

## **Distributive Conflicts and Indian Economic Policy:**

### **Some Notes on Political Economy**

**By**

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### **I The Various Inequalities**

As India has one of the most heterogeneous conflict-ridden societies and a high degree of economic inequality, it is not surprising that distributive conflicts have a powerful influence on the political economy of policy formulation and implementation.

Contrary to popular impression, India may be one of the most unequal countries in the world. In economic writings on India it is commonplace to describe Indian economic inequality to be relatively low. In support the inequality measure of Gini coefficient on the basis of NSS consumption data is usually cited. This Gini coefficient in 2004-5 was 0.325, and is indeed lower than in many developing countries including China, and by constant repetition, both in national

and international documents and the financial press, this has become part of the folklore about Indian inequality.

But there are reasons to believe that the NSS data under-represent the rich, and in any case while for other developing countries the Gini coefficient often refers to income distribution, India's refers to distribution of consumption expenditure (as NSS does not collect income data), which is usually less than that of income (partly because the rich tend to save more than the poor). The National Council of Applied Economic Research (NCAER) occasionally collects income data, and according to their data collected in a 2004-5 household survey, the Gini coefficient of income inequality comes to 0.535. Contrast this with the corresponding figure for China, 0.387—see the comprehensive estimate by Lin, Zhuang, Yarcia and Lin (2008).<sup>1</sup> Not merely the Indian estimate of income inequality far exceeds that of China, it is in the Latin American range. But ethically and socially one is more interested in inequality of *opportunity* rather than that of *outcome* (like income). After all with the same opportunity two people can end up with different incomes, simply because one is more ambitious and hard-working than the other, and many of us may not be too worried about that as long as opportunities are equalized. For Latin America some attempts have now been made to measure inequality of opportunity, but very little as yet in India. But in a country like India inequality of opportunity will surely depend on distribution of land, of education, and social identity—a child born in a rural landless *adivasi* family with very little scope for education will be severely handicapped in her life chances for no fault of her own.

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Land distribution in India is much more unequal in India than, say, in China. The Gini coefficient of inequality of land distribution in rural India was 0.62 in 2002; the corresponding figure in China was 0.49 the same year. (This is partly because India has a much larger landless population). One can say that this does not correct for land quality variation (say from Rajasthan to the coastal deltas). Land quality is partly taken into account in its valuation when land is included in the NSS Assets and Liabilities Survey. By these data, the Gini coefficient of ownership of asset distribution was 0.63 in 2002 in rural India, while the corresponding figure for China was 0.39 in the same year.

Most people seem to be unaware that India's educational inequality is one of the worst in the world: according to World Bank estimates, the Gini coefficient of the distribution of adult schooling years in the population, a crude measure of educational inequality, was 0.56 in India in 1998/2000, which is not just higher than 0.37 in China in 2000, but even higher than almost all Latin American countries (Brazil: 0.39)--again, this is partly because of India's large illiterate population.

Taking a long view, what is more important than static inequality is inter-generational mobility. On this quantitative empirical work is rather scanty. Some preliminary estimates suggest that such social mobility is much more in China than in India, partly no doubt because of the deadening legacy of the system of caste oppression and discrimination in India.

## II Equity and Economic Reform

Does inequality of opportunity matter for economic growth (apart from just offending one's sense of social justice)? Of course it does, if one keeps in mind that barriers faced by the poor in land and capital markets and in skill acquisition and in coping with risks sharply reduce a society's potential for productive investment, innovation, and human resource development. They often block the creation of socially more efficient property rights (for example, in land tenure) and investment in high-risk but high-return innovative projects. Inequality that keeps the work force largely uneducated and unhealthy cannot be beneficial for private business, apart from the law and order problems that inequality-generated conflicts may bring about. Moreover, institutional structures and opportunities for cooperative problem-solving are often foregone by societies that are highly polarized. Equity and efficiency thus often go together, contrary to the opposite presumption of much of mainstream economics.

