy. Most parties are nevertheless only weakly institutionalized. Party discipline is low despite measures against floor-crossing. Formal organizational structure and programmatic appeals are mostly replaced by informal procedures, factionalism, clientelism and mobilization along ascriptive identities. The communist parties and the BJP with its disciplined frontal organizations fare are only slightly better. The poorly institutionalized character of Indian parties does not hinder their effectiveness as election machines and as political agenda-setters.

Party system

Association membership in India numbers in the millions, but interest groups are rather weak and fragmented across ideological and party lines. They often fight against each other instead of against their opponents. This is also why labor relations are rather conflict-prone. Because of the longstanding dominant economic role of the state, labor unions and employers' federations are only partly autonomous. Economic liberalization brought the emergence of new, professional associations. Social movements, such as those addressing women's issues, environmental issues or human rights concerns have become more visible and assertive. They are dominated by members of the middle class, but often act as advocacy associations for the lower strata. Civil society is not deeply embedded, as only a small percentage of citizens are members of any association. Nevertheless civil society has a growing influence on the political agenda and often a positive influence on intra- and interethnic harmony.

Interest groups

Most people prefer a democratic system to any alternative system of government. Unfortunately, this does not always extend to tolerance for dissent or respect for

Consent to democratic norms

religious and cultural diversity. There is also a substantial part of the population that sympathizes with authoritarian ways of leadership and is not averse to imposing its will on opponents by violent means.

Associational activities are multifaceted, as India is among those countries with the largest number of associations and NGOs. Those not (or only weakly) associated with political institutions have become quite vocal and assertive, and have taken on important issues neglected by state agencies or parties (e.g., violence against women, violation of civil rights, transparency in government, protecting the environment). The government now often takes their views seriously and has increased considerably their participation in the planning, implementation and monitoring of government schemes.

Associational  
activities

## II. Market Economy

### 6 | Level of Socioeconomic Development

According to the commonly used development indicators, India is still regarded as a lower-income country, albeit progressing at a rapid pace, second only to China. Its development level, measured by the HDI, nevertheless neither assures every citizen's basic needs nor creates freedom of choice for everybody. India is still the country with the largest number of people living in absolute poverty (around 24% of the population). The incidence rate of poverty has declined since the mid 1970s but has become increasingly concentrated in geographic and social terms. Progress in development was therefore uneven, and differences in social indicators between Union states increased in the 1990s. Poverty and social exclusion is concentrated in some sectors (e.g., agriculture, informal sector), social groups (e.g., lower castes, tribals, Muslims) and Union states with small endowments, weak reform records and poor governance. Despite measures to eradicate poverty and assertive action taken on behalf of the underprivileged, there is no equal opportunity.

Socioeconomic  
barriers

Economic indicators		2004	2005	2006	2007
GDP	\$ mn.	700920.7	810151.4	914891.9	<b>1176890.3</b>
Growth of GDP	%	8.3	9.4	9.7	<b>9.1</b>
Inflation (CPI)	%	3.8	4.2	5.8	<b>6.4</b>
Unemployment	%	5.0	-	-	-
Foreign direct investment	% of GDP	0.8	0.8	1.9	<b>2.0</b>
Export growth	%	28.1	14.8	18.9	<b>7.5</b>
Import growth	%	16.0	45.6	24.5	<b>7.7</b>
Current account balance	\$ mn.	780.2	-7835.4	-9415.3	-
Public debt	\$ mn.	89027.6	80302.7	63798.8	<b>74419.0</b>
External debt	\$ mn.	124399.1	123144.9	175540.3	<b>220956.5</b>
Total debt service	% of GNI	2.8	3.0	2.0	<b>3.5</b>
Cash surplus or deficit	% of GDP	-3.3	-3.3	-2.7	<b>-1.4</b>
Tax Revenue	% of GDP	9.7	10.2	11.3	<b>11.6</b>
Government consumption	% of GDP	10.7	10.5	10.2	<b>10.1</b>
Public expnd. on edu.	% of GDP	3.4	3.2	-	-
Public expnd. on health	% of GDP	0.8	0.9	0.9	-
R&D expenditure	% of GDP	0.7	0.8	0.8	<b>0.8</b>
Military expenditure	% of GDP	2.9	2.8	2.6	<b>2.5</b>

Sources: The World Bank, World Development Indicators 2009 | UNESCO Institute for Statistics | International Labour Organization, Key Indicators of the Labour Market Database | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security.

