Eleven

Multiplying by Zero

Though those that are betrayed
Do feel the reason sharply, yet the traitor
Stands in worse case of woe.

—WILLIAM SHAKESPEARE

Lal Bahadur Shastri died suddenly of a heart attack on 11 January 1966, nineteen months after he became Prime Minister. He died in the fabled city of Tashkent after signing an agreement with Pakistan giving up significant territorial gains in the victorious autumn war, including the strategic Haji Pir Pass, gateway to the Kashmir valley. I was at my parents' home in Chandigarh when we heard the news, and like the rest of the country, we were in a state of shock. Shastri had begun to grow on us. Although we did not want him to part with the pass, we felt that he had displayed qualities of statesmanship. What endeared Shastri to us was a disarming absence of ego, and this had also made him an effective leader.

A great deal died with Shastri that day. Contrary to what most people think, Jawaharlal Nehru's death did not end an era. It was Shastri's death that did. Although he had been a cabinet minister for many years in the 1950s, he was poor when he died. All he owned at the end was an old car, which he had bought on installments from the government and for which he still owed money. He had set high standards. He was the only railway minister who resigned from office following a major train accident as he felt compelled to own moral responsibility. After Shastri's death, values departed from our political life and governance became amoral. A new personalized style of politics came into being. Institutions began to erode, the biggest victim being the Congress Party. More than values, Shastri's early death lost us the opportunity for pragmatic policies in our economic life. Had he lived, our nation would have done far better and more people would have risen out of poverty. Alas, he did not, and what might have happened must remain a counterfactual of history.

There was high drama in the Congress Party over Shastri's succession. Rumors flew and fortunes changed by the hour. The barrel-chested, taciturn president of the Congress Party, K. Kamaraj, turned out to be the kingmaker. He was a brilliant strategist but his strength lay in the absence of ambition—he did not want to be Prime Minister. We respect that in a man. Neither did he know Hindi or English—he spoke only Tamil—and he must have realized that this would be a terrible handicap. He had another quality unusual in a politician—he did not speak. He could spend hours listening without saying a word, and people thought him wise. Again, Morarji Desai was the leading candidate. We did not like Morarji because he was rigid, authoritarian, aloof, with countless silly fads. Neither did the powerful Congress bosses, known as the Syndicate. However, they had different reasons. They wanted someone pliable, whom they could control from the back room.

To stop Morarji, the Syndicate tried to draft Kamaraj. He stood firm. Morarji wanted to have a proper election among the Congress members of Parliament. The Syndicate was afraid that Morarji might actually win a contest and kept stalling a poll. In its defense, it kept saying that it wanted a unanimous candidate, and charged Kamaraj with determining who that would be. We may not have liked Morarji, but we liked the Syndicate's methods less. We supported Morarji's democratic right to an election. From these machinations Indira Gandhi's name emerged. The political bosses favored Jawaharlal Nehru's daughter because they thought a frail and inexperienced woman would turn to them for advice. We disliked her candidacy because it smelled of dynasty. In the end, after endless consultations, Kamaraj revealed his hand—he proposed Mrs. Gandhi's name as the "unanimous choice of the party." Since she had the aura of the Nehru name, he said, she offered the best chance of delivering victory to the party in the coming general election. However, Morarji remained firm on an MPs' poll. Kamaraj then swung into action and began to build pressure. He got the state chief ministers to come out publicly in her favor. This created a bandwagon effect. Finally, a secret ballot was held on 19 January in the domed Central Hall of Parliament among the Congress MPs and Indira Gandhi won 355 to 169.

Lal Bahadur Shastri had been full of common sense. He had come to feel that our elaborate system of controls had become heavy and self-perpetuating. For every control that failed, we needed two more to shore up the original one. In the complex, nonmonolithic government that India had become, controls were causing delays, waste, and enormous harm. He thought it was time to loosen up, and he entrusted the task to L. K. Jha, his principal secretary. The *Times of India* ran a story on the front page in early December 1965 saying that the government was contemplating liberalizing some of the less useful controls—this was the first time I came across the word "liberalization." Four days later, there appeared another story in the same paper. Unfortunately, a month later Shastri died, and with him died the prospects of liberalization. Mrs. Gandhi, who was ideological like her father, brought in her leftist advisers. She replaced L. K. Jha with P. N. Haksar. Mohan Kumaramanglam, the former communist, began to play a decisive role in policy making. They quickly buried the liberalization initiative. Many years later, L. K. Jha confirmed the veracity of the *Times* report—he said that there had been a serious attempt to deregulate the industrial economy under Shastri.

It had become clear that Nehru's economic path was delivering neither growth nor equity. Shastri had done some fire fighting, particularly in freeing agriculture, and he had tried to shift the tone towards the market. But he died before he could change course. We persisted on the wrong path in the 1970s and 1980s even when we knew that we were failing and the "mixed economy" was leading to a dead end. In fact, Indira Gandhi's government became even more rigid, introduced more controls, and became bureaucratic and authoritarian. It nationalized banks, discouraged foreign investment, and placed more hurdles before domestic enterprise. Some East Asian countries, in the meantime, began to make a decisive break with the past and adopted export-oriented policies that did not distort market prices.