In India considerations of equity have often been used as an excuse for all kinds of regulatory excesses. In the name of helping the poor and the small farms and firms many restrictions on private initiative and on capacity expansion and many programmes of government subsidies and handouts have been launched in the past and, under the pressure of vested interests, prolonged indefinitely. Economic reformers have rightly pointed out that most often these policies and programmes did not help the poor (and there certainly exist more cost-effective ways of helping them), while distorting the economic incentives for enterprise and investment and protecting the rental havens of politically well-connected oligarchies. In other words, they helped the cause of neither efficiency nor equity.

At the same time in a country that in terms of inequality of opportunity and inter-generational mobility may be one of the worst in the world, Indian reformers have to be extremely sensitive to (the public perception of) equity issues if they hope to move the cause of economic reform, which has been in general rather halting and hesitant over the last two decades. Cheerleaders of reform among corporate tycoons and financial columnists are often not aware how unpopular reform is, rightly or wrongly, among the general public in India. In the National Election Survey 2004 more than two-thirds of about 23000 sample respondents (who had any opinion on the subject) say that the reforms benefit only the rich or none at all.<sup>2</sup> Politicians are, of course, too savvy not to notice this. Any of the ruling parties over the last two decades which supported reforms played them down during election time. A party that initiates some reforms is quick to oppose them when out of power.

Economic reform, as it aims to bring about more competition, inevitably causes job disruptions and displacements which raise the level of anxiety among workers particularly in a country of very little general social protection. Trade unions of the right as well as left parties in India are opposed to privatization and to relaxation of the job security regulations in labour laws. The Gandhians as well as the leftists had been vocal against the lifting of the policy of reservation for the small-scale industries (and other policies of positive discrimination in favour of small enterprises). In the above-mentioned National Election Survey respondents were asked about reduction in the size of government employees; among the poor, and the low-caste and *adivasi* respondents, who had an opinion, the majority was opposed to such reduction. The newly emergent, hitherto subordinate, social groups, often represented by primarily caste-based or regional parties, as they capture state power and reserved jobs, are obviously not too keen to give

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up the loaves and fishes of office or reduce the role of the public sector (where at the lower echelons the salaries are about three times what one would get in the private sector with similar qualifications).

What financial columnists are quick to describe as anti-reform populism is partly a product of the manifold inequalities and conflicts of Indian society. The severe educational inequality, for example, makes it harder for many to absorb the shocks in the industrial labour market, since education and training could provide some means of flexibility in adapting to market changes. In China the disruptions and hardships of restructuring under a more intense process of global integration were rendered somewhat tolerable in the 80's and 90's by the fact that China has had some kind of a minimum rural safety net, largely made possible by an egalitarian distribution of land cultivation rights in 1978-79. In most parts of India for the poor there is no similar rural safety net. So the resistance to the competitive process that market reform entails is that much stiffer in India. This is in line with a phenomenon all over the world: resistance to globalization is stronger in general in countries where social safety nets (particularly unemployment benefits and portable health insurance) are weaker (compare Scandinavian countries and US in this respect).

### III Collective Action Problems

In general, as social heterogeneity and economic inequality make the social and political environment in India quite conflict-ridden, it is difficult in this environment to build consensus and organize collective action towards long-term reform and cooperative problem-solving efforts.<sup>3</sup> When groups don't trust one another in the sharing of costs and benefits of long-run reform, there is the inevitable tendency to opt instead for the 'bird-in-hand' short-run subsidies and government handouts, which pile up as an enormous fiscal burden. Very few politicians dare oppose the continuing serious under-pricing of water and electricity (along with fertilizers, domestic fuels like kerosene and LPG and gasoline, railway passenger fare, tuition in higher education institutions, etc.), the over-manning of the public payroll, and a long-standing refusal to tax the better-off farmers.

