

If We Were Once Rich, Why Are We Now Poor?

The greatest thing since the creation of the world, except for the incarnation and death of Him who created it, is the discovery of the Indies.

—FRANCISCO LÓPEZ DE GÓMARA

Years later, my grandfather admitted that he was a little sad to see the British go. He raised himself on his elbow and called up to me as I was trying to sleep on the upper berth of the Frontier Mail, “It is certainly nice to feel the fresh breeze of freedom, but you must remember, my son, that India had been the best-governed country in the world for a hundred years, and Punjab had been its best-governed province. Why, Britain itself was not as well ruled because it was, after all, a messy parliamentary democracy, and it was not run by the Indian civil service.” As his words sank in, I peered out of the window at the dusty wheat fields of Punjab rushing wildly by in the light of the full moon. After a pause, he added, “Yes, the English were arrogant, but it was a cheap price to pay for a hundred years of peace, good government, railways, irrigation canals, and the best law and order in the world. You may call me antinational, but this is how I feel.”

“If the British were such good rulers, why was India so poor?” I asked. Clearly, he had not connected governance with prosperity. After a long pause, he admitted that he did not know. “For that you must speak to your uncle, Sat Pal.”

By now my father had been transferred to Delhi, along with the design offices of Bhakra Dam. We lived in the heart of New Delhi, in a spanking new whitewashed neighborhood called Kaka Nagar, under the shadow of Purana Qila, the old fort of Mughal emperor Humayan. We were surrounded by other families of engineers, colleagues of my father’s in the design office of the dam. Slowly, however, other families of government technocrats and professionals moved in and the colony expanded. The government had decided to solve the problem of housing its expanding bureaucracy by building spacious but simple and monotonous apartments on two levels. Those who lived on the ground floor had a pocket garden; those on the upper level got the roof terrace above, which was needed in those days before air-conditioning because we slept outside in the 100-degree heat of the summer nights. The colonies themselves were nicely laid out with playing fields and grassy squares, even if they were standardized constructions of the Public Works Department.

Soon after we arrived in Delhi, my mother’s first priority was to get us into a good school. After some quick research, she decided that it was going to be Modern School on Barakhamba Road. It had the right mix of the traditional and the modern, but most important, it had high standards. It was not as Westernized as our school in Simla. She felt that we needed to become stronger in Hindi and mathematics, which had been the weak spots in our earlier education. The question was how we were to get into Modern. We did not have money or influence. But my mother was determined. She went to

the school first thing Monday morning. The principal would not see her. She waited until lunchtime. She returned on Tuesday morning, and the same thing happened again. She came back home feeling defeated and she cried all afternoon. On Wednesday morning, she tried again. Finally, on Thursday the principal took pity and called her in. He was skeptical of our ability to cope with the tough standards of the school, but she persuaded him to test us. We did reasonably well in the tests and he reluctantly agreed to let us in on a trial basis. As it turned out, all of us did exceptionally well in our first exams. Grudgingly, the principal admitted to my mother that he had been wrong to treat her as he had.

Today every middle-class parent in India goes through my mother's anxiety and humiliation. It is worse now because the middle class has grown and the demand for good private schools has outstripped supply. The story of education in free India is a sad one. The government created a vast number of schools, practically free, after Independence. But they were so uniformly bad that the middle classes shunned them and scrambled for places in a few private schools. Thus there arose a situation of scarcity, and you needed either money or contacts to get in. If this is the plight of the middle class, the situation of the masses is tragic. The state has failed to provide both the quantity and quality of education.