Modern India's tragedy is not that we adopted the wrong economic model in the 1950s, but that we did not reverse direction after 1965. Industrial growth (not economic growth) plunged from 7.7 percent a year between 1951 and 1965 to 4 percent between 1966 and 1980. India withdrew further from world trade, raised tariffs and taxes even higher, and became one of the worst-performing developing countries in the 1970s. Rakesh Mohan, the head of the National Council of Applied Economic Research, has conservatively estimated the economic cost of Mrs. Gandhi's follies at 1.3 percent lower per capita GDP growth per year. Put another way, the per capita GDP would have been at least 80 percent higher in 1990—$550 instead of $300. With some modest liberalization in the eighties, industry did begin to grow, but experts agree that "1966–1980 is effectively the dark period for the Indian economy." Ironically, Mrs. Gandhi ruled in the name of the poor—"garibi hatao" ("End poverty") was her winning slogan during elections. But in the end, she suppressed economic growth and destroyed the chances for the poor.

Experts came up with different answers about what was going wrong and why growth was decelerating. Indira Gandhi's apologists argued that the terms of trade had changed in favor of agriculture after the green revolution. This is patently incorrect, for these terms did not change until the 1991 reforms. Others said that inequalities had grown and the market for mass-consumption products had shrunk. Hence, overall demand was the problem. This hypothesis, too, seems false, for the Gini coefficient, which measures income inequality, does not support it. A third explanation was the lack of capital. This too cannot be true, for the most dramatic change in the post-Independence economy has been the rise in savings rate and capital formation. India's savings rate rose from about 6 percent in 1950 to 14 percent in 1960, 18 percent in 1980, and to 23 percent of income by 1990. The investment rate also rose from 17 percent in 1960 to 23 percent of national income in the 1980s. This compares well with the advanced countries, although it may not be as high as that of the Asian tigers. Thus, shortage of capital was not the reason for our failure.

The blame lies squarely with the productivity of our investments, as well as their capital-intensive nature. Although we saved and invested, the returns were poor. Economist Isher Ahluwalia estimates that the productivity of Indian manufacturing declined half a percent a year between 1960 and 1985. Capital–output ratio deteriorated because we got poor returns from the inefficient, heavy-industry-based public sector. The private sector did not perform because we had emasculated it with massive controls. Ironically, we had created state-owned companies in part to raise our savings rate. We thought they would give good returns and this would augment the nation's savings. But they failed and ended up destroying our savings. The growth in savings actually came from private households.

Infrastructure was the other reason for our poor performance. Power, railways, coal, telephones became bottlenecks. Anyone who lived in India in the 1970s and 1980s felt the horrendous shortages. There were constant blackouts as power was unavailable. Railway freight suddenly started declining. There were shortages of coal, cement, steel. One seemed to feed on the other. For example, once railways started doing badly, then coal did not get taken from the coal mine to the thermal plant that made electricity from coal. If enough electricity was not generated, then coal could not be mined. If coal and electric power suffered, then the railways could not run. Why the bottlenecks developed was a subject of constant study but insufficient action. A combination of declining productivity and slowing investment was the problem. All infrastructure was state-controlled and not subject to market forces. Even cement was heavily controlled. This meant that politicians and bureaucrats set prices and decided when and where to build a new factory. A strong politician could get away with building a power plant in his area even when the shortage was in another area. Or he might build a railway line to please his rural voters when the more industrial areas needed it. He justified it in the name of equity and regional balance. Mismatches quickly came about, for the rules of demand and supply were not followed. Hopelessly low prices meant that the state power companies became bankrupt and did not have the funds to invest in new plants or expand existing ones.

Trade unions became powerful because politicians were unwilling to displease their large vote bank. Trade unions wanted to hire more workers, and existing workers to work less. This suited the politicians, for it meant that they could create jobs and please the voters. According to the law, no one could fire a worker for not working. As the work ethic declined, productivity plummeted. Managers of the state enterprise complained, but no one listened. Workers would loiter on the job and often not show up, and the managers could do nothing. Many power plants ran at half their efficiency. Linesmen of the power companies made private deals with small industrialists and stole a third of the power; they “fixed” the power meters so that their crime could not be detected. A mafia operated in the coal mining area of Bihar and became a law unto itself. Finances of the government rapidly deteriorated and there was no money for new investments. The result was shortages. The amazing thing is that the system did not completely break down.

