

CATO INSTITUTE

BOOK FORUM

"INDIA UNBOUND: A PERSONAL ACCOUNT OF A
SOCIAL AND ECONOMIC REVOLUTION FROM INDEPENDENCE
TO THE GLOBAL INFORMATION AGE"

Monday, April 22, 2002

Moderator:

Ian Vasquez, Cato Institute

With Remarks by the Author,

Gurcharan Das

And with Comments by:

Swaminathan Aiyar, Economic Times (India)

The Cato Institute

F.A. Hayek Auditorium

Washington, D.C.

P R O C E E D I N G S

MR. VASQUEZ: Welcome to the Cato Institute. My name is Ian Vasquez. I direct the Project on Global Economic Liberty.

India has fascinated development economists since the time of its independence, when the country was viewed enthusiastically and with quite a bit of hope as a place where development experts and the Indian elite could test out some of their theories on one of the world's largest populations. In many ways, India became emblematic of the Third World's approach to growth. Development planning was urged on the country, as aid expert and development expert John P. Lewis noted in his 1962 book "Quiet Crisis in India." According to him:

Today such planning is officially viewed as an essential concomitant of any national development that merits American assistance. And the United States Government is urging such planning on Latin American, African and Asian governments that do not yet practice it.

As we all know, that approach did not produce the kind of progress that planners had expected. And Indian policymakers, nevertheless, still stuck to the notion of development planning

well into the 1980's. In the mid-eighties, the Cato Institute published a book on development planning, which apparently Prime Minister Rajiv Gandhi read, and we then got a letter from him to the President of the Cato Institute that thanked us for sending him the book but that said:

While there is a problem of collecting, coordinating, sorting out, and analyzing the tremendous amount of information needed for developmental planning at the national level, the solution perhaps lies in improving the tools of collection and analysis of data and not in abandoning the planning effort itself.

That was in 1985. But there has been a big change in India, with high growth rates and the economic reforms of the early 1990's. It is what Gurcharan calls a silent revolution that is transforming Indian society. Economic reform may be lagging somewhat, but the country's integration with the rest of the world, especially in the telecommunications and high-tech sectors, has already influenced the political dynamic. It has led to a dramatic rise in the Indian middleclass. It is leading to the breakdown of the caste system. And it is changing a number of values in Indian society, including attitudes towards entrepreneurship.

Of course, the story of India since independence is much more complex and nuanced than the version that I have presented. Fortunately, our main speaker today has done a fantastic job of providing his own personal account of Indian history in "India Unbound." I highly recommend this book. The author, whose age is roughly that of independent India's, recounts with intimate understanding the concerns and expectations of his family members, businesses, customers, ordinary Indian citizens, politicians, and friends, as India has struggled to make its way from a traditional society to a modern society.

Indeed, Gurcharan catalogs his own evolution of thought, as he gets to know India through many years of travel, research, and business. In this sense, "India Unbound," I would say, is a very wise book, because it is not afraid of critical self-examination and unexpected conclusions.

Finally, let me just note that what happens in India should be of concern to all of us who care about the future of liberalism. Those of us who live in Washington spent the weekend observing the anti-globalization protests surrounding the World Bank and the IMF meetings. In fact, there is much to celebrate about globalization, and India is one reason. Along with China, India makes up half of the developing world's population, meaning that its high growth rates of recent years, quite apart from the

benefits that it brings to Indians, has helped bring the rise of global inequality to an end, and may even be reversing it.

So I am pleased to introduce one of India's most visible champions of democratic capitalism, Gurcharan Das. He had been the CEO of Procter & Gamble India. He also served as Vice President and Managing Director of Strategic Planning for Procter & Gamble Worldwide. He is, as I mentioned, the author of "India Unbound." He has written three plays and a novel. He graduated with degrees in philosophy and politics from Harvard University. He went to Harvard Business School, as well. He is now the Chairman of the Board of Citibank India, as well as a board member in many other companies in his country. And he writes a regular column for the Times of India.

Please help me welcome Gurcharan Das.

(Applause.)

GURCHARAN DAS, AUTHOR,

"INDIA UNBOUND: A PERSONAL ACCOUNT OF A
SOCIAL AND ECONOMIC REVOLUTION FROM INDEPENDENCE
TO THE GLOBAL INFORMATION AGE"

MR. DAS: Thank you, Ian.

And, Swami, it's good to be together with you in Washington.

This is a city where I came as a child, at the age of 11. I went to high school in Washington for a few years before I went to college. And it's a city which gave me a lot, I think. I recount in "India Unbound" how I had a paper route, like American boys at that time, and I used to deliver the Washington Post at 5:30 in the morning, in that icy cold weather. And my parents thought that was good for character. But I have horrible memories of waking up at 5:15 in the morning to deliver the Washington Post. But it did teach me one thing -- that even if it was raining or snowing, I had to deliver. And I had to cover the newspapers, because my customers expected to get a dry newspaper. And so the importance of the customer was something that I first learned in that little experience.

Now, in the next 20 minutes, I am going to offer you a proposition, that if I had offered this even 10 years ago you would have thought me a fitting candidate for the nearest lunatic asylum. I am going to suggest we begin by imagining a map of India. I don't know how many of you can picture a map of India. It's basically an upside-down triangle. You connect the north city of Kanpur with Chennai, which is Madras, and one of the theses of my book is that 50 percent of the people west of that line will turn middleclass by 2020. And it will take another 20 years before the same thing will happen east of the line.

Now, why do I talk about the middleclass? Because most people would talk about poverty when it comes to India. I speak in terms of the middleclass because in any given society, in any society, the top 15 to 20 percent will succeed regardless and we don't have to worry about them. The bottom 15 to 20 percent will fail and we need to look after them. But in between is the 60 to 70 percent that, in successful economies, has become the middleclass.