In our history class at school we learned that Columbus went in quest of the riches of India and discovered America. Thinking that he had found India, he called the natives "Indians." The name stuck and so has the linguistic confusion. What captured my imagination in school was that India had once been fabulously wealthy and this had set the Europeans on their great voyages of discovery. In the European mind, the name "Golconda" became the symbol of the haunting wealth of India. Famous for his diamonds, the king of Golconda was the richest prince in India after the Mughal emperor. Today his fortress lies in ruins, six miles west of Hyderabad. As the Europeans got to know her, India's wisdom also attracted them. G. W. F. Hegel, the great German philosopher, wrote, "From the most ancient times downwards, all nations have directed their wishes and longings to gaining access to the treasures of this land of marvels, the most costly which the Earth presents; treasures of Nature—pearls, diamonds, perfumes, rose-essences, elephants, lions, etc.—as also treasures of wisdom. The way, by which these treasures have passed to the West, has at all times been a matter of world-historical importance, bound up with the fate of nations."

The Portuguese were shocked that Spain, their enemy, had won the prize of discovering America when it could have been theirs. It took them five years to get over the humiliation, and in 1497 they sent Vasco da Gama the other way, with a flotilla of four ships to go around Africa and find the real India. The two-year voyage was not a commercial success and they lost 116 of the 170 crew members. When they arrived near Calicut, on the Malabar Coast in southwest India, someone asked, "What brought you here?" A member of the crew replied, "We seek Christians and spices." However, the Indians were not interested in European trinkets and clothes. They made far better fabrics and trinkets themselves. But da Gama brought back something more important. He told King Manuel of Portugal of "large cities, large buildings and rivers, and great populations." He spoke

about spices and jewels, precious stones and “mines of gold.” He believed that he had found the legendary wealth of India. In the words of Adam Smith, “The discovery of America and the passage to the East Indies by the Cape of Good Hope are the two greatest events recorded in the history of mankind.”

The English got to this wealth more than a hundred years later, at the beginning of the seventeenth century. By then the kingdoms of Spain and Portugal were united through marriage. The English were at war with this formidable empire, and miraculously they had repelled the seemingly invincible Spanish Armada in 1588. The English first came to the Indies to plunder rather than to trade. They avoided the Portuguese on the west and went east to the Coromandel Coast, where they set up at Madras. Discovering that the fruits of trade were better than plunder, they turned back to the Malabar Coast. Carefully skirting the Portuguese, they set up a trading post in Surat, the rich Gujarati port of the Mughal Empire. Next, they gingerly came downwards and established on an empty island what became the flourishing commercial city of Bombay. On the eastern coast they moved northwards and set up another commercial city, Calcutta.

The English found that India produced the world’s best cotton yarn and textiles and in enormous quantities. India’s textile industry was “unbeatable for quality, variety and cost. This industry not only satisfied the large domestic demand but exported roughly half its output throughout the Indian Ocean and indirectly to South Asia and China. To this huge market, they brought in the beginning of the seventeenth century, the huge stimulus of European demand,” according to David Landes, the Harvard economic historian. Thus, by the end of the seventeenth century India controlled a quarter of the world trade in textiles. “Indian cottons transformed the dress of Europe Lighter and cheaper than woolens, more decorative (by dyeing or printing), easier to clean and change, cotton was made for a new wide world. Even in cold climes, the suitability of cotton for underwear transformed the standards of cleanliness, comfort and health,” adds Landes. The English learned about cotton textiles from India and soon they turned the tables. English textiles brought an industrial revolution to Britain but destroyed the lives of millions of Indian weavers.

During the Mughal Empire, at the end of the sixteenth century, India’s wealth sustained more than a hundred million people. With plenty of arable land, India’s agriculture was “not in any way backward when compared with other contemporary societies, including those of Western Europe,” according to the historian Irfan Habib. Its productivity too was comparable. Even the subsistence-oriented peasant got a good return. India had a vigorous and large skilled workforce that produced not only cotton but also luxurious products for the rich landlords, the courts, and the aristocracy. Consequently, the economy produced a fabulous financial surplus. “The annual revenues of the Mogul emperor Aurangzeb (1659–1701) are said to have amounted to \$450,000,000, more than ten times those of (his contemporary) Louis XIV. According to an estimate of 1638, the Mogul court of India had accumulated a treasure equivalent to one and a half billion dollars.” The economic surplus was used to support the vast and growing Mughal Empire and finance spectacular monuments like the Taj Mahal.