Our company’s salesman in Bengal was a bit of a hero during the 1980s because his sales were consistently rising. One of the reasons, he said, was his excellent performance from Haldia, where a state fertilizer plant had been set up. Thousands of well-paid workers had lifted the demand for our products. A sparkling new township had come up with bungalows for managers and nice flats for workers. There were wide roads, bright lights, a school, a dispensary, and a hospital, even a subsidized store for the employees. The capital budget of the plant had paid for this middle-class dream. However, the factory never produced a kilo of fertilizer! And this went on for years. The cleaning crew kept the factory clean, the mechanics kept the machinery in good order, and the workshop supplied spare parts. The managers and workers came to work, and the personnel department marked attendance. Everyone was paid, including a bonus, and even overtime in some cases. However, they had no work because soon after the factory was built it was discovered that the company was unviable. If they had produced, they would have lost masses of money. It was cheaper not to produce. Yet they could not close down. Not only was it bad politics to close, the law did not permit it.

The plight of Haldia was extreme, but there were other examples. Another firm, Scooters India Ltd., in Lucknow, was still paying wages to three thousand workers in 1992, although it had not built a scooter for ten years. By the end of the eighties three-quarters of the state-owned companies were losing money. To pay for these losses the subsidy to state enterprises rose from 3 percent of their income in 1970–77 to 26 percent in 1980–81. It was 20 percent in 1988–89.

Prakash Tandon, who wrote the classic memoir *Punjabi Century,* relates a fascinating tale of public and private sectors. Each year he used to take his family on holiday to Kashmir by road from Bombay. One year, he noticed a petrol station had come up on the highway beyond Nasik. About the same time a large public-sector factory had also come up twenty kilometers beyond the petrol pump, complete with wide, tree-lined boulevards, spacious homes, schools, hospitals, and sports amenities.

The next year, Tandon noticed that the petrol pump was doing good business and a mechanic's workshop had come up alongside. The following year, he found that a roadside restaurant had also come up whose food was especially popular among truck drivers. A cigarette and paan vendor followed; then a fruit seller; next came a tailor and a general merchant. In less than a decade, a flourishing little town emerged. Meanwhile, the state company began to lose money, and in the same period its losses had grown colossal.

The contrast is instructive. In one case, wealth was created organically. A lonely petrol pump attracted entrepreneurs, and they offered services that people wanted. They reinvested their profits and they expanded. Their profits attracted others. In the end, society's wealth was generated from within and it supported a flourishing population of a thousand families. It had all started with a petrol pump! Twenty kilometers away, the state also created a town. However, with one difference—the state destroyed society's wealth.

During these unfortunate decades the number of people who depended on the state expanded enormously. Fully 70 percent of the employees in India's "organized sector" (that is, firms employing more than ten workers) received their paychecks from the government. If one excludes civil servants and the government bureaucracy, 55 percent of the Indian industrial workforce was on the rolls of public-sector companies in 1990. Yet the public sector's share of production was only 27 percent in 1990. By contrast, China's state-owned firms employed 40 percent of its industrial workers. The very rapid growth of private enterprise in the eighties following China's reforms means that India's economy is now more socialist than China's.

By 1990, India's planning process had created a large rentier class of state employees in the public enterprises and the bureaucracies of the central, state, and local governments. This class exercised great power. It mediated every significant decision. It directed society's resources—it decided what to produce, at what price; who would get subsidies, who would get credit; who would get licenses. This gave this new class enormous authority over ordinary citizens and the ability to extract "rents"—the economist's term for corruption and bribery. Since nothing happened without some sort of exchange, there also emerged a group of power brokers who cultivated the ruling class and utilized their contacts for personal gain.

After 1967, India withdrew further from world trade. Our products became shoddier and more expensive as we raised tariffs dramatically. Actual duties collected went up from 21.2 percent of total imports between 1960 and 1965 to 54.8 percent in 1985–90, while exports stagnated around 5 percent of GDP. We protected our industry with draconian controls that we administered in a ridiculous "case by case" manner. Ironically, these heavy-handed controls were created to conserve foreign exchange; yet we were in balance-of-payment difficulties in twenty-nine out of thirty-five years from 1956 onwards. Despite these enormous defects, industry did manage to grow at a little over 6 percent a year over the forty years from 1950 to 1990, and its share in the country's income doubled from 11.8 percent in 1951–52 to 24.6 percent of GDP by 1990–91. But it was not enough for the economy to take off. Although we saved and invested, the returns were poor. Our expenditure on the bureaucracy far outstripped the growth in the nation's income. Predictably, India's position declined in the world and among similarly placed countries. Based on John Page's broad comparative data for the Third World, Rakesh Mohan concluded that "India was amongst the worst performers among developing countries between 1950 and 1982."

I sometimes wonder how we could have gone so wrong when we had such brilliant economists. The Delhi School of Economics had acquired a formidable and well-deserved international reputation as a center of excellence. It had Jagdish Bhagwati doing seminal work on trade; A. L. Nagar was engaged in pathbreaking work in econometrics; Sukhamoy Chakravarty was one of the authorities on planning models and one of the first persons to employ Pontryagin's mathematical principles in economics; Tapan Raychaudhari and Dharma Kumar had formidable reputations in economic history; Amartya Sen and Prasanta Pattanaik were world-renowned in social choice theory—with Amartya Sen going on to win the Nobel Prize. However, Professor Jagdish Bhagwati was the only Indian economist of note who tried to rouse Indians to the danger of Nehruvian socialism. His book (with Padma Desai) *Indian Planning for Industrialisation* was the first comprehensive study of the variety of ailments caused by our left turns of the 1950s and 1960s. As the intellectual climate worsened, rather than bang against the wall of intellectual intolerance erected by Indira Gandhi, Bhagwati left to teach first at MIT and then at Columbia University in New York. Amartya Sen also went away to the London School of Economics, then to Oxford, and finally to Harvard.

