

# BTI 2008 | India Country Report

<b>Status Index</b>	1-10	<b>7.35</b>	# 25 of 125	
Democracy	1-10	8.10	# 21 of 125	➔
Market Economy	1-10	6.61	# 42 of 125	➔
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scale: 1 (lowest) to 10 (highest)    score    rank    trend

This report is part of the Bertelsmann Transformation Index (BTI) 2008. 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 125 transformation and developing countries are evaluated.

The BTI is a joint project of the Bertelsmann Stiftung and the Center for Applied Policy Research (C•A•P) at Munich University.

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Please cite as follows: Bertelsmann Stiftung, *BTI 2008 – India Country Report*. Gütersloh: Bertelsmann Stiftung, 2007.

## Key Indicators

Population	mn.	1,094.6	HDI	0.61	GDP p.c.	\$	3,072
Pop. growth <sup>1</sup>	% p.a.	1.4	HDI rank of 177	126	Gini Index		36.8
Life expectancy	years	64	UN Education Index	0.61	Poverty <sup>3</sup>	%	80.0
Urban population	%	28.7	Gender equality <sup>2</sup>	-	Aid per capita	\$	1.6

Sources: UNDP, Human Development Report 2006 | The World Bank, World Development Indicators 2007 | OECD Development Assistance Committee 2006. Footnotes: (1) Average annual growth rate 1990-2005. (2) Gender Empowerment Measure (GEM). (3) Percentage of population living on less than \$2 a day.

## Executive Summary

India is today a fully consolidated, inclusive democracy with no extra-constitutional veto players. Poor law enforcement, a sluggish judicial system that often results in justice being denied, a lack of political neutrality among the police forces, and poorly protected civil rights in tension-prone areas constitute the most glaring deficits in this otherwise successful model of transformation. India's economic order has undergone far-reaching, rapid transformation since 1991, giving the country one of the most dynamic economies in the world. Productivity in the services and manufacturing sectors, spurred primarily by local investment, has fueled India's economic ascent, although agriculture continues to lag further and further behind. There are still a number of reform deficits, especially in regard to cutting heavy public deficits, slashing unproductive subsidies, eliminating the massive infrastructural backlog, and bringing labor, land and bankruptcy laws in line with international standards. Some of these deficits have already been tackled in the last two years, albeit cautiously; more must be done if the government is to sustain 8% annual growth.

India's relatively good BTI rankings for the state's monopoly on the use of force, the efficiency of administration, judicial independence, and the high esteem of democratic procedures remained consistent during the period under review. The government tried and succeeded in making the political and economic process more inclusive by increasing expenditures for basic education and health, investing in rural infrastructure, and launching a massive employment guarantee program in the most underdeveloped districts. Care was also taken to accommodate the grievances of minorities such as tribal groups and Muslims, and to find a negotiated solution for long-standing regional conflicts (Kashmir, northeast India). This effort ran parallel to efforts to come to better terms with India's neighbors, especially with Pakistan, where the composite dialogue was followed up, leading to substantial improvements for the local population in

Kashmir. The Indian government also took the lead in furthering regional cooperation by making greater concessions than other involved parties. In the economic arena, there was a definite slowdown of further economic reforms, especially in regard to privatization, liberalization of foreign investment, and progress in making the currency fully convertible. Declining reform momentum was accompanied by fiscal prudence, introduction of less market-distorting taxes (e.g., VAT), a further scale-down of customs rates, and conservative monetary policies. The political process has become more inclusive, elites of formerly disadvantaged groups have been empowered, effective decentralization is making progress, but gender gaps remain, and regional and personal income distribution has deteriorated slightly.

## 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 reform. 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, have been economically empowered and assumed 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 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 completely transformed India into a vibrant and dynamic market economy, where only a few sectors are closed to private enterprise and international investment, 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.

