

# Bankers Trust Company



# Country Assessment

International Economics

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INDIA UNDER RAJIV

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countercyclical

Justs: ~~the~~ form, coherence, effectiveness

Indira II Jewels  
parliament  
state govts  
civil svc  
cabinet  
state firms

Local crises, formerly manageable, become larger

Assam  
Sikhs/Punjab  
Bihar, landlords  
provoke Rajiv

Ec reform

physical controls  
heavy industry

Assassination - no big deal

Rajiv

overwhelming victory  
based on lack of competition

statelike state  
promises reform: pol corruption  
collapse/corruption ec openness

Scenario I:

Scenario II

very conservative from moment

**DRAFT**

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## INDIA UNDER RAJIV

India has enjoyed a long period of deceptive stability. For some time after independence, the country was blessed with a leadership of world renown (Nehru and others), a Congress Party whose broad national support glued the country together politically, a functioning parliament, effective state governments, a civil service of some competence by third world standards, a professional and non-political military, and some state firms which had highly capable leadership.

India's economic management for most of the generation after independence had most of the vices, and a few virtues, of socialist and nationalist ideology. The country emphasized military and heavy industry to an overwhelming degree, and built up steel, railroads, and other heavy industries to a scale of production quite comparable to that of a medium-sized European country. It emphasized state ownership of these firms, which needed, and continue to need, extraordinary subsidies. It suppressed the leading industries which might have generated exports, notably textiles (which were deliberately hobbled on the ground that there would be no market, just about the time that other Asian countries began to build successful takeoffs around that industry), and tea and cotton, whose exports were limited in order to keep domestic prices down. In order to discourage middle class consumption and the emergence of an "unfair" pattern of final demand, most privately owned and consumer oriented industries were constrained by production ceilings. To enforce such policies, India expanded its omnipresent bureaucracy, which became ever more stultifying and corrupt.

The same nationalist and socialist ideas led India to constrain imports and to limit its foreign borrowing, so that it maintained a high standard of creditworthiness despite poor overall economic management; this pattern was quite similar to China's from the 1950s through the 1970s.

The years of Mrs. Gandhi were marked by steady deterioration of the political institutions and by the sporadic emergence of more sensible economic management. She made an abortive effort to rule by Emergency fiat, as has been done successfully in many Asian countries, but this aborted when she failed to make sufficient economic reforms to create a takeoff and when her arbitrary measures created a backlash against corruption and authoritarianism. She was ousted in a democratic election, then returned to power when the opposition proved too divided to govern.

Fearful for her power, she systematically dismantled all potential bases of opposition and used every state institution as a base of patronage. She increasingly resorted to demagogic attacks on minorities, on foreign countries, and on anyone who appeared to be gaining political power. By doing these things she safeguarded her personal power at the cost of worsening the numerous tensions of Indian society and weakening the national institutions which had given India the capacity to cope with those strains. This was the way Marcos destroyed the Philippines' polity and economy, and the eventual results would have been similar. All of this was documented in last year's review, seven months prior to the assassination of Mrs. Gandhi. Assassination was the price she and her country paid for her divisive policies.

Simultaneous with these political developments, the Indian economy had experienced the fragile beginnings of some auspicious developments. Patient investments in agriculture had largely made the country self-sufficient in

\* any ruler can be  
assassinated by discontents

the assassination in many ways  
have  
be  
Durable  
effect of arresting  
this undesirable trend.

rice. Urgent efforts dramatically reduced the country's formerly dangerous dependence on imported petroleum. Modest modifications of the constraints on production of consumer goods had created a significant improvement in consumer sectors. Mrs. Gandhi's weakening of the institutions which implemented central controls also created space within which consumer industries could improve. There were the beginnings of a slightly less restrictive attitude toward foreign investment and foreign commerce generally.

After Mrs. Gandhi's assassination, the country lacked credible national leaders -- testimony to the effectiveness of her effort to destroy all potential bases of opposition. Lacking either opposition or Congress Party leaders of national experience and popularity, and feeling sympathy for the fallen leader even while it expressed revulsion at her policies, India chose its new leader by dynastic succession. Rajiv Gandhi, Indira's son, was not an obvious candidate to run a nation of over 700 million people. Unable to complete his undergraduate degree, he had become an airline pilot. He demonstrated no interest in politics until, following the death of his brother Sanjay, his mother drafted him as an advisor and Congress Party leader. When his mother died, he became, once again by default, India's prime minister.

Notwithstanding the weakness of his qualifications, Rajiv elicited an outpouring of public support. His demeanor was calm, his speeches statesmanlike. He campaigned on a platform of national unity, clean politics, and economic improvement.

In the subsequent election, his platform, his demeanor, the public's sympathy, and the absence of credible opposition created the greatest landslide in Indian history for both the Congress Party and its leader, Rajiv. The national opposition parties of both right and left were destroyed; the resulting vacuum was partially filled by emerging regional parties.

In the aftermath of the election, India has experienced a national euphoria. Most of India believes that Rajiv will repudiate the legacy of his mother's political errors and widen the cracks through which economic expansion has begun to occur. This confidence benefits the economy.

It remains to be seen how far Rajiv will proceed in the promised directions. He has been slow to replace the old advisors and administrators, and it is too early to tell whether this results from wise caution in implementing a strategy for change or from indecision. He has not yet shown how he will deal with the crises in Punjab and Assam, nor has he yet made a move to undo his mother's provocation of Pakistan or to ensure a workable relationship with troubled Sri Lanka. While he has promised cleaner politics, he has not told how he will replace the corrupt financing of the Congress Party. He has proclaimed that his mother erred in using dubious means to unseat opposition state governments, but he has not yet established a record of restraint. Whether his appointments to government offices and state firms will promote strong and competent leadership remains to be seen.

The euphoria may be correct. If so, we will see the gradual emergence of:

- new means of financing the Congress Party;
- local elections to provide the Congress Party with a local base;
- younger advisors on economic policy;
- reduced physical controls on private industry;
- reduced subsidies for state enterprises;
- greater openness in foreign economic policy;
- firm but conciliatory moves in Punjab and Assam;
- conciliation of Pakistan.

Such a scenario would gradually but decisively increase India's investment, growth, and trade. In such a scenario, India's need for financing would increase, creating opportunities for foreign banks. Credit officers would have to watch the increase of debt more carefully than at present, but a tradition of financial conservatism would remain a strong influence.

Alternatively, Rajiv could prove to be effective at articulating India's desires but ineffectual at choosing and implementing the necessary reforms. India would then continue to shuffle along as the old elephant of the third world, offering limited risks and limited opportunities, more creditworthy and more stodgy than most of the third world, but with a long-term trend toward deterioration of the central government. The huge vote for the Congress Party would not foreshadow the rebuilding of a national institution, and the fragmentation of the opposition into regional parties would worsen India's fissiparous tendencies. Emphasis on heavy industry would persist, and the state enterprises would constitute a growing drain which could eventually threaten the country's financial standing. Such deterioration could eventually threaten the country's creditworthiness; in the short run, however, it could enhance growth by opening opportunities for states to innovate and for some industries to evade controls.

India moves very slowly. Its complexity and inertia provide time to wait and watch before acting. The assassination of Indira Gandhi did not detract from India's creditworthiness, and the euphoria over Rajiv's election has not yet decisively improved it. India's longer-term prospects are better than they would have been had Indira survived, because she had set the nation inexorably on a bad course and her son now has an opportunity and a mandate to improve the course. But he has not yet defined his course.