Apart from fine theoreticians, there were some outstanding practitioners. One of them was I. G. Patel. After important roles in the finance ministry in the 1950s, he became the governor of the Reserve Bank in the Janata government of 1977, and later was head of the London School of Economics. I. G. Patel set high standards of behavior. At the Reserve Bank, he resisted loan and debt write-offs and did not allow the banking system to deteriorate. However, he became increasingly uncomfortable during Mrs. Gandhi's second regime. Just before the 1972 elections, L. N. Mishra, Mrs. Gandhi's minister, and his friends rang him up frequently asking for clearances, which he invariably refused. Later, in 1980, when IG was at the Reserve Bank, politicians lobbied to give a license to the notorious Bank of Credit and Commerce International (BCCI), the Middle Eastern bank which grew rapidly in the seventies and collapsed in the early nineties. IG suspected BCCI and refused it a license. However, the minister of state at the time called for the BCCI file, overrode IG and approved the license. When IG heard about it, he rushed to Delhi and asked to meet the Prime Minister. Because of that meeting, the license to BCCI was withheld. After Mrs. Gandhi returned to power, IG began to feel uncomfortable and he resigned. There were two other Oxbridge-educated economists—Manmohan Singh, who served in important roles in the 1970s and 1980s, succeeding IG as governor of the Reserve Bank, and Montek Singh Ahluwalia, who was in various economic ministries throughout the eighties. Manmohan and Montek later became famous for ushering in India's 1991–93 economic reforms. The troubling question is why these outstanding people did not blow the whistle. They kept serving a bankrupt system for years, providing it with intellectual respectability and support.

My leftist friends were euphoric that day in 1969 when Mrs. Gandhi nationalized India's fourteen largest banks. They had always been critical of our banking system. They regarded the banks as "monopoly capitalists," controlled by a handful of big business houses, who made loans only to their affiliated companies or to their cronies. Mrs. Gandhi's purpose in nationalizing the banks was to reorient credit flows to the neglected areas—agriculture, small-scale industries, and small borrowers. She wanted banks to open branches in small towns and villages and bring the average Indian into the banking system. All worthy goals, which she succeeded in achieving. In the next two decades bank branches rose from 8,262 in 1969 to 60,190 in 1991—half of them in rural areas—and the average population served by a bank declined from 65,000 in 1969 to 11,000 in 1991. Bank deposits soared from 13 percent of GDP in 1969 to 38 percent in 1991, and loans expanded from 10 percent to 25 percent of GDP in the same period.

That was the good news. The bad news was that the efficiency of the system sank. Productivity and profitability of banks plunged. By 1990, the banks' gross profits dropped to 1.1 percent of working funds (without counting their bad debts) and their establishment expenses rose to 2 percent of working funds. Bad debts—what is euphemistically called "nonperforming assets"—rose to 20 percent of the credit outstanding. Consequently, most of the public-sector banks are bankrupt, especially the rural banks. They have been "captured" by their employees, the unions, and politicians, and it takes my wife half an hour to make a deposit or withdraw money from our local branch.

I once chanced to meet the manager of one of the rural branches of a nationalized bank. It was on the night train between Delhi and Amritsar. We shared our dinner like friendly travelers, and before I settled down to read for an hour prior to going to bed, he told me a few things about running a rural branch. He was a sincere young man, deeply concerned, and he wanted to unburden himself about his day-to-day problems. Neither he nor his staff, he told me, decided who qualified for a loan. The local politicians invariably made this decision. The loan takers were invariably cronies of the political bosses and did not intend to repay the money. He was told that such and such a person was to be treated as a "deserving poor." Without exception, they were rich. When the loan turned bad, the political bosses disowned any knowledge of the loan or the recipient. Therefore, at the time of the default it was the bank manager's head on the chopping block. Periodically he received instructions from headquarters to roll over the loan when it was against the rules to do so. These too were delivered orally. He dared not ask for written orders, because the only order in writing would be his transfer to an even remoter location. In contrast, when he or his office gave loans to genuine small farmers and traders, they invariably paid them off. There might be delays, but he always knew the reasons, and he was certain that the money would come back as soon as the crop was harvested.

Even more frustrating was the behavior of his staff. He did not run the office. The trade union representative decided who did what, who was to be promoted, and who transferred. He tried to promote a female clerk who was doing exceptionally well. But he was vetoed by the union leader. "Of what use am I?" he asked me sadly. I deeply empathized with his situation. I went to bed thinking what I might have done in his place. However, I could not find an easy answer. At least in my company I did not have to put up with this nonsense. The next morning, as we were getting off at Amritsar, I suggested to him that he find another job.