## Transformation Status

### I. Democracy

#### 1 | Stateness

There are virtually no problems of stateness in India. The state's monopoly on physical violence is nearly complete, apart from some rural conflict zones in central India (Naxalite), areas of separatist activity in Kashmir, and some small states in northeast India. In these regions, insurgent groups sometimes run a rather circumscribed kind of parallel administration.

Monopoly on the use of force

Identification with the nation and the definition of nationality pose no real problems. A few splinter groups in zones of separatist activity do not regard themselves fully as citizens of India. Less radical groups in these same regions would be content with the award of a generous degree of regional autonomy or by acknowledging their economic grievances, and have intermittently signaled a willingness to negotiate these issues.

State identity

The secular credentials of the country were more or less fully restored at the national level after the new government, the United Progressive Alliance (UPA), took power in late 2004, although, at the state level, endeavors to indulge in communal politics should be noted (initiatives against "forced" conversion, against cow slaughter, etc.). Initiatives to improve the socioeconomic status of Muslims, and to restore the traditional rights of tribal peoples with regard to land and forest products, have begun recently. The rising importance of Hinduism in politics, and the acceptance of this influence by a large majority of the Indian population, has challenged the traditional laicist model of Indian democracy. The Hindutva party, the Bharatiya Janta Party (BJP), has become the second strongest party and a major political force in the Indian parliament. This development may initiate a transformation of the political system from a secular model to a model where religion is written into the constitution, like in Islamic states, or Hinduism in Nepal.

No interference of religious dogmas

India inherited an efficient administration from the colonial government, with recruitment and promotion policies based on merit. This heritage was undermined

Basic administration

to a certain degree by increasing reservation quotas for certain sections of the population and frequent, politically motivated transfers of officers. These tendencies are more pronounced at the state level, where administrations were practically politically colonized. Indian police forces are highly inefficient, politically dependent and corruption-prone. As a consequence, the conviction rate of criminals is low, police atrocities against civilians are frequent, and the government quite often has to rely on the army to quell internal disturbances. Changes for the better are coming into sight, however, since the Supreme Court has mandated the establishment of a police commission to look into such matters, and 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, fair and more or less violence-free elections, accompanied by increasing voter turn-out (especially among the poorer and underdeveloped segments), increasing sophistication and independence of voters, and therefore by increasingly frequent and peaceful power transfers. Even in conflict-ridden union states (e.g., Punjab, Kashmir), elections have led and lead to political de-escalation, so much so that they have been used explicitly for this purpose.

Free and fair  
elections

There are literally no veto powers or political enclaves. The military has always exhibited maximum political restraint; it is under strict civilian control and conceives of its own role in purely professional terms. Civic associations (unions, employer federations) have always acted as junior partners of the government and are fragmented, politically affiliated and rather weak (thee occasional militancy notwithstanding). Since there are few intermediaries between the government, the governing parties and the population, elected rulers have a nearly unlimited power to govern at large.

Effective power  
to govern

Freedom of association is fully guaranteed, and the formation of interest groups is legally straightforward. Consequently, associations, unions, NGOs and social movements proliferate (although association density is moderate). Most of them are poorly institutionalized and politically fragmented, or act as frontal organization of their respective parties and lack internal democracy. Social movements and NGOs abound, and these often act as democratic, social or environmental watchdogs, such as advocacy agents for less privileged groups or even as intermediaries in communal conflicts; not all of these groups are free of political interference. Strikes and demonstrations are frequent and are only rarely dissolved or discouraged.

Association /  
assembly rights

India can boast of the largest and growing circulation of free, discerning and outspoken newspapers, of every different political shade, in all national and

Freedom of  
expression

regional languages. Nearly every political party, association or social movement has its own publication. Citizens also have a broad choice among a multitude of state and private television channels, which report nonstop on political developments. Although freedom of expression is undermined in rare instances, this has more to do with radical popular movements than with state repression.

### 3 | Rule of Law

Horizontal division of power is assured, and vertical division, though often restricted by politically motivated replacement or undermining of state governments, has been restored in the wake of coalition government since the 1990s and their dependence on smaller, regional parties. The parliament's control of the executive suffers from modest professional competence among parliamentarians and a lack of support for the gathering of data and research.