The tragedy of India over the last 50 years is not that we have poor people but that we deliberately suppressed the middleclass for this period. And even as late as 1980, only 8 percent of the people constituted the middleclass. We have a National Council of Applied Economic Research, NCAER, which makes these definitions. They don't really call it the middleclass. They use the words "consuming class," but the idea is the same. I used their numbers.

The idea was that it was 8 percent. And even now, when the middleclass has more than tripled, and it has exploded over the last 20 years, it is still less than 20 percent of the population. Now, you might say, well, 20 percent of 1 billion, that's 200 million people; that's a large middleclass. Yes, it is. But for the Indian society, it is still a failure until you get to that 50-percent level.

So why do I make this outrageous proposition that India is turning middleclass and is going to turn middleclass? I have two and a half reasons, and I am going to try to persuade you over the next 15 minutes with these two and a half reasons. And they go back really to two very old ideas in economics. The first idea is an idea that goes back to Adam Smith. And that is the idea that if a rich country and a poor country are linked together by trade or investment, then the standard of living of the two should eventually converge. This is called the Theorem of Convergence.

The idea itself is fairly intuitively straightforward -- that if the standard of living depends on productivity, and productivity in turn has so far been linked pretty close to technology, so when a rich and a poor country are linked together the poor country merely takes the technology from the rich country. It doesn't have to reinvent the wheel. The rich country may have taken 50 years, 100 years, to come to that point of technology. And we can see that every day with computers and cell phones that we use in India. They were not invented there but yet they are having a huge impact on productivity for the people who use them.

So the question, though, in your minds, I'm sure, is: But why haven't I seen convergence in the last 50 years? It makes sense that the convergence should take place, but it seems

that the rich countries have grown richer and the poor countries, while they may not have grown poorer but they certainly have not converged. And the answer to that question also is fairly simple -- that they were not linked in the last 50 years, until recently.

Basically, after the Second World War, you had three kinds of countries. You had what we called the First World, the Second World and the Third World. The First World were the rich Western countries. Now, these countries were linked and we did see convergence take place. Because the poor countries before the Second World War -- countries like Italy, Portugal and Spain -- were quite poor. And after the War, by the early seventies, the standard of living started to converge, the Southern European countries with the Northern European countries. So convergence took place in the First World.

The Second World, of course, was the communist world. That was closed. So let's move to the Third World.

The Third World: Jeff Sachs, whom you just quoted, and Andrew Warner, another scholar with Jeff at Harvard, did a study which was published in the Brookings Institution papers in January of 1995, and it's a very good study, where they examined 87 countries. And in these 87 countries they found that 74 of these 87 were closed. Only 13 were open. That means they were linked with the global economy.

The 13 that were open grew six times faster than the 74 that were closed. This was a study done between 1965 and 1990, so 25 years. Over that 25-year period, the 13 open economies outperformed the others by six times. And can you guess where those 13 virtuous countries were? Most of them were in the Far East. So, in fact, convergence did take place certainly for those 13 virtuous countries.

The difference, though, now between the world in 1970 is only 20 percent of the world's population lived in open economies. Today, more than 80 percent of the world lives in open economies. And I count China also as part of that. They defined openness in a very technical way, but I think intuitively one could certainly say that China is an open economy.

Anyway, the point is that today 80 percent of the world lives in open economies. And of all the reforms that we did in 1991 in India, I think the most important one was to link ourselves with the world. That was where essentially we lowered import barriers, lowered import tariffs, made the currency slowly convertible on the trade account, and really joined up with the global economy. We still have high tariffs compared to many countries, but it is a sea change over what existed.

And really, the fundamental reason to believe what I said about 2020 and 2040 is the economic reforms that we have done and that we are in the process of making happen. A lot of

us get very frustrated at the slow pace of those reforms, but the direction has been pretty much one way, in the right direction, since 1991. And I would say that if you look at the performance of the Indian economy, it is hard to do a one-to-one linkup between growth rates and reforms. But, nevertheless, if we look at a wide enough picture -- let's take 100 years, from 1900 to 2000, a big enough time period -- and now I'll speak these numbers, so you will have to write them down if you want to note them -- between 1900 and 1950, the Indian economy grew around 1 percent, but the population also grew around 1 percent. So the per capita income grew at zero. And that is why we rightly said that our economy had been a stagnant economy in the Colonial period.

After independence, from 1950 to 1980, the economy's rate of growth picked up, to 3.5 percent, but the population also picked up, from 1 percent to 2.2 percent. So, in fact, the net per capita income growth was 3.5 minus 2.2, which is 1.3. And this is what we moaned and groaned was the Hindu rate of growth. Because after doing everything, you still got 1.3. Mind you, India was one of those 74 closed economies, so its growth rate mirrored pretty much the growth rate of the 74 countries.

Between 1980 and 1990, the growth rate picked up. It picked up to 5.6 percent. And the population growth rate basically stayed pretty much the same at 2.1. But you still got

5.6 minus 2.1, so you have 3.5 percent per capita income growth. Now, that is beginning to move upwards.

And from 1990 to 2000, the last decade, the growth rate has been 6.4 percent per year, and the population, for the first time in decades, has begun to slow down. It's a small slowdown. The average still for the decade was 1.8. But you are talking about a per capita income growth of 4.6. Now, if any of you has a compound interest calculator, you can see that over 10 years of a 4.6 percent growth rate certainly means that the economy is more than 50 percent richer at the end of the decade than it was before.

So here is an economy which, if you average for the last 20 years -- and let's get out of reforms; this is non-reforms -- this is an economy that has grown at 6 percent average for 20 years. Now, you have to remember that the industrial revolution in the West took place at a growth rate of 3 percent. So, what is going to happen in the future?