## 7 | Organization of the Market and Competition

Market competition is assured in most sectors of the economy. Once massive, regulation density has been markedly reduced in many sectors, with the exception of agriculture and the labor, housing and land markets. Business transactions with the administration are however still cumbersome, costly and time-consuming. Several hundred products are still reserved for exclusive production by the small-scale sector, obstructing their employment potential. The regulation of foreign and big local companies was dismantled. The investment regime now ranks among the most liberal in Asia.

Market-based  
competition

Sector concentration indices are still high, despite government endeavors to the contrary during the last few decades. Privatization of public companies came to a standstill and was not always followed by sufficient regulation of the new ventures, allowing windfall profits for new owners. Legal procedures for the restructuring and liquidation of sick private or public companies are inadequate, time-consuming and inefficient, thereby obstructing the switch of economic assets to more productive uses. The weak protection of shareholders encourages risky company strategies.

Anti-monopoly policy

Trade barriers have been lowered but are still not on par with the standard in competitor countries in Asia. Moderate tariff rates (average 14%) and the near complete abrogation of non-tariff barriers are compensated to a certain degree by the massive use of anti-dumping measures, where India ranks near the top. Customs clearance has improved but is still more time-consuming than in comparable economies.

Liberalization of foreign trade

The Indian financial system is highly developed and deep. It has been thoroughly reformed since 1991. State banks are still dominant, however, the public sector absorbs a considerable share (41%) of bank resources and around 40% of bank credit is still directed to priority sectors. Profitability of public and private banks, which already mostly meet Basel II standards, has increased. The share of non-performing loans has declined to a trickle. The stock markets are efficient, well developed and buoyant. The most glaring deficit is still the under-development of facilities for corporate debt.

Banking system

## 8 | Currency and Price Stability

In India, where public tolerance for inflationary tendencies is low, a consequent policy of price stability has always been followed. The Reserve Bank of India always pursued a cautious monetary and currency policy, supported by strong internal mobilization of savings and increasing inflows of foreign capital and remittances. Currency reserves reached a record level in early 2008 (around \$310 billion), forcing bank authorities to sterilize part of the inflows.

Anti-inflation / forex policy

The Reserve Bank reacted to the impact of recent price rises in food and oil in India by cutting bank liquidity further. This was followed by strong liquidity infusion into the banking system in late 2008, after the full impact of the international financial crisis was felt. International institutional investors pulled out, causing a marked depreciation of the rupee. The Reserve Bank had to sell around \$60 billion of its reserves to counter the downward spiral.

With the implementation of the Fiscal Responsibility and Budget Management Act, aiming at fiscal balance by 2008/09 and supplemented by similar initiatives of state governments, the consolidated deficit of the center and the states came down to a

Macrostability

manageable level (below 7% for 2008/09). This was achieved in spite of the fact that new, massive social programs were launched, a new pay hike for public employees was introduced, and physical infrastructure was updated. India's manageable deficit can in part be attributed to tax buoyancy (foremost in income and corporate taxes), improved tax administration but also to a relative stagnation in public investments. Other factors include creative budgeting, especially the launching of government bonds for the new debt waiving scheme, and the deficits of oil companies. Deficits are mostly financed through internal sources, external indebtedness is therefore not a problem. Even internal indebtedness fell, though debt service is still absorbing more than 20% of public revenues.

## 9 | Private Property

Property rights are adequately defined, although the constitution allows for restrictions in the public interest. No state government or important political party questions attempts to uphold property rights, the prerogative of private initiative, and the need to attract foreign investments. Enforcement of legal titles is, however, costly and time-consuming, acquisition of new land for corporate use from farmers or tribals is often politically contested.

Property rights

Private local and foreign companies are allowed in nearly every sector of the economy, although clearance is still time-consuming and costly, and the permissible share of foreign investment has not been extended. In a narrowing range of product lines, only small-scale companies can do business. Agriculture and allied industries are still heavily regulated. After 1998, the privatization of public companies was expedited but came to a near complete halt after the new government took office in 2004.