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 tightly controls the upkeep of stipulated election codes. The courts remain institutionally autonomous, in spite of pressures by the executive, as well as interference in the nominations and transfers of politically unpopular judges. The upper courts recently undertook an effort to restore their independence in nominations. Rule of law is restricted by understaffing and the slow functioning of judicial institutions, leading to massive accumulation of unfinished litigation and the keeping of accused but unconvicted people in custody. Low thresholds for initiating and prolonging processes, as well as overly detailed laws and regulations, also aggravate these problems. Underprivileged sections of the population shy away from the courts because they remain unaware of their rights, and litigation costs remain prohibitive.

Independent judiciary

Misuse of public office is frequent in India and only sanctioned intermittently (today more than before). This has to do with the modest transparency of administrative transactions and the heavy regulation of the economy, which is slowly relaxing after economic liberalization. The culture of corruption is deeply entrenched in India, leading to the factual bidding for offices with the highest expectations for bribes. As a consequence, India is still listed in the upper ranks of several international rankings on corruption and malpractices.

Prosecution of office abuse

Civil rights are ensured, except in regions where emergency laws prevail. Rights of underprivileged groups are limited by private security forces, which often act with impunity. Relevant protection laws are not enforced satisfactorily, the

Civil rights

judicial system is sluggish, which leads to unreasonable delays in the completion of criminal cases, and the accused are often victimized while in police custody.

#### 4 | Stability of Democratic Institutions

Democratic institutions in India are more or less stable, with the exception of infrequent destabilizations of state governments (for political ends), the shaky character of multiparty governments in the last decade (which conferred political blackmail power on even minor parties), combined with the endemic defection of parliamentarians to the opposition or new parties to profit from new political equations. This has also delayed important constitutional and economic reform projects. Institutional efficiency is also hampered by continuing heavy regulation of the economy, proliferation of ministries and government agencies, and the aforementioned congestion of the judicial system. It is fair to say, however, that the record has definitely improved recently, in that a consistent government program could be carried out, aiming at the improvement of the weaker sections. A new anti-defection law in 2004 tried, with some success, to curb defections by limiting the premium for rebels.

Performance of democratic institutions

Democratic institutions are highly accepted and esteemed, even if particular institutions, such as the parties or the police, are not trusted. Even the poor have the sense that their vote carries weight, and they take pains to register for voting. Democratic competition is the only game in town, except for small radical groups. Even they opt intermittently for inclusion in the mainstream.

Commitment to democratic institutions

#### 5 | Political and Social Integration

The Indian party system is relatively stable, volatility is low and the system rewards centrist tendencies because of the extremely pluralistic character of society. This means that coalition building for government is easy. Most parties are nevertheless weak institutions, and party discipline is low despite measures against floor-crossing. Formal organizational structure and programmatic appeals have been replaced by informal procedures, clientelism, and mobilization along ascriptive identities. The communist parties and the Bharatiya Janata Party (BJP), with its disciplined frontal organizations, represent an exception to this pattern. The poorly institutionalized character of Indian parties does not hinder their effectiveness as election machines and as institutions for setting government agendas. It also does not hinder the progressive empowerment and recruitment of lower strata into the party structure.

Party system

Millions of people are members of associations in India, but interest groups are rather weak, fragmented across ideological and party lines, and they often fight

Interest groups



against each other rather than against their opponents. This is also why labor relations are rather conflict-prone. Because of the long-standing 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 (of women, for environmental or human rights concerns, etc.) have become more visible and assertive. They are dominated by members of the middle class, but often act as advocacy associations for lower strata. Missing associational links between the population and interest groups are to some degree compensated for by direct links between parties and social groups.