This is a general problem of collective action in a country where even the elite is highly fragmented. In terms of social and economic divisions the Indian elite may be more fragmented than the elite in most other countries, reflecting the fact that India has one of the world's most heterogeneous societies (in terms of language, religion, caste and ethnic divisions). The resultant collective action problem makes it more difficult for the divided elite groups to agree on a goal, and even when they agree on a goal, it is difficult for them to coordinate their actions to achieve that goal. This becomes a particularly acute political-economic problem in the matter of long-term public investment in infrastructure (power, roads, transport, telecommunication, ports, irrigation, etc.). Infrastructure is widely regarded as the crucial bottleneck for Indian economic

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growth, and the Indian elite is to largely benefit from any improvement in infrastructure<sup>4</sup>. Yet substantial public investment in infrastructure which takes a relatively long time to fructify may require significant short-run sacrifices. In the current situation of large fiscal deficits, this means giving up on the part of the elite (and the so-called middle classes) on government subsidies or benefits of under-priced public goods and services, or on salary or perks in government jobs, or allowing for major raises in taxes and user charges. But coordinating on short-run sacrifices or curbing particularistic demands on the public fisc (it has been estimated that about two-thirds of all government subsidies go to the relatively rich) for the sake of long-term elite goals has been very difficult to achieve in India.<sup>5</sup>

#### **IV The State Presiding Over Economic Conflicts**

Of course, in the last two decades the old rent-sharing equilibrium (among business houses, the salariat and rich farmers) has changed somewhat and tilted in favor of capitalist business. The hegemony of the latter is reflected in the more general acceptance of pro-business policies and reform in trade and industrial policy without a great deal of opposition in policy circles. While infrastructure remains a bottleneck, there is a more general consensus on the other major public good, i.e. macro-economic stability, as a pre-condition for economic growth. While inflation

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control has remained high on the public agenda, there has been less agreement on a whole range of other reform, particularly relating to the factor markets (labor, land, electricity, etc.) and on fiscal subsidies and rent-sharing with the newly emerging social groups. Unlike in the case of delicensing or tariff reform, in reform of the job security laws in the labour market or of the procedures of acquisition of agricultural land for industrial, commercial or mining use or in charging market prices for electricity, the life and livelihood of a very large number of people are involved, and we know from the literature on collective action how it is rendered difficult when it involves large-sized groups with conflicting interests and with weak mechanisms for transmission of information to the central decision-makers.

There are two kinds of collective action problems. One relates to sharing the costs of bringing about change (the 'free-rider problem'); the other relates to sharing the benefits (the 'bargaining problem'). Over the years both of these collective action problems have become more severe in the Indian polity. As more and more of hitherto subordinate social groups have come up to be politically important particularly at the state level (in a welcome expansion of political equality and democracy in India), the sources of demands on the polity have become more diverse. In the first two decades after Independence the massive country-wide organization of the Congress Party used to coordinate the transactional negotiations among different groups and leaders in various parts of the country. That once-mighty organization has fallen into disarray. The proliferation of small and regional parties and their increasing importance for the survival of coalition Governments at the centre have often meant that catering to particularistic demands overrides coordination for the long haul.

When the interest groups are socially and economically fragmented, pulling in different directions with none dominating the whole show, state policies get buffeted around, and any

steps towards economic reform are likely to be often rather perfunctory. But at the same time such fragmentation may also give the state somewhat more autonomy, in the sense that it does not have to march to the tune of one dominant interest group<sup>6</sup>, and an astute political leadership can play off one group against the other and get its way to some extent, and even earn its own rent in the form of special power and privileges. In such a context the state leadership can retain some potency as an organizational actor in goal formulation, agenda-setting and policy execution, even when they act within the broad constraints of interest group politics. Such autonomy<sup>7</sup> of a government may also allow it to take advantage of the malleability and fragmentation of interest groups to diffuse some resistance to reform. It is in this context that one can see the point made by Jenkins (2000) that the Indian political system has clever, if sometimes clandestine, ways of introducing many kinds of reforms<sup>8</sup>—what he calls ‘reform by stealth’— and that accommodations arranged through informal political networks mediate conflicts between winners and losers, and particular reform measures generate a chain reaction of demand for more reform from within.