From my perspective, the base case would be a 7 percent growth rate and a 1.5 percent population rate, which would be 5.5 percent. And one could be a few points off here, but a 5.5 percent per capita income growth rate for the next three decades is what I would project. This kind of growth is what the Tigers grew at basically. And this kind of growth -- and I could be off a little bit here; obviously, if you do reforms faster, it

secures this number much more -- your growth could go up to 8 also. If you have bad reforms, you could go down a few percentage points.

I call it a base case, because really, no matter who is in power, their ability to do harm to the growth rate is somewhat limited -- much less than what it was before. So that's why I called it "India Unbound." There has been a liberation from politicians themselves to do this.

Now, I said two and a half reasons. Very quickly, let me give you the second reason why I think we have this good future. And this future, by the way, it is not India alone, as I said. If India can conquer poverty, I think the whole world can. The second reason has to do with the world's change from an economy that was basically a manufacturing/industrial economy to a knowledge economy. And for some reason Indians are performing well in this services/knowledge economy.

And I explain this reason in my book. I speculate, of course. And this has partly I think to do with our Brahminical heritage. And it is the same Brahminical heritage which came in the way of succeeding in the industrial economy. It came in the way because the Brahmins have contempt for manual labor and they have reverence for knowledge. So that contempt for manual labor, you need tinkerers to create industrial revolutions. And tinkerers need to combine working with hands with knowledge.

And we prevented the people who work with hands from getting knowledge. So what you have, those are the Sudras and the Brahmins. And the Banyas, who are the people who run businesses, they basically are also upper caste. And they have the same values of the Brahmins. They have the same contempt for manual labor.

Anyway, my time is running out, so I am not going to be able to fully explain this. But what I want to say, though, is that what was a negative has become a positive. In other words, the Brahminical heritage, which was a negative from the point of view of the values that it brought to the industrial age now brings a positive value. In other words, that reverence for knowledge is what is helping the country. And in a sense, we have 3,000 years of experience with abstract thought, from the Upanishads downward. And just as spiritual space is invisible, so is cyberspace. So maybe our core competence as a nation is invisible.

That was one key thought that I wanted to leave behind, that maybe it is something. Otherwise how do you explain this? It is hard to explain this software boom that has been happening over the last 10 years. And we were talking about that even in this worldwide recession, Indian software exports are up.

The final reason really has to do with I believe India is on the verge of a second green revolution. And like the first

green revolution, this is also technology based. And it will be based on the miracle seeds. And the bureaucrats have been trying to kill this revolution for the last 10 years by not approving the new seeds. For the first time, I think, BT cotton was approved a few weeks ago in India. But a green revolution will require a lot of other things. You have to change the agricultural economy from basically a peasant economy. No peasant economy created green revolutions. What creates green revolutions are agribusinesses.

I think that in the last two budgets, the best news in the budgets was the opening up of agriculture. So, to come back to these protests in Washington that you have seen, in a sense, the WTO is our best friend in this regard. The WTO will slowly open up the agricultural markets. India has plenty of sunshine, plenty of water, plenty of arable land. We have twice the arable land of China and one-third the productivity. So you can see how far one can go. So, in a sense, if China is going to clothe us, we can feed China and provide China with software.

These are really the few thoughts that I have. Let me just close with an anecdote. The book is an anecdotal book. It is not a work of analysis by an economist. I left P&G at the age of 50. I took early retirement and went back to India. There was a friend of Swami's, named Niman, who was editor of Business World and Business Standard, two respected business newspapers

and journals. He said, why don't you go around the country and tell us what has happened to the country after the economic reforms.

And the first trip that I took in that journey was from Madras to Pondicherry. And we stopped in the morning at a roadside cafe. And it was just a village cafe, nothing fancy. It was under the trees. And this boy, Raju, was serving us coffee, good, South Indian coffee. And Raju, who was hustling between the tables, told us, first, that this was his summer job. Now, the idea of a summer job having arrived in a village in Tamil Nadu got my attention. The second thing Raju said was that he was earning 450 rupees a month. That's about \$15 a month. And he said that this was just enough for him to bicycle to the neighboring village in the evening, when he finished his work, to take computer classes.

So that 450 rupees paid for his computer education, which was done by a private company, called Aptech. And Raju said that his ambition in life was to run a computer company one day. And we asked Raju, where did you get this idea? He said, I saw it on TV. This man, his name is Billgay. He thought it was one word, "Billgay," he called him. He said, this man, that's my hero. He said, I'm going to be one day Billgay.

And then I knew at that point that India was changing and that what was changed more than anything else in the last 10

years was not just the reforms that had taken place but the young people's minds. And I came across dozens of stories, many of which I tell in the book, of young people who are like Raju. And the biggest change in India is I think amongst the young especially, but amongst a lot of people, where their minds, their dispositions, are different.

Thank you.

(Applause.)

MR. VASQUEZ: Thanks very much, Gurcharan.

Our next speakers is Swami Aiyar. He is the Consulting Editor of the Economic Times, based in India. He also writes a weekly column that is known as "Swaminomics" in the Times of India. He was educated at Stephens College, in Delhi, and Magdalen College at Oxford. He was also, for about two decades, the India correspondent of the Economist magazine. He has also worked at the World Bank, as Assistant Editor of the World Bank Research Observer, and has been a consultant to the World Bank and to the Asian Development Bank for many years.

Please help me welcome Swami.

(Applause.)

SWAMINATHAN AIYER,
ECONOMIC TIMES (INDIA)

MR. AIYAR: Gurcharan's book is called "India Unbound." I wished it was actually true. I would say India is half gagged and half bound. It is better than being fully gagged and fully bound. Some of the bandages and some of the gages have been taken off. It still remains very substantially bound.