Private enterprise

## 10 | Welfare Regime

Traditionally, India has offered only a rudimentary system of social security for the privileged workers of the state and formal sector. In 2005, however, the government introduced a massive employment guarantee scheme for the poor in rural areas (granting a maximum of 100 days work), which was extended to nearly all districts later. The scheme's introduction was managed satisfactorily and has already helped to raise agricultural wages. The government also introduced a rudimentary health and pension scheme for the elderly living below the poverty line. Additionally, there are many central and state poverty schemes, which provide subsidized food and cooking oil, credit for self-employment and, ad-hoc rehabilitation packages. These programs are still poorly targeted (leading to significant spread effects to the non-poor), recent improvement efforts notwithstanding. Public expenses for basic social services have risen since 2006 but are still inadequate compared to international averages.

Social safety nets

India is certainly not a frontrunner in improving social indicators, which vary widely between states, districts within states, and between religious and social groups. Equality of opportunity is not assured; social indicators correlate positively with income, position in the caste order and urban background. Women are disadvantaged in a systematic way, especially in the “Hindi belt,” demonstrated by the massive female deficit in the population. Members of the lower castes, tribals and Muslims are discriminated in terms of education, land ownership and – despite quotas – in access to positions in the public sector.

Equal opportunity

## 11 | Economic Performance

India has become the second fastest growing economy worldwide. Growth was most pronounced in the service sector, but was rapidly catching up in industry leaving only agriculture behind. Growth was predominantly driven by total factor productivity (recently also by shooting up of savings and investment) and by buoyant internal and external demand (exports are still growing by more than 20% annually). Growth is, however, relatively capital- and skill-intensive, therefore poverty eradication and employment generation for the masses is less than it would be otherwise. India being now more integrated into world markets suffered a pronounced setback from the international financial crisis in late 2008, but short-term growth prospects are still better than elsewhere. Long-term prospects are bright because of quite a few untapped growth sources (e.g., growing labor force, migration).

Output strength

## 12 | Sustainability

The quality of the environment leaves much to be desired and is deteriorating. The economic costs of environmental degradation are considerable (according to World Bank estimates between 6% to 8% of GDP) and mainly due to unsafe water, air pollution and soil degradation. Main victims of this degradation are the poor. There is neither a dearth of comprehensive laws to keep the environment safe nor lack of regulatory institutions or active ecological movements. Missing are adequate staffing of environmental agencies, sufficient monitoring (especially of small and medium enterprises) and sufficient sanctions for non-compliance. This is only partly compensated by judicial activism in environmental matters.

Environmental policy

Education achievements in India leave much to be desired. During the review period, enrolment in the primary and secondary systems increased (thanks in large part to new initiatives) and gender disparities went down, but millions of children are still out of school, drop-out rates are high, and – most importantly – the quality of education (in terms of cognitive achievement) is very poor. Geographical, social and religious factors strongly influence students’ educational success. Parents who

Education policy / R&D

can afford it have opted out of public schools in favor of proliferating private institutions, which are barely monitored and regulated. The Indian government now spends more for education than it did before, but still less than comparable countries. Underfunding is most pronounced in secondary education and vocational training. India, on the other hand, can boast of a full range of high-class colleges, universities and elite institutions producing sufficient numbers of graduates for skill-intensive sectors. Traditionally research-averse private companies were forced by international competition to enhance their efforts. Public research is still heavily focused on defense and space applications.

# Transformation Management

## I. Level of Difficulty

Difficulties in regard to democratic consolidation in India are low because of a sustained tradition of popular participation, deeply rooted democratic institutions, absent extra-constitutional veto powers and the balancing-out of multiple, cross-cutting social, regional and religious cleavages. Difficulties in actual political management are considerable, as governments at the center are composed of a multitude of mostly small and therefore particularistic parties and factionalism in parties is rampant. During the review period, however, the main governing party lost some important state elections, which made it more difficult for it to achieve its aims. The party faced waning popularity as inflation spiraled and economic growth began to subside, but also because it became locked into a stalemate with the Communists on the clearance of the nuclear deal with the United States, eventually forcing the government to seek a vote of confidence. Underprivileged social groups (and others) have become more assertive and are aggressively asking for state largesse – in terms of quotas, subsidies or tax benefits – for states/autonomous districts of their own or simply for their improved integration into the hierarchy of power.