Social movements and civic organizations of different kinds are highly visible and assertive. Members of the middle class dominate these movements. The lack of associational links between the population and interest groups is to some degree compensated for by direct links between parties and social groups. Although there is a very broad and robust network of social organizations and civic associations, the deeply communal character of associational life and the segmentation of organizational life along religious, ethnic or caste lines contributes to the fragmentation of associational life into several "sub" or "partial" societies. Social trust between various communal groups and between castes is fragile or low.

Associational  
activities

## II. Market Economy

### 6 | Level of Socioeconomic Development

According to commonly used development indicators, India is still regarded as a lower-income country, although it is progressing quite rapidly. Its development level, measured by the HDI, nevertheless does not assure every citizen's basic needs or freedom of choice. India still has the largest number of people living in absolute poverty (around 26% of the population). Incidence of poverty has declined since the mid-1970s, albeit lately at a decreasing rate, but is increasingly geographically concentrated. Development progress was uneven, and the difference in social indicators between union states increased in the 1990s. Poverty and social exclusion is concentrated in some economic sectors (agriculture, informal sector), some social groups (lower castes, tribal peoples, Muslims), and union states with poor endowments, a poor record of reform, and bad governance. There is no equal opportunity in spite of moderate inequality, numerous programs for poverty eradication, and assertive action on behalf of the underprivileged.

Socioeconomic  
barriers

Economic indicators		2002	2003	2004	2005
GDP	\$ mn.	507,799	601,804	695,856	<b>805,714</b>
Growth of GDP	%	3.7	8.4	8.3	<b>9.2</b>
Inflation (CPI)	%	4.4	3.8	3.8	<b>4.2</b>
Unemployment	%	-	-	5.0	-
Foreign direct investment	% of GDP	1.1	0.8	0.8	<b>0.8</b>
Export growth	%	21.9	9.8	18.2	<b>21.9</b>
Import growth	%	10.3	11.7	45	<b>22.1</b>
Current account balance	\$ mn.	7059.5	6853.2	-	-
Public debt	\$ mn.	82,256.5	84,640.1	89,004.4	<b>80,280.9</b>
External debt	\$ mn.	105,019.9	112,854.6	124,375.8	<b>123,123.0</b>
External debt service	% of GNI	3.1	3.5	2.8	<b>3</b>
Cash surplus or deficit	% of GDP	-4.7	-3.7	-3.6	-
Tax Revenue	% of GDP	8.8	9.2	10.2	-
Government consumption	% of GDP	11.9	11.2	11.0	<b>11.3</b>
Public expnd. on edu.	% of GDP	-	3.7	-	-
Public expnd. on health	% of GDP	0.9	0.8	0.9	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	2.9	2.8	3.0	<b>2.8</b>

Sources: The World Bank, World Development Indicators 2007 | UNESCO Institute for Statistics | 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. A formerly dense regulatory environment has been significantly simplified in most sectors, with the exception of agriculture, labor and land markets; business transactions with the administration remain cumbersome, costly and time-consuming. Several hundred products are still reserved for exclusive production by the small-scale sector, obstructing their employment potential. Regulation of foreign and big local companies was given up, and the investment regime is now 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 was not always followed by sufficient regulation of the new ventures, allowing windfall profits for the new owners. Legal procedures for the restructuring and liquidation of private or public companies are inadequate, time-consuming and inefficient, thereby obstructing the mobilization of economic assets to more productive uses. Weak shareholder protections encourage risky company strategies.

Anti-monopoly  
policy

Trade barriers are still considerable, notwithstanding massive tariff cuts and the nearly complete abrogation of non-tariff barriers. The average tariff rate stands at about 16% (2006); protection is enhanced by the frequent use of anti-dumping measures, where India ranks at the top. Customs clearance is still more time-consuming than in comparable economies.

Liberalization of  
foreign trade

The Indian financial system is highly developed and robust. 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. Equity capital of banks is sufficient to cover potential losses of non-performing credits (whose share has come down). The stock market is well developed and buoyant.