I will give you one example. The Confederation of India Industry at the World Bank recently did a piece of research on what are India's problems vis-à-vis China and some other countries. And in one survey of businessmen the question was: How much of your administrative time is spent with various government functionaries and inspectors?

In the case of Latin America, it was 4 percent. In the case of most developing countries, it was 5 to 8 percent. In India's case, it was still 16 percent. One-sixth of your entire time was taken up with various officials of one kind or the other.

I will give you another gem, another piece of CII research. We said we were going to throw open the power sector to private investment. We are going to liberalize it and foreigners can come in. Enron came in. It became a fiasco. Because of the special nature of Enron, everything got diverted

to something else. But what the CII survey showed was that if you want to set up a power project in India, you still require a total of 97 different clearances from different authorities, most of them sequential, most of them requiring a bribe along the way.

It adds further that India's real problem is that while, according to Transparency International, we are the ninth most corrupt country in the world, unfortunately there are too many honest guys in the middle. So when I've paid my first 47 bribes, the 48th guy refuses to come on the take, and everything gets held up.

(Laughter.)

MR. AIYAR: There is this complete uncertainty and high risk even in the question of trying to get through this thicket of bureaucracy by bribing. So, as I said, India has this problem that, as someone once said, there are 100 guys with their foot on the brake and none with their foot on the accelerator. That is a very major problem for development.

So much of this continues. I asked a friend of mine who had gone from the government and the World Bank to the private sector, okay, with all this liberalization, all this ending of a whole lot of red tape that earlier was mandatory, what about kickbacks that you have to give to politicians to get a project through? He shook his head. He said for every project we still keep aside 10 percent for payoffs. So you can

understand straightaway, if you are going to be internationally competitive and your project costs 10 percent higher than anybody else's, that is a very major problem just on the capital costs, apart from delay and everything else.

Gurcharan said that there is a middleclass boom, a housing boom. Some of this is true. The liberalization of the financial sector certainly has helped in this respect. In fact, I believe that consumer finance this year is going to overtake industrial and commercial finance, which will really be very revolutionary in various ways. But the fact remains that one reason why all the banks, instead of lending to industrialists, are very anxious to lend to Gurcharan and me and the rest of the middleclass.

You see, in India, because of the law's delay, because any case goes on forever and forever, there are liquidation cases of which many, 60 percent, are more than 10 years. In effect, there are no lender's rights. When I have given you a loan, you have given me your particular factory as collateral, but the legal process just does not allow me to repossess it. Therefore, any money that I give you is in a sense a favor to you. And any repayment of a loan is a favor to me.

(Laughter.)

MR. AIYAR: The process certainly does not enable us to carry on. So this is not yet a market. So we desperately need a

judicial system that works, a police system that works. Instead, we get a case where one of the most celebrated accused in the Bombay scam of 1992, Harshad Mehta, he died of old age before the case could be brought to a conclusion.

We had a Prime Minister, our liberalizing Prime Minister, Mr. Narasimha Rao, who was accused in a particular corruption case by Lakhubhai Pathak. Mr. Lakhubhai Pathak died of old age; the case is still going on. Mr. Narasimha Rao expects to die before that particular case is finalized.

So if you have this kind of complete logjam, how do you have accountability? The liberalization of markets has brought about a great increase in the accountability of the businessman. If he no longer delivers, the consumer can go away from him to somewhere else. But at the end of it all, accountability has also to be dealt with by the state. If that cannot be delivered, we will continue to be in trouble. Therefore, apart from economic reform, we really do have a huge, pressing need for administrative, judicial and police reform.

What has driven this entire process? Why is it that India has liberalized? People have this habit of saying, well, there used to be a political consensus on socialism and it has moved to a political consensus on liberalization. Again, I think that is imperfectly put. There is now a political consensus on half-baked liberalization. There is more of a consensus on

keeping it half-baked than on liberalizing. This needs to be fully understood. And in the process, what brought it about? Was there any Ian Vasquez out there? Was there any Milton Friedman? Any Ronald Reagan? None. It was not driven ideologically at all.

What really happened was that for 40 years politicians were spending more and more and more and more, as politicians will. And they spent more and more money on capturing the commanding heights of the economy in every possible way that the public sector could. And equally they spent it on subsidizing everything in sight that they possibly could. And the fun and games went on for 40 years. But by the end of the 1980's, you come to this huge fiscal crunch. There just was not enough money both for subsidies and the commanding heights. And then the question was: What do we do now?

And across the political spectrum, having nothing to do with right or left, the politicians decided that subsidies we have to stick to. As a result of which subsidies as a percentage of GDP continued to be 15 percent, just as high as before the reform period. But this is the whole point -- with the fiscal crunch, if you said, I am going to focus all my limited government funds on subsidies, somebody else then has to do the investment. The government cannot do it anymore. That is how, in this completely non-economist, non-ideological manner, we

moved reluctantly, rather than in triumph, towards the market. And that particular fiscal stimulus continues to be there.

The overhang of debt is such that this is what is gradually forcing the government to say, look, we cannot do it, we cannot do it, we have to allow others to come in. Something else has to be done. So it has moved forward.

So if at all there is now a new consensus in this new "India: Half-Bound," it is, one, the political consensus is, well, we would love to do it all, but we cannot do it all, so we have to encourage private and foreign investment. Number two, to the extent possible, we should still not close a single undertaking or sack a single guy. And that remains an extremely strong part. And you will find, therefore, that whether it is closing down a factory and the lender repossessing or hiring labor retrenchment, there is a huge resistance to it.