Structural  
constraints

Difficulties in managing economic transformation are considerable, as the protracted resistance among left and regional parties and their affiliated unions blocks nearly every reform proposal, from privatization to a necessary increase in oil prices to labor law reforms. Economic transformation itself is increasingly difficult. Since the electoral verdict of 2004, pro-poor growth has become a priority and the national government has had to make room for investments in social infrastructure, rural development and safety nets (e.g., rural employment programs), while at the same time continuing investments in physical infrastructure.

Civil society is only partially helpful in overcoming India's structural constraints. Highly fragmented, labor unions are not able to conclude and honor any social pact. Labor militancy has subsided somewhat in the last few years as the share of regularly employed workers declined. Industrial federations have become more assertive and are demanding a follow-up to the first round of economic reforms, but they are also hesitant to back real trade concessions in bi- and multilateral

Civil society  
traditions

negotiations. NGOs and social movements have taken on a more active role as guardians of the environment and civil and minority rights. They have also assumed a more active role in upholding the probity of political life and the accountability of government at every level. Their activities can render governance more difficult, leading to long delays in public programs (e.g., irrigation dams, power generation) and regulations such as the new forest policy.

The incidence rate of militant conflicts in India remained more or less unchanged during the review period. At a time when the conflict over Kashmir was once again intensifying, the Indian government initiated negotiations with militant groups and roundtable discussions on the future of the state as it continued dialogue with Pakistan, which improved linkages between stakeholders in Kashmir. The conflict in Kashmir intensified again in the summer of 2008 because of a trivial incident; the state was put under the president's rule but regular (and relatively peaceful) elections were held in late 2008. In West Bengal, agitations for an independent state of Gorkhaland intensified, followed by all-party negotiations. In Assam, violent attacks by militant students against immigrants were answered by renewed military strikes, which led to a series of bomb attacks by militants. Separatist unrest in the North-East states continued. A series of bomb blasts in major Indian cities in summer 2008 – most prominently those in Mumbai – all perpetrated by Islamist terrorists within India (apparently with some support of groups in Pakistan), raised concerns worldwide. These attacks and a strike by Hindu militants demonstrated that religious fanaticism was again on the rise. It should be noted that the attacks on Christian minorities in Orissa and Karnataka that were instigated by Hindu extremists were either tolerated or encouraged by the relevant state governments. Naxalite activities subsided in some parts of the tribal belts. The government shifted the focus of its response from that of a purely military reaction to a mixture of development, decentralization and reintegration of refugees. The scattered and fragmented nature of these events means that they did not pose a serious challenge to state integrity.

Conflict intensity

## II. Management Performance

### 14 | Steering Capability

Prioritizing actions constituted a difficult challenge for the government during the period under review. As additional economic reforms were blocked, it turned its focus toward hitherto neglected areas, aiming in particular to provide education for

Prioritization

all, upgrade rural health facilities, develop urban and transport infrastructure, establish a minimal social security net and institute a nationwide employment guarantee program. These were highly desirable aims, as these sectors have been neglected during the economic take-off of the past 15 years. However, more could have been done if budget deficits would have been reined in earlier. Nonetheless, money for the new programs was spent and monitored better than in earlier periods. In addition, the government successfully maintained the economy's dynamism by introducing tax reforms and launching new initiatives with moderate financial means.

A serious effort was made to trim the multitude of often overlapping central programs under one umbrella (e.g., in education, health, employment), to put resources directly at the disposal of responsible authorities, to improve participation of local stakeholders and to monitor program output (by relevant yardsticks). While policy implementation has definitely improved, delays and the uneven utilization of budgetary resources or spread of benefits to non-target groups are still frequent. A large part of the blame falls on badly governed states. The government unfortunately could not always resist the temptation to introduce populist measures, as was the case with the new debt-waiving scheme for marginal and small farmers or the decision to pass on oil price increases.

Implementation

The political leadership's learning record is uneven. Learning processes are evident in newly launched programs that have been thoroughly prepared by expert committee reports, incorporate civil society input and draw upon best practices. Political learning in other fields is rather slow and incomplete, caused not in the first instance by knowledge deficits but by the conflicting interests of powerful social groups and their political representatives on whose support the government depends. Vivid examples include the gradual improvement over 20 years of tribal rights to forest lands, the only nominal slashing of subsidy programs, the hesitant rise of state-controlled oil prices and the latest loan waiver scheme for farmers. Most of these learning deficits are expensive, benefit the wrong groups and carry negative consequences for sustainable development.