Because of nationalization, genuine entrepreneurs have had a harrowing time getting loans. Amrik Singh, whom I met in Bombay, was fed up with the routine of his job and decided to become a hog farmer. An enthusiastic electronics engineer, he had looked at a number of alternatives, but the rural life appealed to him. His friends tried to discourage him. However, he felt that "fourteen years in electronics is a lifetime." Being a serious person, he vigorously began studying pigs and soon became quite knowledgeable. He acquired property in a village 105 kilometers away and gave it a nice name, Arcadia Breeders. Having got the land, the next step was to find capital. For that he approached the nationalized bank in his village for a loan. The bank manager refused. Amrik Singh then asked him for a "no-objection certificate" (NOC), which would qualify him to approach another bank. The bank manager would not issue him an NOC either. After numerous visits, he at last got the manager to relent. "Submit a report," he said. "I will reject it and issue you an NOC." Amrik Singh protested, "But if you reject it, no other financial institution will touch it." Many follow-ups and seven months later, Amrik Singh finally succeeded in getting his prized NOC from the bank manager. He had learned his first lesson: had he bribed the bank manager, he would have received the loan.

After getting the NOC, he applied to another nationalized bank for a loan. This took eleven months, and only because of a chance meeting with a classmate at the rural refinance bank, which pushed his case. Meanwhile, his costs shot up and he worried if his project was still viable. Finally, he shifted to the village and began constructing sheds for the animals. A month later, the tehsildar, or village head, came by and ordered him to stop construction because he could not build on agricultural land. Amrik Singh argued that hog production was an agricultural activity like poultry, and sheds were permitted for the animals. The tehsildar refused to listen. He approached the deputy director of animal husbandry and requested him to clarify in writing that hog farming was an agricultural activity. The deputy director also refused to help. Three months later, he threw in the towel and decided to convert his land for nonagricultural use. For this he required a no-objection certificate from four different departments. Soon he became discouraged, running from one office to another. Giving up, he hired a middleman, who promptly bribed the different departments and got him the conversion in less than a month. The same tehsildar signed the order. By now he had lost six months, the monsoon had arrived, and he could not begin construction because the labor was deployed in paddy growing. He finally resumed construction after a year's delay.

Amrik Singh also qualified for Rs 100,000 seed capital under a government scheme to encourage entrepreneurs in rural areas. He promptly applied for a loan from the Development Corporation of Konkan. Again, after repeated follow-ups, he got the loan sanctioned after ten months. However, he received only Rs 69,000, because the corporation had run out of money. It seems a large part of the corporation's funds had been spent on the officers of the bureaucracy and on the traveling expenses of politicians. Consequently, the government shifted the power of giving loans to the district industries commission. Two and a half years later, when he had still not received the money, he lodged a complaint with the ombudsman, the Lokayukt of the Maharashtra government. Eight months later, he received the balance amount.

The experience of my pig farmer is no different from that of thousands of young entrepreneurs. In other countries, the entrepreneur's battle is with competitors. In India, the main enemy is the government bureaucracy. Bank nationalization has made matters infinitely worse. The bureaucrat has figured out that an entrepreneur has limited resources; he faces the pressure of time because interest costs mount by the day. So the government functionary attempts to delay every decision. It is true that many entrepreneurs fail because they are crooked or incompetent, but a large number do not succeed because they cannot cope with the bureaucracy. I am convinced that entrepreneurship in India will not flourish until we get rid of "Inspector Raj." As a citizen, I too have had to seek permissions from the government on various occasions. The last time was when we made the mistake of remodeling our house in Delhi. It took two years, thirty-eight visits, and hundreds of phone calls to the New Delhi Municipal Council and related departments before we got the permission to do so.

To the socialist mind of the 1960s, business families had a bad odor. Most people believed that they ran their businesses only for their families' welfare, without any concern for the consumer or outside investors. They thought that business houses were crooked—they did not pay their taxes, they underinvoiced their sales, and they siphoned money out of the business. Parliament was also obsessed with the "monopoly power" of business houses. Between 1964 and 1969 the government appointed four committees to examine the affairs of big business. They looked into seventy-five business families and did not like what they saw. Each year the Department of Company Affairs collected information on the growth of assets and sales of the seventy-five houses and placed it obediently before Parliament.

I am convinced that much of the findings were true. Some families defended themselves in private, saying that government controls and a 97 percent tax rate were responsible for their acts. The defense was also true. The License Raj did indeed make businessmen crooked. They cornered industrial licenses (meant to broad-base enterprise) and perpetuated the control of markets. Their products were shoddy because there was little or no competition. Shareholder returns were not the reason to do business—only control and ownership mattered. The way to do business was to get a "friendly bank" to give you a loan for the capital cost of your project. You recycled 15 percent of this loan and it became your equity contribution in the company. Then you siphoned out money from the business by giving your uncle commissions on purchases and your nephew commissions on sales. You could also grow by buying up cheaply the plantations and trading businesses of the departing English companies. By financing the elections of a dozen MPs, you could buy protection.