Point number three, continue to subsidize everything in sight and, if possible, discover some new things to subsidize. That remains part of the going political consensus. Number four, since liberalization has taken away many of our traditional sources of corruption, we really must invent a few new ones. This is one of the few things that may keep privatization going, incidentally, if it may be associated with certain kickbacks which make it more politically acceptable.

So we are in this particular position where we have a potential of growing at 10 to 12 percent a year, yet we are only growing at 5 to 6 percent a year. With this half-baked liberalization, I don't really see us growing forward very much faster than this. The positive part is that this opening up has made a huge difference. It has gotten to the point where it cannot be reversed, because it has been too successful to easily get rid of.

Secondly, what Gurcharan referred to, suddenly, out of the blue, in one sector we have become globally competitive. This is the software sector. I am afraid I am too cynical and too multicultural to accept that Hindus have something to do with it, that we are great spiritual guys. I think all human beings are much the same and it makes absolutely no difference where you came from.

If you ask, why did India suddenly become so successful in the case of computer software, I have two very simple explanations. It is due to the two things which we tend to condemn. One was British Colonialism and the other is the brain drain. Thanks to British Colonialism we got the British language and the ability to go to these various places. And the huge advantage that we have over China is that English is the language of the global software community. India speaks it and China does not. So that has been an absolutely tremendous advantage.

The second, as I said, is the brain drain. From the 1950's onward, vast numbers of Indians were going abroad. We have not only an Indian diaspora of 20 million but a high-tech diaspora of 1 million. And this high-tech Indian diaspora of 1 million has a higher GNP than the 1 billion people of India produces. The reverse effect of that particular brain drain is basically what has driven our software sector. So we are lucky. We are finally making use of this particular thing. It is helping drive the process forward.

But at the same time I say we cannot depend on just these outside influences. We desperately need our own administrative, judicial and police reform.

Thank you.

(Applause.)

MR. VASQUEZ: Thanks very much, Swami.

We have time for questions now. If you have a question, please raise your hand. Wait for the microphone, and identify yourself and your association.

Right here.

MR. DUNNE: Robert Dunne, from George Washington University's Economics Department.

I go to India every few years, and I was struck by the beginning of changes in the seventies in attitudes. And I thought it was driven by the example of South Korea, Hong Kong,

Singapore and Taiwan. But what really changed things I thought in the eighties was the People's Republic of China taking off, and both an envy of that and a fear of it, and the feeling in India that we can't let those people get much ahead of us, we better figure out what they're doing.

Now, the one thing I fear is that this communal violence could throw the whole thing off track. Can somebody suggest to the folks in the two religious communities, you have all this success going for you, the one thing that will absolutely wreck it is religious wars? And what can be done to stop this?

MR. DAS: Actually, Swami had a column on Sunday in the Times of India, where he gave a very good answer to you. He said that, of a billion people, 99.999 percent are extremely religious people. So every few years you will have a religious outbreak. And the amazing thing was why, for the last 10 years, we had had none. And basically what Swami is saying is it is not going to be a major factor.

As to your other question about looking at what drove India, I wish that you were right. I wish that we would look at China more often. I wrote a column myself a few weeks ago in the same paper, the Times of India, where I said to ignore Pakistan, heed China. And this was my advice to Indians. A friend of mine had visited India. He had been a CEO of an American company and

lived in India for two weeks. And he noticed that for every seven references to Pakistan, there was only one reference to China over these two weeks in Indian newspapers.

The point is I think we do not look enough at China, and we look too much at Pakistan. And Pakistan tends to drag us down into fundamentalism and religious wars. And looking at China would actually show the single-minded purpose towards the economy and prosperity.

MR. AIYAR: I wish we had taken notice of Korea when it started. I regret I said that what applies to a small country cannot possibly apply to us. And, secondly, look at those guys, they are all going to become neo-Colonial puppets. You have no idea how in India the intelligentsia positively chortled as to how India was going to do very well and these stupid guys like Hong Kong, Singapore and Korea were going to go down the drain. This chortling continued long after it had been shown that the Colonial puppets were becoming 30 times richer than India. And we took a very long time.

I think what is correct to say is that when we had our own fiscal breakdown and total bankruptcy it coincided with the collapse of the Soviet Union. That was far more powerful than the Chinese thing. The collapse of the Soviet Union showed that whatever the answer to your problems till then -- you remember what Ian read out -- they said the only problem with the planning

is it was not sufficiently detailed. If only we had even more detailed planning, we will solve it. That became impossible after the collapse of the Soviet Union. Then China showed that there is another way to go.

So I think that many of these things helped. At the end of it all, what has kept it going actually is that it succeeded. And the fact that it began to work in India -- ultimately, all systems work on inertia. It's keeping going. But, regrettably, it's that half-baked thing that is keeping it going. The half-baked stuff is very much there. At the end of it all, believe me, we are not following China, we are not following Korea; we are following India, as we always do.

MR. VASQUEZ: Yes, right here.

MS. FINSTON: Good afternoon. My name is Susan Finston, and I'm here from PhRMA, the Pharmaceutical Research and Manufacturers of America.

In terms of brain drain and Indian talent, 15 percent of the laboratory research scientists in our labs in Europe and the U.S. actually were trained in India. So I think there are some similarities to information technology, except that of course you cannot get a patent for a medicine in India. And when you look at the green revolution, seeds also need patents. They are a little bit better in the UPOV area, the plant variety area, but not tremendously, not sufficiently.

I was wondering if either could comment on the prospects for getting some kind of statement from the government on sun-setting the exclusions for patents on medicines that would enable greater investment and greater growth in India for the benefit of both India's pharmaceutical sector and the companies that I represent.