While liberalization has meant a significant reduction in the discretionary powers of the central bureaucracy particularly in trade policy and industrial regulations, the state governments still retain a great deal of leverage over the industrial sector at the ground level through their control of land, water and electricity and labor and environmental regulations. Different states apply these regulations with different degrees of alacrity and the differing political attitude to creating a hospitable investment climate for private capital often reflects political conflicts within the state. There is a growing body of public opinion that the state should mainly be a facilitator in the

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industrial and service economy and reorient its role away from public ownership and control of business enterprises towards more on health, education and other basic social services for the poor, and even when the state is to be the major funding agency for some of these services, it does not necessarily mean that the actual provision of the services has to be bureaucratically managed, instead of being contracted out to the private sector or some form of private-public partnership. But, in spite of some progress, the political implementation of this view in large parts of India has been slow and fitful.

#### V Resistance to the Logic of Capital

In India where society has been stratified and fragmented for many centuries, distributive conflicts often take the form of demand from hitherto subordinate groups for protection and relief from the state. This demand is often expressed in asking for mandated reservations as group entitlements (for jobs, seats in higher education institutions and in legislative bodies, etc.), and this has become the most popular redistributive tool in public discourse. Public sector job reservations for some historically disadvantaged groups, for example, fervently catch the public imagination, even though objectively the overwhelming majority of the people in these groups may have no chance of ever landing those jobs, as they and their children largely drop out of school by the fifth grade. Attention is thus directed at symbolic policies, and the patronage benefits are primarily enjoyed by the elite of these groups, deflecting public attention away from the more general and difficult challenges of improving the delivery structure of social services like basic education, health (public health and sanitation as well as medical care) and nutrition.

Reservations often become a surrogate for effective public action against poverty, disease and illiteracy. The logic of reservations, of course, also defies the logic of market reform.

Resistance to market reforms in India is also provided by environmentalists and those concerned with the rights of urban squatters, and of the indigenous and other marginalized people. In general the people who eke out their fragile living in the overwhelmingly large informal sector particularly in the periphery of the urban economy use their political/electoral power of numbers to negotiate with the state some forms of tenuous protection against the onslaught of the market and legality<sup>9</sup>. Markets, and capitalist development in general, have become identified with uprooting the livelihoods of the little people and despoliation of the environment and of traditional rights over community property. The record of resettlement and rehabilitation of people displaced by roads or dams or mining and industrial projects is dismal in India, and recent history of such projects is replete with arbitrary land acquisitions, paltry compensation, defrauding by contractors, and renegeing of promises to these poor people. This is the context of widespread opposition to land acquisition for commercial purposes in India. The Indian Government's attempt to replicate the Chinese-style Special Economic Zones has hit this formidable road block in some, though not all, states. It is a major instance of distributive conflicts casting a dark shadow over policies of economic development in India. Here the political process has so far failed in providing a viable and generally acceptable programme of compensation, retraining, and rehabilitation in many cases of necessary change<sup>10</sup>. This is more than just a failure of the state; even the well-meaning NGO movement, apart from trying to carry out the necessary task of giving voice to the deprived and underprivileged groups, has not been able to play a very constructive role in the outcome, particularly in paying enough attention to

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the various complex trade-offs involved and the need for difficult compromises that can balance the different interests. In general, the voluntary groups being single-interest pressure groups cannot serve the function of inter-group transactional negotiations and compromises which the large encompassing party organizations used to coordinate under their own umbrella in the past.

Another type of distributive conflicts arises in the context of regional allocation of resources.

While the logic of capital has unfolded itself in recent years in its free mobility across state boundaries in search of more business-friendly policies and infrastructure, stoking the frenzy of inter-state competition for investment, a fundamental tension of fiscal federalism expresses itself when the more successful states openly resent the redistributive dispensations of the Finance Commission (and the Planning Commission), and yet a central coalition government cannot afford to ignore the demands of populous backward states with a large number of MP's.