This was the scene when Indira Gandhi made her next major socialist move after bank nationalization. She enacted the Monopolies and Restrictive Trade Practices (MRTP) Act in 1969 and crippled private industry for a generation. When Parliament was debating the MRTP bill, I got the opportunity to meet the legendary J. R. D. Tata. Every citizen of Bombay knew that he controlled the largest industrial empire in India. He was the uncrowned prince of the only city in India where commercial power is esteemed above political power. Although the house of Tatas was at the top of the monopolies list, everyone respected JRD for his integrity. The Tata companies were thought to be squeaky clean and not to have indulged in questionable practices.

Piloo Mody, my fat and generous friend and a Swatantra Party MP, drove us to a shaded bungalow surrounded by a spacious green compound in the heart of the concrete jungle. We had come to JRD's home, The Cairn. We walked along a long, winding passage, interspersed with dozens of steps, past faded public rooms that seemed rarely used but were filled with flowers. Eventually we arrived in JRD's study. When he got up to receive us, I realized that he was smaller than I had imagined. I sat on a gray sofa and looked around the simple, lived-in room. The portrait of Jamshetji, the founder of the Tatas, caught my eye. So this was the daring man, I thought, who had defied colonial prejudice to set up a steel plant in 1907 and one of the greatest hotels in the world—the magnificent Taj Mahal Hotel—because he was not allowed to stay in the one beside it at the Gateway in Bombay.

JRD looked at me and said, "Yesterday in Parliament, they called me a monopolist with 'great concentration of power.' I wake up each morning and I am supposed to say, 'I have great concentration of power. Whom shall I crush today? A competitor or a worker in my factory, or the consumer?'" I did not quite know what to say.

"No, dear boy, I am powerless," he said. "I cannot decide how much to borrow, what shares to issue, at what price, what wages or bonus to pay, and what dividend to give. I even need the government's permission for the salary I pay to a senior executive." He smiled sadly. "Let's have some tea, shall we?"

Turning to Piloo, he said, "Now, let's see what your Swatantra Party can do about this bill—it is such an ineffective party! You do know what this new legislation means, don't you? Henceforth, I will not be allowed to start a new business or even expand an older one. What do they expect me to do?" There was an uncomfortable pause. "Sit here and wait till I die, I suppose." His face was again filled with sadness.

"But that's precisely why I have come, Jeh—to fight this bill in Parliament," said Piloo. "I need your comments on the draft memo for the Select Committee." Wearily, JRD opened the drawer and pulled out the draft. "I have corrected it in several places. Do you think it will do any good? She has the votes, you know."

Behind him in the cupboard I saw the famous reports—*The Mahalanobis Committee,* 1964; *The Monopolies Inquiry Commission,* 1965; *The Hazari Committee,* 1966; and *The Dutt Committee on Licensing,* 1969. He saw me looking at them and he said bitterly, "I have read them all." He handed Piloo the memo and we got up to go. On the way home, Piloo said, "You did not see him at his best, and this new bill has been the last straw. Things started going downhill with the nationalization of Air India sixteen years ago. He is a pilot at heart, and ever since they took Air India away, he has not been the same."

"He seems to live very simply for a man in his position," I said.

"He doesn't care about money," said Piloo. "He is not wealthy. All the Tata shares are in trusts. Whatever he inherited personally, he has also put that into a trust. In any case, he pays ninety-seven percent of his earnings to income tax; then, he pays wealth tax, and this takes his tax rate to over one hundred percent. His entire income goes in taxes, and he has to sell some assets each year to live on."

Despite their great efforts in Parliament, the Swatantra Party could not stop the MRTP bill. In the end, Mrs. Gandhi had the votes. No one read JRD's carefully drafted memorandum. A different sort of MP had come into power, one who had no use for such information. Tata's methods seemed to belong to a different era. The MRTP Act turned out to be one of the most damaging in modern Indian history. Any group with combined assets above Rs 20 crore was declared a monopoly and effectively debarred from expanding its business after 1969. A single company, with assets above Rs 1 rore, puny by world standards, was similarly placed under "antimonopolistic supervision and control."

Freddie Mehta, a director of Tatas, told me in 1989 that the Tatas made over a hundred proposals for new business projects or to expand existing ones over the twenty years since the MRTP law. All of them were rejected. In the mid-1980s, Rajiv Gandhi's government raised the MRTP asset limit fivefold to Rs 100 crore. Finally, in September 1991, the Narasimha Rao government scrapped this ridiculous law.

For all their difficulties from a hostile government over the past fifty years, Tatas' core businesses were strong and they were still the largest industrial group in 1997 with a sales turnover of more than Rs 35,000 crore ($10 billion). India's first political and commercial families, the Nehrus and the Tatas, had been family friends since Motilal Nehru first brought his two children, Jawaharlal and Vijaylakshmi, to JRD's father's home in the 1920s. This friendship had continued through the years. At Jawaharlal's request, JRD had sent a parcel of mangoes to the Mountbattens in the summer of 1949. For years, Indira Gandhi used to accompany her father to JRD's shack on Juhu Beach in Bombay, or they met when JRD was invited to Nehru's home in Delhi. Both Nehru and JRD had spent their impressionable years in Europe and acquired a rational, scientific temper. Even their vision of modern India was the same. Yet JRD continued to feel a sense of personal defeat until the end—he was not able to make Nehru or Indira appreciate the value of private enterprise.