MR. DAS: The WTO is going to ensure that. 2005 is the sunset. You have to do it if you want to remain a member of the WTO. Indian companies now have been preparing for 2005, and the regime is going to be dramatically different. One of the things that has happened through this period of piracy is that Indian scientists learned to reverse engineer, and those same skills can be used for the right engineering also. Therefore, the Indian pharmaceutical industry is actually going to play a part.

There are not going to be suddenly great discoveries, but already what you are seeing is that Indian pharmaceutical companies are providing new dosage forms to multinational companies and earning good royalties as a result of those discoveries. Two particular companies are Dr. Reddy's Laboratories and Ranbaxy.

MR. VASQUEZ: A question here.

MR. DILLON: Ken Dillon, Spectrum Bioscience.

You have mentioned China as a model, but China has its own pathologies. And I'm wondering about two of them in

particular. Their very rapid growth has come at a terrific environmental cost. And the second thing is a great deal of social disruption -- unemployment and so on. I'm wondering, is it perhaps actually more healthy for India to grow at a certain circumscribed level -- perhaps 6 percent, whatever it is -- and therefore be able to control these pathologies in its own development?

MR. DAS: Can I read you a paragraph from the introduction of my book which, in a sense, answers your question.

India embraced democracy first and capitalism afterwards. And this has made all the difference. India became a full-fledged democracy in 1950, with universal suffrage and extensive human rights. But it was not until 1991 that it opened up to the free play of market forces. This curious historical inversion --

-- and it's historic because every other country has done it the other way except one, and that is the United States, which got democracy also before capitalism, in 1776, and the early 19th century, when the industrial revolution came with capitalism --

This curious historical inversion means that India's future will not be a creation of unbridled capitalism, but will evolve through a daily dialogue between the conservative forces of caste, religion, and the village, the leftists and the Nehruvian socialist forces which have dominated the intellectual life of the country for so long, and the new forces of global capitalism. These million negotiations of democracy, the plurality of interests, the contentious nature of the people, the lack of discipline and teamwork imply that the pace of economic reforms will be slow and incremental.

The economists have been trying with some frustration to paint stripes on India since 1991. It does not realize that India will never be a Tiger. It's an elephant that has begun to lumber and move ahead. It will never have speed, but it will always have stamina. A Buddhist text says the elephant is the wisest of all animals, the only one who remembers his former lives, and he remains motionless for long periods of time, meditating thereon. This inversion between capitalism and democracy suggests that India might have a more stable, peaceful and negotiated transition into the future than, say, China. It will also avoid some of the harmful side effects of an unprepared capitalist society,

such as Russia. Although slower, India is more likely to preserve its way of life and its civilization of diversity, tolerance and spirituality against the onslaught of the global culture. If it does, then it is perhaps a wise elephant.

It's called "The Wise Elephant," this chapter.

MR. VASQUEZ: Any thoughts on that?

MR. AIYAR: I will simply say the biggest pathology of all is poverty. If you are going to tell me that you solve the problem of poverty and get the pollution, I will say I would love to have that problem in terms of priority and being very clear on what I would like.

MR. VASQUEZ: Right here.

QUESTION: A very quick proposition to both of you on India's software success. You talked about reverse engineering. We are very good at it. Anybody who knows the Indian market knows that when you buy a product you are never sure it will work. We are not people who are for perfection. We are fairly good at improvising and getting along. Can you imagine a German or a Japanese making software? He will look for perfection. He will not release the software until the last glitch is solved. Would Indians do it? No. We will work along as it is.

And I think along with the brain drain, along with the English language, along with mathematics, along with abstraction and the ability to think outside the box, the fact that we are very prepared never to wait for perfection, to just get along, I think that would explain a lot of the reasons why we have done well.

MR. DAS: I'm sorry, what you are missing is that when you said various things in India were badly made, they were badly made in a period of protectionism, of preventing anything good coming in. The shoddiness was not inherent; the shoddiness was induced by bad policies. When exactly those same Indians landed up at Harvard or MIT or Silicon Valley, they produced absolutely first-class, world-class stuff. So the problem is not with the Indians. The problem is with the environment. I think that is proved quite conclusively.

MR. VASQUEZ: Yes, right here.

QUESTION: I am a small entrepreneur. In fact, my company is based offshore in a small village in Tamil Nadu. We produce a bunch of remote services for the U.S. market.

My question is more about one of the conventional pieces of wisdom in India, especially when we get a corrupt politician coming in, is the cry goes up all across the editorial pages of: What we need is visionary leadership. When are we

going to have honest politicians? And business leaders repeat this mantra and so do the editors and journalists.

And one of the issues I have with that is that it does not recognize I think the bigger problem in India, which is not the fact that our politicians are scoundrels. To me, I think any politician anywhere are; it's not that it is inherent in India, that our politicians are more venal than others. I think politicians anywhere, if they got a chance, would be scoundrels. I think the problem lies in the institutional setup. What incentives and checks do we have?

Because what happens is either that we are attracting the wrong people to be politicians or there is some sort of unfortunate filtering that prevents the honest people from rising up, and it brings all the crooks to the surface. And until we correct that -- I think this is piggy-backing on what Swami said about the judicial and administrative reform, and I think this is probably one of the bigger issues that I see with India today.

MR. DAS: I think you are right. Swami also pointed out that our soft underbelly today is governance. The only thing I wanted to say -- and you can't disagree with that -- but the point here is that with this wretched governance that we have, we have grown at 6 percent compounded in real terms for the last 20 years. Just think, the upside, and with a little improvement, a little administrative reform, where this all could go.

Democracy is run and should be run by modest men. And India's politicians are certainly modest.

(Laughter.)

MR. DAS: What I am saying is that, to me, with all this, there is something going on. I mean, it is quite unprecedented for a country of a billion people, for 20 years, to have grown at 6 percent. And certainly in the nineties we have seen literacy rates that have climbed up rapidly. Literacy has gone from 52 to 65 percent, which means a doubling of the rate of literacy growth.

