Make-in-India

For whom and at what cost?

Quality institutions, state-of-the-art infrastructure and efficient allocation of resources will be crucial

Of the many simmering slogans coined by the NDA government, "Make in India" is the most important as it promises to make India an important investment destination. However, like most other slogans, it is important to be clear about what has to be achieved and how. After all, Jawaharlal Nehru too strived to make in India by erecting high protective barriers. The policy completely ignored the interests of the consumers who had to put up with products of inferior quality at high costs. We departed from the strategy in 1991 because, it was not sustainable. Therefore, the slogan should have a different connotation not merely in terms of the tapestry, but also in terms of the real content.

Making India an important investment destination requires a systematic approach and strategy involving both policies and institutions. This requires the existing systems and processes to undergo significant changes to remove the structural rigidities and to create an accommodating ecosystem. The distributional coalitions that have deeply entrenched in the system will not easily allow such structural changes. A clear understanding on the part of the policy makers of what needs to be done to create a favourable ecosystem is necessary. This requires clarity, appropriate strategy and its communication with the people.

Operationalising of Make-in-India entails the Indian economy being internationally competitive, which requires the efficient use of existing resources and creating a favourable climate for achieving technological progress. Creating such an ecosystem calls for a combination of reforms to change the character and quality of institutions, provide state-of-the-art infrastructure and get the prices right to achieve efficient allocation of resources. Given the nature of federal polity and the fact that in a number of areas the states have important roles to perform, the policy and institutional changes will have to encompass both the Union and states. The Union government will have to work out strategies to carry the states in this long journey.

The most important intervention by the government is to change the character and quality of institutions. Admittedly, labour laws have been a binding constraint in promoting labour intensive industrialisation and the Union government's initiative in giving a greater role to the states is the best way forward. The pernicious effect of labour laws has led to declining fortunes of labour intensive industries like textiles and leather in which India has a comparative advantage. With labour becoming expensive in China, India can reclaim its lost ground. The labour laws rather than protecting the interests of labour have caused slow growth of employment and more particularly, organised sector employment in India.

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A critical component of institutional restructuring is administrative reform. The second Administrative Reforms Commission has made useful recommendations, but surely, in a situation where bureaucracy is the most influential interest group, the tyranny of status quo will continue. Ensuring accountability and rewarding performance and making appointments on the basis of competence are the need of the hour. Bureaucrats never fade; virtually every regulatory system has been captured by the retired bureaucrats and competence has not always been the criterion in these appointments. The vitiation in the ease of doing business is exemplified by the functioning of the taxman. Not much has changed since the NDA government has taken over to change the attitude of tax administration.

Much as we have decried the licence-permit raj, this continues to pose impediments in various ways at all levels of government. The number of bureaucratic clearances required for every initiative from the Union, state and local levels are numerous. Courts do not resolve disputes within a reasonable time period and in the absence of an effective redressal mechanism, people are forced to take sub-optimal decisions. Protection of life and property is the basic function of the state and basic prerequisite for taking investment decisions. The Union government has to take a lead, though reforms encompass all levels of government.

A lot has been written about the infrastructure deficit in the country. The investment in infrastructure projects stuck for one reason or another is estimated at over 8% of GDP. The cobweb needs to be cleared. The land acquisition issue is stuck in the political logjam; there are no easy solutions and the industry will have to work around it. The major problem in the power sector is the disconnection between the policies relating to generation and distribution. Despite several rounds of reforms based on bailouts to discoms, political interference and ineffective regulation have continued to paralyse the sector. The promise of recapitalisation of public sector banks may provide some financial room, but this is not going to solve the structural problems in the financial sector. The most important initiative needed is to step up public investment in infrastructure. Although the low volume of budgeted investment at the Union level is a matter of concern, the government has done well to front load capital expenditures. Better revenue collections from indirect taxes too point towards a possibility of enhanced investment spending. It is important to come out with an acceptable model concession agreement for PPPs to move forward in this area. Private investment clamours for low interest rate which implies that the fiscal deficit should be contained. In this environment, increase in public investment is possible only when the tax-GDP ratio increases. The GST reform promises much, but with compromises and distortions, one is not sure how much it will deliver. Indeed, it is necessary to view GST reform as a process, not a big bang reform.

A major structural problem constraining productivity in India is the control on prices. Even after 24 years of liberalisation, prices of many goods and services are determined through administered fiat rather than by demand and supply. Controls on prices have distorted the resource allocation at macro and micro levels and has proliferated subsidies. Administered interest rate on provident funds places a floor on the reduction in interest rates. Pre-empting a large proportion of household sector's savings for public spending distorts the structure of interest rates. Overvalued exchange rate hurts the export sector. We cannot distort cane prices, and then increase import duties on sugar to protect the sugar lobby and persuade increased proportion of blending ethanol in petrol to consume sugar sticks. Subsidising irrigated water results in the farmers adopting water intensive crops even when that is not appropriate. Subsidising electricity results in depletion of underground water. Subsidising urea results in the distorted consumption of fertilisers and soil salinity. The examples can be multiplied.

Indeed, many of the initiatives relating to Make-in-India require coordinated calibration of reform by both Union and state governments. It is also important that the required reforms get bi-partisan support. Forging consensus and securing support cannot be achieved through confrontationist strategy. The opposition has nothing to lose by opposing and it is here the ruling party has the primary responsibility to adopt a conciliatory approach to build consensus. Building hot and cold will not certainly help the cause of reform to Make-in-India.

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