JRD tried a number of times to engage Nehru, but each time he was rebuffed. Once, before lunch in Delhi, JRD innocently mentioned that the public sector ought to be making a profit. Nehru snapped back, "Never talk to me about profit, Jeh, it is a dirty word," and he turned to look out of the window, a well-rehearsed sign that Nehru was not interested in listening. To make amends, Nehru quietly took JRD to see his giant panda. Indira had a different manner, but she could be equally impolite. Every time JRD tried to discuss economic policy with her, she would begin to doodle or open her mail. Once when this happened, JRD whispered to his colleague, Sharokh Sabawalla, "She's not interested. We are boring her." Mrs. Gandhi looked up. "No, no. I'm not bored. I'm listening, Jeh."

JRD used to urge Mrs. Gandhi to give more autonomy and accountability to the public sector. At a lecture he once said, "I am convinced that a prime cause of the inefficiency and high cost prevailing in most public enterprises does not lie in the quality, competence, or dedication of their management and staff, but in the continuing denial to them of the degree of managerial freedom of action essential to the efficient management of any large undertaking." Thus, JRD summed up the failure of public enterprise in modern India. I agree. The blame squarely lies with the bureaucracy, which has done serious harm by consistently interfering with state enterprises on a day-to-day basis. The bureaucrat and the politician have slowed decision making to such a pitiful pace that morale and discipline have been crippled. In the beginning, it may have been natural for the ministries to keep a watch on their creations. However, in time, it should have given way to managerial autonomy, as in European public enterprises.

The Gandhians compounded the follies during Mrs. Gandhi's raj. They forced the government to protect traditional industries, like handloom textiles, even when it was obvious that we were throwing good money after bad. They were hostile to modern industry, especially large industry, because it did not create enough jobs and it destroyed traditional industry. They did not understand that unviable companies must die. They felt that once capital and employment are created, they must be protected at any cost. This brand of thinking came to be called Gandhian socialism, and it became especially popular during the Janata Party's rule. Gandhian socialists succeeded in reserving 863 industries for the small sector. This meant that only entrepreneurs who invested less than Rs 60 lakh could enter one of these industries, and thus they eliminated competition from large or medium enterprises. Small firms lost the incentive to improve their products, update production techniques, reduce costs, and introduce new technology or new designs. Underlying the Gandhian socialist philosophy was a distrust of the competitive market, and the belief that whatever could be produced by small industry was inherently better, no matter what the cost and quality.

Abid Husain's committee showed in the mid-1990s that small-scale reservation was responsible for our miserable export performance, and wanted it scrapped. The Gandhian socialists were unmoved. The committee argued that the success of Japan and East Asia had been built on the competitive export of simple manufactures—toys, shoes, garments. In India these were precisely the products reserved for the small sector. Competition would have improved our products and their potential as exports, but socialist thinking has sunk into our bones so deeply that the very subject is now a holy cow. We continue to hold the view that the small and the weak must be protected at any cost. Because of this thinking, our labor legislation makes it impossible to remove a worker on any grounds. Eventually, managements in the 1990s stopped recruiting labor and began to "farm out" manufacturing to smaller companies, who were not governed by the same stringent laws or were able to bribe labor inspectors. Labor in the organized sector stopped growing. My company did the same. We asked several entrepreneurs, one near Ahmedabad and another near Hyderabad, to manufacture Vicks throat drops on our behalf. We gave them supervisors to ensure quality, and our costs dropped significantly.

One day in the hot summer of 1975 I came home early. I had learned that the Supreme Court had confirmed that Indira Gandhi was guilty of corrupt election practices and would have to resign. I was shocked. "How can they do it for something so trivial? It is like removing the Prime Minister for speeding in traffic," I said. The Allahabad High Court had found her guilty of using a government employee in her election and state machinery to put up rostrums and mikes during her campaign. I felt it was a minor impropriety, not an offense. Mrs. Gandhi had won by 100,000 votes, and this could not have affected the outcome.

Instead of resigning, Indira Gandhi declared an Emergency. Before dawn the next morning, police parties acting under her orders woke up political opponents and locked them up. In the next thirty-six hours, India had changed from a democracy to a dictatorship. We were angry but our anger did not last long. We were not excessively political in the commercial city of Bombay, and like millions of Indians, we slowly got absorbed in our work and our daily lives. Because of press censorship, neither did we know what was happening. The one thing we did notice was that public life began to improve visibly. Clerks began to work in government offices, trains and planes began to run on time, labor in factories became more productive, public officials became courteous and responsive. People began to say that if this was what it would take to get India going, perhaps the Emergency was not such a bad thing. Even Gandhi's great disciple Vinoba Bhave called it Anushasan Parva, a period of discipline.