Banking system

## 8 | Currency and Price Stability

India has followed a consistent policy of price stability, mainly for political reasons (tolerance for inflation was traditionally low). This did not change much during the period under scrutiny, although high public deficits and mounting oil prices made the containment of inflation sometimes difficult. The Central Bank of India has always pursued a cautious monetary and currency policy, supported by strong internal mobilization of savings (by private households) and increasing inflows of foreign capital and remittances. Currency reserves reached a record level in 2006 (around \$165 billion). There was therefore some upward pressure on the currency, contained by the reserve bank through sterilization of inflows.

Anti-inflation /  
forex policy

The consolidated fiscal deficit of the union and the states reached a record level in 2002 – 2003, far above the level of most comparable countries and hardly sustainable, although financed mostly from internal sources. The newly elected government acted immediately and passed a Fiscal Responsibility and Budget Management Act, aimed at fiscal balance till 2008 – 2009 and supplemented by similar initiatives of state governments. Due mostly to increasing tax revenues, deficits did decline afterwards, with a pause in 2005 – 2006. This pause is attributed to higher transfers to the states, which were mandated by the finance commission, and the launching of ambitious programs for the improvement of physical and social infrastructure, and for a new employment guarantee measure

Macrostability

in rural areas. With the persistent economic boom and the introduction of a buoyant value-added tax in 2005, fiscal balance seems possible in the near future. External indebtedness has come down to a manageable level, but internal indebtedness is still very high (80%) and absorbs (via interest payments) more than a quarter of public revenues.

## 9 | Private Property

Property rights are adequately defined, although the constitution allows restrictions in the public interest. No state government or important political party questions the upholding of property rights, the prerogative of private initiative and the necessity to attract foreign investments. Acquisition of new land for private use by companies is however very difficult, costly, and heavily contested politically.

Property rights

Private local and foreign companies are allowed in nearly every sector of the economy, although clearance is still time consuming and costly. In a narrowing range of product lines, only small-scale companies are allowed to do business. Agriculture and allied industries are still heavily regulated. Privatization of public companies was proceeding at a slow pace since the mid 1990s, accelerated after 1998 (except in the states), and came to a near complete halt after the new government took office in 2004.

Private  
enterprise

## 10 | Welfare Regime

In India, there is only a rudimentary system of social security for the privileged workers of the state and formal sector, although in 2005 the government introduced an employment guarantee for the poor in rural areas and is investigating a system for the informal sector. There is a whole gamut of federal and state poverty programs providing subsidized food and cooking oil, employment during crisis periods, credit for self-employment and ad-hoc rehabilitation packages. These programs are still badly targeted, leading to significant spread effects to the non-poor, notwithstanding recent improvement efforts. Public expenses for basic social services are inadequate by international comparison and do not guarantee universal coverage, leaving aside the question of their mostly poor quality.

Social safety nets

India is not a frontrunner in improving social indicators. There are wide variations between states, districts within states, religious and social groups. As a consequence, equality of opportunity is not assured; social indicators correlate positively with income, position in the caste order, and urban environment. Women are systematically disadvantaged, especially in the underdeveloped

Equal opportunity

“Hindi belt,” which is demonstrated by the massive female deficit in the population. Members of the lower castes, tribal groups and Muslims are discriminated against in terms of land ownership and in access to public sector positions.

## 11 | Economic Performance

The Indian economy has grown at a rapid pace in the last few years, faster than most other developing countries. Growth is most pronounced in the service sector, slightly less pronounced in industry and even less in agriculture. It is driven by total factor productivity growth, buoyant internal and external demand (exports are shooting up), but growth remains somewhat jobless. Moderate investment rates have increased lately to a level where, in combination with further deregulation, fiscal prudence, provision of adequate educational facilities, and the liberalization of agriculture and the small-scale sector, growth rates of 8% and more are sustainable and the absorption of the increasing workforce is feasible.