So there are things happening which are not related to governance. And in some sense what is happening much more is the freeing of the Rajus from the process, the drag on the system, the political system. And that is also somewhat ironic, because we have had 50 years of experience with democracy and institutions, and we have had only 10 years experience with the institutions of capitalism -- and that, too, half-baked capitalism, as Swami pointed out. So it seems that those 10 years, they are working to give you these results.

MR. AIYAR: I think you are dead right. What is wrong with the institutional incentive structure? Gurcharan says some things have been improving; correct. But on the political side, we had this election commissioner who determined that 40 members of Parliament and 700 members of state legislatures had long

criminal records. This was not the case in the earlier days. Something is happening. The incentive structure is attracting more and more criminals into politics. It's very simple. Once you become an elected member of the legislature, the prosecution against you appears to either cease or slow down to almost zero speed.

I have one institutional change -- seniority in all cases, all criminal cases, to elected people. I think the moment you said that seniority will be given to such cases, every single elected criminal will promptly resign and get the hell out of there.

(Laughter.)

MR. AIYAR: This is the kind of institutional change we need. We badly need it.

MR. VASQUEZ: Over here.

MR. WOLFE: My name is Gabriel Wolfe. I was in India three years ago, and I met Rakesh Mohan, another graduate from the World Bank. He said everybody knows what is wrong in India; the problem is, what do we do to get from where we are to where we want to get to?

And it does seem to me, in contradiction to what Dr. Das says, the important thing is not that there has been growth at 6 percent per year, but how is it that so many intelligent people can be so poor for so long?

My question to both speakers is: What one action would you suggest government could do to hasten the progress to get from where India is to where Indians want it to get to?

MR. AIYAR: I have one very clear suggestion: Immediately disassociate the entire criminal investigation machinery that we have in India from the politicians. At which particular point in time the entire structure, instead of saying the police are to be used to support the patronage network of the politicians, it becomes we will actually get the criminals.

I have a very strong feeling, the moment you have this one single thing, the amount of accountability in the system will improve tremendously. We are already getting better accountability through marketization. If you also get better accountability through the enforcement mechanism, in my view, those two together, in terms of any one single thing, will produce the greatest result.

MR. DAS: I think it's a similar sort of prescription. I would say it has something to do with governance and administrative reform. There are many areas of administrative reform, and I think if we can just get one of those done, whether it is related to the bureaucracy or the politicians, you would certainly have huge benefits to performance there.

I personally also feel that in education, while the higher education system has delivered these people to Silicon

Valley and so on, primary education, universalizing that very quickly, will have a huge multiplier effect in the country. And that certainly has not been pursued or been on the agenda. In other words, both qualitatively and quantitatively education reforms.

MR. VASQUEZ: Yes, right here.

MR. MALLACK: I'm Roe Mallack, from Congressman Bernie Sanders' office.

My question is for both Mr. Das and Mr. Aiyar. It concerns factors contributing to economic growth. A recent BusinessWeek article states that closing the education gap between the highly literate and the illiterate in developing countries is more instrumental to economic growth than are closing income disparities within those countries. To what extent do you agree with this statement? And what role do you think the private sector and free market reforms can play in closing the education gap within India?

MR. AIYAR: Well, the two are highly correlated. Income and education are highly correlated. If you close one gap, you will close the other. It doesn't really happen any other way.

As to why it is not happening -- India had this tremendous failure, tremendous failure, in primary education. And there is this huge Indian Institutes of Technology, because

Nehru wanted to catch up and show the white man I'm as good as you. So at the higher education level we actually did some very good things, but we neglected that huge thing at the bottom. And we are getting a delayed payback on that higher education thing through the software boom which is coming back because of the Indian Institutes of Technology which Nehru set up. Those have been the general, so to speak. The troops have been provided in some cases by the private institutions, but the generals came out of that public sector system of excellence that Nehru set up.

At this particular point in time, as Gurcharan said, one of the key things is raising education -- and not just raising education but raising skills in general. For this the state is the only one that can actually help the poorest to get it. Private education, the marketization of education, is coming up in a big way. More and more institutes are filling the gap, particularly in technical education. And so you are getting a marketization, which is providing a better degree of education than was the case earlier. But the poor are getting left out in the process, because they would need something free or very close to free to take advantage of this. So you cannot get away from that urgent need.

MR. DAS: Not to take away from what Swami said, but Ian and Swami and I were in Goa a few months ago and there was an unusual Englishman there, named James Tooley, from the University

of Newcastle, who specializes in studying private education at the primary school level around the world. And he was talking about a revolution that has been taking place in India and in some other countries, where for \$1 a month a child can receive education, and it is private education. And those people who provide this education actually make a profit. Whereas the government spends something like 3,000 rupees on the same child -- which would be \$75 per year. So \$75 per year versus \$12 per year is what these people charge.

I talked about an education revolution, in a sense, going on, which is no thanks to the state. And the state will have to play a very big role. But it is very interesting to see these initiatives, these private initiatives in something like education, which no one believes. I mean, to make a profit when you charge \$1 a month, that is fantastic. And I think these are the kinds of things that we need to bring out, applaud, and also for the Indian state not to put hurdles in the way of these schools -- which it does very often.

MR. VASQUEZ: Yes, in the back.

MR. KOBER: Stanley Kober, with the Cato Institute.

I would like to push this issue of democracy and governance further, in light of the first question with regard to the violence in Gujarat. Because the problem there is not simply the intensity of the religious hatred that has been demonstrated

but also the evidence of government complicity by the government in Gujarat, that the government has been complicit and even encouraged it, that the police have not only stood aside but participated in some of the atrocities, and the question then of whether the government in New Delhi, the central government, will take action to investigate if it is demonstrated here. There does not seem to be any indication of that, and that is a real concern.