It was too good to last, however. Gradually the discipline began to decline. Indira Gandhi's rule was replaced by her son's tyranny. Sanjay Gandhi was only twenty-eight, but as far as his mother was concerned, he could do no wrong. A dropout from the prestigious Doon School and an apprentice motor mechanic with Rolls-Royce in England, Sanjay Gandhi had won his mother's confidence by giving her the slogan that won her the 1971 elections—"End poverty." As Sanjay began to rule with his coterie, we heard that every chief minister and cabinet minister had become his sycophant. Once Sanjay's slipper fell, we heard, and three chief ministers ran to pick it up. They followed his most ridiculous and most criminal orders without hesitation. All our institutions were infected by the virus. The police, the judiciary, the civil service, the state chief ministers, the cabinet, the presidency—all went into decline. Corruption became rampant and the cult of sycophancy became the ruling ideology as the number of political opponents in jail reached 100,000.

Despite press censorship, we began to hear horrendous tales. Sanjay Gandhi had the laudable thought that India's expanding population needed to be controlled. He hit upon the idea of sterilizing the male population of India. With his usual frenzy, he threw himself into this project. Anyone with more than two children would be mandatorily sterilized. He gave quotas to petty bureaucrats, but he did not lay down safeguards. There was no regard for age, whether a person was married or single, or how many children he had.

We wondered how did Indira Gandhi, who had grown up in one of the most cultivated homes in the country and was privileged to meet the best minds of the age, allow this to happen? How could the daughter of such a principled and idealistic father have done this debased deed? Some said that the answer lay in her contradictory childhood. Her mother had died when she was young; her early years had been lonely when her father was constantly away in jail; she was left in the care of her two tough aunts, Nehru's younger sisters. Hence, she had become introspective and withdrawn. This had been compounded by an unhappy marriage with Firoze Gandhi, who died young in 1960. Ever since his death, they said, she depended only on her two sons, Rajiv and Sanjay. Whatever the reasons, we were staggered by the insolence of her action.

Mercifully, the Emergency lasted only twenty-one months. Mrs. Gandhi made a blunder in thinking that she was still popular and could win an election. After all, even a dictator needs legitimacy. She called and lost the election. Morarji Desai, now a part of the Janata opposition, finally got what he had always wanted. He became India's fourth Prime Minister on 24 March 1977.

Between 1965 and 1991, instead of changing course as many countries did, we tightened our system, making it more rigid and bureaucratic. Even China changed course in 1978, letting in competition, and set out on a historic path of growth. India continued to eliminate competition because it regarded it as wasteful. We made modest reforms in the 1980s, but it was far from what was needed. For example, we partially lifted controls on cement, and within two years we went from terrible scarcity to plenty. The only loser was the cement controller. But we did not learn from this and decontrol other industries as well.

It is easy to blame Jawaharlal Nehru. Although he initiated the wrong economic policies, they represented the wisdom of his age. As the failure became apparent, many developing countries changed course in the early 1970s. India did not. One *has* to blame Indira Gandhi, who ruled India during most of this period. In another sense, the entire Indian ruling class is guilty. We cannot trust ourselves unless we understand how well-meaning professionals, steeped in a modern scientific outlook, could further such an insane economic tyranny. I feel a chill when I think that it was our brightest economists and administrators (some of whom later became reformers) who were in positions of power and who defended and acted on behalf of this tyranny. “India’s misfortune,” says Jagdish Bhagwati, “was to have brilliant economists.”

More and more young Indians insistently ask how we could have created these terrible things. And why did so few protest and demand economic freedom? The reason is that the victims were unorganized private citizens—farmers, businessmen, the unemployed, consumers. Businessmen are fine producers of goods and jobs, but they are cowards and do not speak out. One of them, Rahul Bajaj, did finally speak out at a hearing of the Monopolies Commission. The court asked him why he should not be prosecuted for producing more scooters than his licensed capacity. Bajaj replied, “Sir, my grandfather went to jail for my country’s freedom. I stand ready to do the same for producing on behalf of my motherland.” The MRTP inquiry was quietly dropped. In those dark days I used to worry myself silly that we had produced Vicks VapoRub beyond our authorized limit during a flu epidemic. Our legal manager spent months working with lawyers to prepare a defense in case we were hauled up. We lived in the same fear when it came to our profits. During good years, our profits had marginally exceeded the government’s profitability limit as laid down by the Drug Price Control Order.

Most people remember the Emergency because it represented a generalized loss of liberty. They do not understand that by suppressing economic liberty for forty years, we destroyed growth and the future of two generations. For the average citizen it was a great betrayal. Lest we forget, we lived under a system where a third of the people went hungry and malnourished, half were illiterate while the elite enjoyed a vast system of higher education, and one of ten infants died at childbirth. Our controls and red tape stifled the entrepreneur and the farmer, and the command mentality of the bureaucrat, which fed the evil system, continues till today to frustrate every effort at reform.