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), mainly due to unsafe water, air pollution and soil degradation. The main victims of this degradation are the poor. There are specific laws to keep the environment safe, as well as environmental movements. In this respect, a pronounced activism of NGOs and the courts has to be acknowledged. Adequate funding for environmental programs, sufficient inspection and monitoring of progress are still lacking. Total area of natural parks nevertheless increased, a new forest policy was implemented (increasing reforestation), emission levels of factories came down, and courts have become more proactive in prosecuting polluters.

Environmental policy

Education in India leaves much to be desired. Enrollment into the primary and secondary system increased and gender disparities went down, but millions of children are still out of school, dropout rates are massive and – most importantly – the quality of education in terms of cognitive achievement is very poor. Student achievement is in addition highly influenced by geographical, social and religious factors. Parents who can afford to do so have opted out of public schools to proliferating private institutions, which are, however, inadequately monitored and regulated. The Indian government does not provide adequate resources for the educational system, and secondary school financing has been especially neglected. On the other hand, India can boast of a full range of good colleges,

Education policy / R&D

universities and elite institutions that produce a sufficient number of graduates for future-oriented economic sectors. In India's formerly closed economy, private companies were traditionally averse to research, and public research was heavily biased towards defense and nuclear applications. This has slowly changed because of stiffer competition in the local market, technology transfers and research outsourcing via foreign investment.

# Transformation Management

## I. Level of Difficulty

Difficulties in regard to democratic consolidation in India are moderate. This has to do with a long tradition of popular participation, the deep roots of democratic institutions, the missing veto power of other political actors and the balancing out of multiple, cross-cutting social, regional and religious cleavages. Difficulties in managing economic transformation are considerable, as further reforms stumble over the protracted resistance of left and regional parties and their affiliated unions, which block nearly every proposal, from privatization to an increase of public prices for essential commodities to making the currency fully convertible. Difficulties in managing transformation are also significant because of the multiparty character of the governing coalition, making every move dependent on the wishes of minor parties that have no stake in the common good, but rather a keen interest in furthering the narrow interests of their constituencies. The political necessity to make growth more inclusive after the electoral verdict of 2004 also creates difficulties, forcing the national government to make room for investments in social infrastructure, improve conditions in rural areas, and massive expenses for employment programs, while continuing to clear the backlog in infrastructure. The need to cut subsidies and slash surplus labor in the public sector to manage this transition is often frustrated by the political system's deeply entrenched patronage character. Last but not least, the bureaucracy is keenly interested in the upkeep of discretionary policies.

Structural  
constraints

Civil society is only partially helpful in overcoming these obstacles. Labor unions are highly fragmented and therefore not prone to adhere to any social pact. One must admit, however, that labor militancy declined after liberalization as well as the number of days lost due to labor conflicts. More so than in the past, NGOs and social movements act as guardians of civil and minority rights as well as watchdogs for the quality of political life and government accountability at every level. This does not always make governance easier, as it leads to long delays in public programs (irrigation dams, power generation etc.) and regulations such as the new forest policy.

Civil society  
traditions

Militant conflicts have subsided quite substantially. The conflict over Kashmir was melting down when the government initiated roundtable discussions on the future of the state, initiated negotiations with militant groups, and continued the composite dialogue with Pakistan. The militants are still divided on the issue of negotiating proposals for wide-ranging autonomy, but the number of violent incidents has definitely come down. In the conflict prone northeast, the government also acted responsibly, amending emergency acts to better protect human rights (Manipur), entering into negotiations with militant groups – which, however, sometimes broke down – and spending substantial sums on developing the hill regions. An important bleak spot remained the handling of the Naxalite problem, where Maoist-inspired militant groups fight for the rights of the landless. The government dealt with the Naxalites more or less exclusively by military means when peace negotiations broke down in early 2005. The Naxalite movement has now spread to over 160 districts. Religious conflicts subsided after the new coalition government took over.

Conflict intensity

## II. Management Performance

### 14 | Steering Capability

The government is able to prioritize actions even under difficult circumstances. The government's aim to develop India into a hub of global economic activity and as a great power on the international scene remains in sharp focus. Government policy is guided by a Common Minimum Programme, where priorities are set and followed.