However, very little of the central transfers (or direct subsidies) goes towards correcting the severe infrastructural deficiencies of the poorer states. As inequality across regions increases, migrants from stagnant areas have been trying to move to areas where jobs are expanding faster, often causing nativist unrest and inconvenient dilemmas for the interests of capital seeking pan-Indian markets but at the same time keeping patronage relations with the local power brokers in tact. Similarly, in the extraction and movement of resources from the poor but mineral-rich areas of India (where coercive but ineffective regional governments, often captured<sup>11</sup> by the mining mafia, meet equally violent insurgencies organizing sections of the long-deprived *adivasis* against 'internal colonialism' by the rest of the country), capital already faces a great deal of resistance.

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In this paper we have tried to give a qualitative and broad account of the different types of distributive conflicts that have become prominent in the process of economic development in India and how their impact will shape the nature of problems that afflict economic policy making and implementation. Looking to the future, the tension between the inexorable logic (and hegemony) of capital on the one hand and that of increasing inequality and political fragmentation (making collective action on long-term policy commitments more difficult and interrupting the progress of market reform) on the other, will pose the major policy dilemma in India from the political-economy point of view. As the economy transits from agriculture and small-scale production to activities that generate agglomeration economies and 'growth poles', the high-value generating areas of urban concentration are likely to come into political conflict with the far-flung rural areas and small towns where the masses of voters (endowed with their paltry immobile resources) subsist. It is not clear if the technologies of the future will be more scale-neutral than in the past. While information and communication technology as well as biotechnology and the new drive for energy-efficiency may allow smaller-scale and flexible production reducing the forces of inequality and the spread of education among an increasingly young labour force (at least over the next quarter century) brings forth some inter-generational mobility in our stratified society, there are opposing, unequalizing, forces inherent in finance, risk-taking and marketing economies of scale, increasing demands for skill-intensity in production, and the forces of labour heterogeneity and global competition undermining worker organizations. Needless to say, in-depth research on these issues, both in the form of case studies in political sociology and quantitative economic evaluation of the distributive impact of different policies, will be highly valuable.

## Endnotes

<sup>1</sup> Both the Indian and the Chinese estimates here correct for spatial price variation between rural and urban areas, which is not done in the usually cited estimates of Gini coefficients.

- 2 See Suri (2004). This has also been confirmed in a January 2007 smaller survey by the same team of the Center for Study of Developing Societies (CSDS). Of course reformers have also done a poor job of explaining reforms to the common people. If it were to be made clear to them, for example, that electricity reform which may involve a higher electricity price also implies a higher capacity for the public utility to provide less erratic power supply, or that deregulation means loosening the grip of corrupt inspectors over small enterprises, some of the opposition could decline. In fact the January 2007 CSDS survey finds that 63 per cent of the respondents are prepared to pay higher rates for electricity if it is regularly supplied.
- 3 This is in line with a large theoretical and empirical literature on the relation between inequality and collective action-- see, for example, Baland and Platteau (2006) and Bardhan (2005).
4. Of course, lack of infrastructure, like power or roads, hurts the poor small producers even more than the large producers.
5. This was the central point of Bardhan (1984) in discussing the collective action problem that hinders public investment in India.

6. Yadav and Palshikar (2009) have even suggested that in recent years as the complexities of competitive politics at the multiplicity of state levels rise, the aggregating coalition governments at the center can have some policy autonomy which can operate somewhat independently of the particularities of political contestation in individual states.
7. This is related to the old Marxist literature on the 'relative autonomy of the state'.
8. 'Reform by stealth' usually does not work when it affects large groups. It cannot be substantial and purposive enough to break, for example, the basic political logjam in the macro economy caused by the staggering fiscal burden of subsidies to different interest groups.
9. Chatterjee (2004) emphasizes the importance of the contingent, and often para-legal, negotiations between the state and what he calls 'political society' of the poor in Indian cities.
10. For some constructive suggestions on the formulae for land compensation, see Bardhan (2009)
11. In some cases such capture (in collusion with local political leaders) has been made easier by the formation of smaller states based on legitimate demands for devolution of power to ethnic minorities.

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