Policy learning

## 15 | Resource Efficiency

The government is more efficient than before in its use of the available financial and human resources for the transformation project, it could do better. The central and states' combined budget deficit is still massive, amounting to 6% of GDP for the fiscal year of 2007 – 2008 (excluding shadow budgets and guarantees). The deficit absorbs a high share of savings and bank credit/deposits, thereby crowding out private investment and public investment in critical areas such as infrastructure development, maintenance, education and health. This deficit can be attributed to poorly targeted and partly unproductive subsidies, generous salary increases in the

Efficient use of assets

public sector, a high interest burden, the exclusion of agriculture (and to some extent the service sector) from the taxation net and a multitude of relatively unproductive tax incentives and loopholes. Tax administration has, however, improved significantly. The central government's new Fiscal Responsibility Act and parallel acts initiated by the states, combined with the central government's allocation of taxes to the states have helped to improve tax administration and reduced primary deficits which could have been brought to zero in the fiscal year of 2008 – 2009, had it not been for the impact on India of the international financial crisis and the rise in oil prices.

The coordination of conflicting objectives is hampered by political forces moving in different directions and overlapping mandates of far too many departments following their own agendas. By consolidating central programs under a few heads, establishing several interministerial committees, and creating a coalition steering body at the central level, the government improved its ability to coordinate policies. Unfortunately, coordination between the central government and the states was negatively affected by new umbrella programs able to bypass the states, growing – and often discretionary – transfers to states outside the framework of the Finance Commission, and direct foreign economic assistance to the states.

Policy  
coordination

Corruption, which is deeply embedded at every level of the polity and administration, has become accepted as a fact of life. This does not mean that there is a dearth of legislative actions to curb corruption or of relevant units to fight it, but there is a fundamental lack of respect for legal endeavors to end malpractices, especially among the political leadership, who are among the most visible culprits. The roots of this problem lie in the discretionary leeway granted bureaucrats in a still heavily regulated economy, escalating election campaign expenses, donations to political parties that go unaccounted for, and a strong culture of patronage. As investigations are rare and stretched thin, very few politicians or civil servants have been convicted in India.

Anti-corruption  
policy

## 16 | Consensus-Building

Most people, groups and parties in India would agree that the country is and will remain a consolidated democracy and that it will continue to nourish its full-fledged market economy. This does not mean that they necessarily agree on the means to achieve these ends. There is intense disagreement over several issues, including the proper share of the public and private sectors in economic activity, further integration into the world market (especially in terms of removing the remaining tariff and non-tariff hurdles), full convertibility of the currency, the (market-based) pricing of public services and goods, and the creation of special economic zones. There is also significant dissent over the secular character of the state, the extension of reservation quotas, women's political empowerment, and the treatment of

Consensus on goals

minorities. Finally, parties in power that pursue distinct objectives, such as the nuclear treaty or privatization, frequently switch sides once they are no longer in power.

Anti-democratic veto actors do exist but are small in number and influence. Most prominent among them are militant (separatist) groups in Kashmir and the North-East, and Naxalites in the tribal belt. Some of these groups could be brought back into the mainstream if offered genuine autonomy within India and generous rehabilitation packages. The small remainder could be dealt with by firmness. Some problems are intractable, as every attempt to resolve a problem is likely to create new minorities.

Anti-democratic  
veto actors

Political cleavages are accommodated as much as possible through measure such as reservation quotas, development packages, the creation of new states or autonomous regions. In addition, newly emerging groups have been incorporated into the political leadership or have created new political organizations. In rare cases these examples of statesmanship were thrown overboard for political mileage.

Cleavage /  
conflict  
management

The participation of civil society in the political process has definitely increased. India is sometimes represented as the NGO capital of the world, counting up to 100,000 different organizations and self-help associations. Protests, demonstrations and strikes are an everyday occurrence. NGOs have also gained institutional footing, supported as they are by generous donations from the local population and international agencies. The government, which is the main cooperation partner for associations and the most important addressee of demands, maintains tight control over transfers. Parliaments do not play a prominent role in NGO interactions. Despite the large number of associations, the participation rate of the population is still rather low.