Prioritization

Implementation of new programs and initiatives suffers often from protracted political conflicts over details, long delays in the formulation of execution rules, overlapping mandates of administrative units (a specific case is the hesitant delegation of functions to local authorities), the excessive number of new programs put alongside old ones, such as primary education, and an overemphasis on inputs instead of outcomes.

Implementation

The political leadership is capable of learning from past errors, but only with a pronounced time lag, caused by conflicting social forces and their political representatives. Reforms have therefore proceeded in a highly incremental way, quite often by stealth. Recent vivid examples are the gradual improvement of tribal rights to forest lands, which have spread over more than 20 years, the cautious and incomplete targeting of subsidy programs, and the hesitant pass-through of higher oil prices to local consumers.

Policy learning



## 15 | Resource Efficiency

The government does not use the financial and personnel resources available for transformation very efficiently. The budget deficits of the Union government and the states are still massive; they amount to 7.6% of GDP (not including shadow budgets, guarantees etc.) and absorb a high share of savings, crowd out private investment and public investment in critical areas such as infrastructure, maintenance, and education and health. Poorly targeted and partly unproductive subsidies are in part to blame for these deficits, as are generous salary increases in the public sector, a mounting interest burden and inadequate efforts to mobilize tax resources from agriculture and the services sector. Mobilization efforts have improved as value added taxes have been introduced, loopholes closed and tax compliance improved. Public expenses management suffers from poor services monitoring, poor targeting and corrupt practices. Earmarking for operation and maintenance of facilities is far too low, contingent liabilities (for pensions and guaranteed) are not adequately dealt with, and budget forecasts are often too optimistic. The new Fiscal Responsibility Act, and parallel legislation in the states, have already brought a certain turnaround; deficits went down, public investments showed a marked rise and – even more importantly – resources were made available for neglected sectors (rural infrastructure, education, employment programs) and groups (Muslims, tribal peoples).

Efficient use of assets

Coordination of conflicting objectives is hampered by political forces moving in different directions and by the overlapping mandates of far too many departments. At the federal level, coordination was improved by the establishment of several inter-ministerial committees and a coalition steering body. Coordination between the union and the states, however, still leaves much to be desired.

Policy coordination

Corruption is well entrenched at every level of the polity and administration; it 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 certainly a basic lack of respect for legal endeavors to end malpractice, especially among the political leadership, who are among the most visible culprits. Escalating campaign expenses, unaccounted-for donations to political parties and a vivid patronage culture are responsible. As investigations are rare and stretched out, very few politicians or civil servants have been convicted in India.

Anti-corruption policy

## 16 | Consensus-Building

Agreement on India becoming a full-fledged market economy and consolidated democracy is widespread among all relevant political actors. This does not mean that they necessarily agree on the means to reach these ends. There are pronounced factual debates on the proper share of the public and private sectors in economic activity, on full currency convertibility, on the need to push reform toward a full-fledged market economy or fully consolidated democracy. This results in political stalemate or, in the best of circumstances, in slow but consensual progress.

Consensus on goals

There are no genuine veto actors. Militant groups are dealt with harshly if they do not give up their violent agenda, but can be brought back into the political mainstream if they compromise.

Anti-democratic veto actors

Political cleavages are accommodated as much as possible, for example by reservation policies, development packages, or the creation of new states or autonomous regions; emerging groups are incorporated into the political leadership. In rare cases, this statesmanship is thrown over board for political mileage.

Cleavage / conflict management

Civil society's participation in the political process has clearly increased. India is sometimes referred to as the NGO capital of the world, with up to 100,000 different organizations and self-help associations. Protests, demonstrations and strikes are an everyday occurrence. NGOs have also become more institutionalized, supported by generous donations from the local population and international agencies. Transfers are still tightly controlled by the government, which is also the main cooperation partner of the associations and certainly the most important addressee of demands. 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. Rehabilitation of past victims of communal conflicts, natural disasters or land alienation suffers from undue delays, avoidance of responsibility and limited compensation. The record is improving, however, as recent compensatory policies towards tribal peoples, Muslims and the lower castes illustrate.