The Times of India itself recently editorialized that this is the biggest crisis for Indian democracy since Partition. I think that needs to be addressed in light of that.

MR. AIYAR: If you have an administration and the police that cannot deliver decent roads, that cannot deliver decent electricity, decent water, decent food, the idea that you can give decent law and order or a decent police situation is highly unrealistic. There is a highly inefficient and moribund state apparatus which needs to be cleaned up.

In a country like India, with this huge history of multicultural tensions and conflicts, religion versus religion, caste versus caste, region versus region, there are a huge number of national tensions that always happen. It is an extremely difficult experiment to try to run a multicultural society of this particular nature, in a democratic nature. There are constant eruptions of various kinds. We require a very high

quality of police, administration and polity if we really want to control that. We don't have it.

But the idea that you can just fix it by replacing one politician by another I don't think is the case either. In this particular case of Gujarat, there is not only the problem of the sectarian tensions that have always been there, there is the growing feeling that the government is too moribund and useless to bring anybody to book.

MR. DAS: The interesting thing about Gujarat is also that it has been, in the last 10 years, the fastest growing province of India, where the growth rate has been 9.8 percent compounded over an eight-year period. And I wonder if there is a connection of some kind.

MR. VASQUEZ: Yes, Dan.

MR. GRISWOLD: Dan Griswold, with the Center for Trade Policy Studies here at the Cato Institute.

Coming back to the comparison with China, it is hard to go to Wal-Mart or some other place without buying something made in China, from clothing to toys, but I virtually never see anything made in India. And I wonder, can India achieve this large middleclass through just services -- software, these call centers, this sort of thing -- or does India need to create some kind of globally competitive industrial base? And if so, what

might that be? In other words, what sectors of the economy besides these services is China going to make its presence felt?

MR. AIYAR: This has been dealt with quite extensively in that particular piece of research I mentioned earlier, between the Confederation of Indian Industry and the World Bank. It is very clear that Indian business has a huge disadvantage vis-à-vis China and access to capital, where we pay 12-13 percent, whereas a Chinese businessman would pay 3 to 4 or maybe 5 percent. There is a problem in the hassle factor, where 16 percent of the businessman's time of various kinds is tied up, and in China it is less than half of that. The cost of land, the cost of electricity, is half in China. The labor regulations, the effective productivity of labor, is much higher in China.

We would have to tackle each and every one of these issues one by one. Tackling only one of them by itself is not going to do it. I have a sad suspicion that we are not going to be able to solve these problems very fast. More likely, China's success will raise China's own wage rates so high that it will once again create some kind of space for us to grow into. So it will be the Chinese success that enables us to rise more than our ability to rise above our own problems.

MR. DAS: At the same time, I talked about the two areas -- one is the area of services. And certainly in the services area, what it will do is it will remove educated

unemployment completely. In other words, today, we graduate about 2.5 million people every year. And anyone with even a modicum of English can go into a little call center school for three months, or six weeks, and can get the right sort of accent to answer the phone, whether your customer is an American Express cardholder or Delta Airlines or whatever. So, even today, what we are seeing is that what is disappearing is what happened for the last 50 years, which was educated unemployment.

The second thing, I think if we can get the agricultural reforms underway, certainly we have a natural competitive advantage in agriculture. And that is certainly one to harvest. Finally, even in the industrial sector, which is where I think you were asking, in the industrial sector there are certainly companies who are globally competitive, like Tata Iron and Steel, Hindalco, which is an aluminum company, and some of the cement companies are extremely competitive. So there will be some sectors where you already have competitiveness.

But I think, overall, I would agree with Swami that that is not where the action is. The Indian action is not going to be there. I happen to believe, though, between agriculture -- even if we went from a green revolution to a knowledge revolution and skipped the industrial revolution -- we would not be too badly off, because the value added today in the world economy is in the knowledge services. Therefore, with export of a little

bit of software, you can import a lot of steel. And that's the sort of idea, that industrial products are becoming commodities. Therefore, when people ask me, you're doing well in software, but what about hardware, I have to tell them that hardware is a commodity and software is not. Therefore, I would rather be playing the software game than the hardware game.

MR. VASQUEZ: We have time for one more question before we break. Right here.

QUESTION: I am a product of those Institutes of Technology and the Institute of Management from India. Today my thinking is more in line with Gurcharan Das'. It is not as cynical as Swami's, who I thought had a little more cynicism. Because of these Institutes of Technology, this reverse brain drain has become possible. In 1994, Lee Kuan Yew was interviewed by Fareed Zakaria for Foreign Affairs Journal. And he said that Singapore had a model to go on. They took the Japanese model and they moved towards it. The problem would come once they reach the level Japan has reached. He had stepped down as Prime Minister.

India does not have any model. The closest would be something like the United States of Europe. And the United States of Europe, Western Europe primarily, population-wise is still one-third. And languages and religions are not as many as exist in India. Everybody acknowledges that India is a

democratic country, but I feel you cannot ever overemphasize that. It has become a cliché now, but the government tries to be everything to everybody. And Gurcharan said that America is the only other country which embraced democracy before capitalism. The brand of democracy also was a bit different, because you had slavery for 100 years and another 100 years before civil rights were given to the various peoples.

MR. VASQUEZ: Could you ask your question?

QUESTION: That was a comment. Those were some of the thoughts I wanted to make.

MR. VASQUEZ: On that more optimistic note, you are now unbound. Before you leave and go upstairs for an informal lunch, please join me in thanking our guests today.

(Applause.)

(Whereupon, the Cato Institute Book Forum concluded.)