Civil society  
participation

Reconciliation between the victims of perpetrators of past injustices is a weak point in India. Delayed police investigations, laborious judicial proceedings, limited compensation and the denial of responsibility on the part of responsible agencies have frustrated attempts to rehabilitate victims of communal conflicts, natural disasters and land alienation. The record is improving, however, as demonstrated by recent compensatory packages for tribals, Muslims and members of the lower castes.

Reconciliation

## 17 | International Cooperation

International development cooperation plays a very limited role in consolidating democracy, and initiating, implementing and financing market reforms, as assistance is minimal in relation to the usual parameters (e.g., GDP, gross investment, exports). However, this aid had a distinct impact on launching reforms

Effective use of  
support

in social sectors and on improving and managing physical infrastructures. The Indian government has often expressed its intent to do without foreign aid in the future and cultivates a self-confident posture in its contact with donors. This does not mean that the government will not ask for more assistance if the necessity arises, as was the case when the global financial crisis began to impact India, or when union or state governments do not cooperate. During the review period, quite a few union territories, with the support of international organizations, initiated far-reaching educational, health and infrastructural reforms. There is, however, no room for a unilaterally imposed political dialogue. Although governments of all political leanings acknowledge the need to attract more foreign direct investment, measures to advance liberalization and regulate foreign direct investment are implemented hesitantly and with an eye to the local constituencies.

The Indian government has become a reliable partner in curbing nuclear proliferation and in the fight against international terrorism. It has been actively engaged in several peacekeeping missions and is actively backing and broadening its engagement in multilateral and regional organizations. This government does obstruct progress, however, when perceived Indian interests are supposedly under threat (e.g., WTO negotiations, non-proliferation treaty, lowering greenhouse emissions).

Credibility

India has often displayed an overbearing and uncompromising attitude towards its neighbors. In the last few years, however, India has demonstrated a new preparedness to make unilateral concessions so as to accommodate neighbors (in regional cooperation). It has also restrained from using excessive political interference (e.g., Nepal and Sri Lanka), and it has dealt constructively with Pakistan over long-standing conflicts (e.g., Kashmir).

Regional  
cooperation

## Strategic Outlook

The Indian government aims to reach the status of a developed economy by 2020 as it becomes a major global player. Supported by economic reforms, the country has experienced rapid, productivity-led growth over the past decade. With a massive increase in foreign investments and high remittances, the country enjoys a comfortable balance of payments situation, substantial foreign reserves and the benefits of sustainable debt. Having established federal arrangements capable of expressing diversity and including the elites of underprivileged groups, India is positioned better than some other countries where democratic consolidation and political inclusion have yet to be engineered.

Because the distribution of economic growth is not equal, the government should be encouraged to foster a more equitable sharing of benefits. Some populist aberrations notwithstanding, the central government's people-friendly program was a step in the right direction. While India has improved its fiscal indicators (with a foreseeable slippage in 2009), further improvements are needed to fund the country's large infrastructure deficits – especially in developing power networks, roads and ports – which impair its competitiveness and hinder the growth of labor-intensive enterprises. Funding is also needed to improve the quality and services of the health and education systems. Agricultural irrigation and rural infrastructure are further areas demanding investment. More flexible labor regulations could attract more labor-intensive investment while creating jobs for the unemployed millions and those trapped in poor quality jobs. Most environmental indicators suggest that growth is extracting an increasing toll on the country's natural resources. Climate change will have a massive impact on India, primarily in terms of its water resources but also in terms of agricultural yields. Efforts to lower the water and energy intensity of production are urgently needed to minimize the fallout of local sources of environmental degradation.

There are a few areas in which India's democratic credentials could stand improvement. Most prominent among them is the judicial sector, which is plagued by corruption, understaffing and a massive backlog of litigations. It should be noted, however, that the high courts and the Election Committee have been proactive in prosecuting cases of misuse, and in upholding civil rights, the transparency of government procedures (which has been supported by freedom of information acts) and safeguarding the environment. Initiatives to enhance the police forces' independence from political interference and their trustworthiness are urgently needed. The international community should support policies aimed at engaging local rebel groups in Kashmir and the North-East. At the same time, attempts on the part of foreign-sponsored terrorist groups to destabilize peace efforts should be unequivocally condemned as should the Hindu radicals' prosecution of minorities (e.g., Christians, Muslims), which is frequently tolerated or even encouraged by state authorities.