Reconciliation

## 17 | International Cooperation

International development cooperation plays only a very limited role in the initiation, implementation and financing of market reforms or in pursuing democratic progress. The Indian government intends to do without foreign aid in the future and is cultivating a self-confident posture in contact with donors. That does not mean that the union or state governments are not cooperative. Quite a few union states initiated far-reaching reforms in the educational, health and infrastructural sector or in regard to the overall approach of market-friendly reforms, supported by international organizations. In principle, however, there is no chance for a political dialogue dictated unilaterally. Liberalization and regulation of foreign direct investment is also done more with an eye to the local constituencies – and therefore hesitantly – than to foreign partners, although the need to attract more foreign investment is acknowledged by governments of all political shades.

Effective use of support

The Indian government has become a reliable partner in combating international terrorism and in curbing nuclear proliferation. It was and is actively engaged in a multitude of peacekeeping missions and is actively backing and broadening its engagement in multilateral and regional organizations. This, however, does not mean that the government is not obstructing progress in specific instances where perceived Indian interests are negatively affected, such as WTO negotiations, or the nonproliferation treaty.

Credibility

India has often displayed an overbearing and uncompromising attitude towards its neighbors. In the last few years, India has demonstrated a new willingness to incur higher costs to accommodate neighbors in regional cooperation, to restrain from excessive political interference (e.g., Nepal and Sri Lanka) and to deal on a constructive basis with long-standing conflicts such as Kashmir. The peace dialogue with Pakistan proceeded during the period under review. India and Pakistan improved the transport system between both countries and extended their diplomatic relations, especially on topics related to the future of the disputed Kashmir territory.

Regional cooperation

## Strategic Outlook

The Indian government aims to convert the country into a developed economy by 2020 and into a major player on the global scene, both of which seem highly feasible. Supported by wide-ranging reforms, the country has experienced rapid, productivity-led growth over the past decade. The rapid growth of exports, increasing foreign investments and high remittances have resulted in a turnaround of the current account balance. Parallel to faster growth, India has made progress in many social indicators and has reduced income poverty. Governance performance has, however, been uneven; average income remains low and there has been little movement on some critical social indicators. There also remains a substantial disparity of opportunity, particularly in the education, health and economic security of vulnerable groups. Income disparities are increasing between faster and slower growing regions, between skilled and unskilled workers, but are still manageable and less pronounced than elsewhere. India is endowed with a growing range of world-class enterprises, a reservoir of highly skilled workers and enjoys a window of opportunity because it is still in the first phase of the demographic transition. Democratic consolidation and the political incorporation of the lower strata have already been achieved, so that political turmoil should not unduly obstruct development. The government should be encouraged to foster greater balance in sharing the fruits of economic growth. The people-friendly program of the new Indian government is therefore headed in the right direction; this should be complemented by fiscal restraint, efforts to broaden the tax net and a rebalance of expenditures to make room for the rehabilitation of infrastructure, to vitalize agriculture and improve educational and health services. Broad participation in economic growth will certainly make the needed additional reforms acceptable. One long-term strategic challenge is to ensure environmental sustainability in the context of diminishing water availability and increasing pollution. The democratic credentials of the country are not in doubt but could be improved by stricter observance of the federal setup and by efforts to reform the judiciary and clear the massive backlog of litigations. The high courts and the election committee have, however, followed a more assertive course and have become more proactive in prosecuting malpractices. This should be encouraged, as it will help, together with improved procedural transparency in government that is supported by freedom of information acts, to restrain corruption in general. The international community should encourage policies that reasonably accommodate genuinely local-based rebel groups in the northeast. The efforts of foreign-sponsored terrorist groups in Kashmir to destabilize peace efforts should be unequivocally condemned, as should the prosecution of minorities such as Christians or Muslims by Hindu radicals.