My uncle and the nationalists were correct in saying that India was the leading manufacturing country in the world in the early eighteenth century. Manufacturing, of course, meant handloom textiles

and handicraft at that time. India had a 22.6 percent share of the world's GDP, according to economic historian Angus Maddison. Paul Bairoch confirms that it had a 25 percent share of the global trade in textiles. "More important, there was a large commercialized sector with a highly sophisticated market and credit structure, manned by a skilful and in many instances very wealthy commercial class." Indian methods of production and of industrial and commercial organization could stand comparison with those in vogue in any other part of the world. It had developed an indigenous banking system. Merchant capital had emerged with an elaborate network of agents, brokers, and middlemen. Its bills of exchange were honored in major cities of Asia. It is not surprising, then, that English travelers to India found an economy that was dynamic and commercial, not stagnant or backward.

Given the enormous financial surplus, large exports, plenty of arable land and people, an agricultural productivity equal to the best in the world, and a large artisan workforce, the question is, why didn't a modern industrial economy emerge in India? Why did India become instead one of the most impoverished countries? Despite a dynamic and a growing commercial sector which responded to market forces and extensive foreign trade, the truth is that eighteenth-century India was significantly behind Western Europe in technology, institutions, and ideas. Neither an agricultural revolution nor a scientific revolution had occurred. "The competitive strength of Indian manufacturers in overseas markets was based on a ruthlessly inequitable system of distribution ... [and] in the long run the manual skill of the Indian artisan could be no substitute for technological progress." Even with his expanding trade, the Indian merchant was unable to change the local supply structure in order to improve the quality of his exports or to improve his logistics. This sort of flexibility in attitude would have required the application of a scientific mind.

Notwithstanding the surplus and the trade, the peasant was extremely poor. François Bernier, a French physician who spent twelve years in India, wrote about the poverty of the masses. He described their decrepit houses, their humiliating lives, and the dramatic inequality between the rich few and the impoverished many. Because the rapacious Mughal state took away something like half the agricultural produce, there was little incentive to improve the land. Despite their vigorous trade, the merchants hid their wealth for fear of the tax collector.

There is no easy answer to the problem that the country was prosperous and the people were poor. One obvious explanation is that in an overpopulated country there is plenty of cheap labor. When the supply of labor is elastic, it always seems more economical to hire people than to invest in machines. This was true in the eighteenth century and it is true today. An English observer wrote in 1807, "In India it is seldom that an attempt is made to accomplish anything by machinery that can be performed by human labor."

Having said that, it is important to remember that 250 years ago there did not exist the great disparities in income that exist today between nations. According to Paul Bairoch, the difference in income between Europe and India (or China) was 1.5 or 2 to 1. The economic fortunes of England and India began to diverge in the nineteenth century. India remained slow and England experienced an industrial revolution. This is not because India was a colony of England but because England had achieved the preconditions for industrialization—it possessed a variety of social, political, and economic institutions, attitudes, and values which permitted it to respond to technological

opportunities.

Thus, I return to the original question: If we were once rich, why are we now poor? Following my grandfather's advice, I went to meet my uncle Sat Pal. He had always been my grandfather's favorite. He came from Ramnagar, the village where the English forces had won the decisive battle against the Sikh army in 1849, paving the way for a hundred years of British rule in Punjab. Sat Pal went to our local Dayanand Anglo-Vedic School and later to the Government College in Lyallpur, where he won all the prizes. My grandfather used to dream of a brilliant career for him until one day, to his horror, he discovered that Sat Pal had become a Marxist. It was a great blow to our family, whose bourgeois hopes of prestige and wealth were shattered.

After Independence, Sat Pal became a respected labor leader in Cheharta, near Amritsar. He was loved by the workers and feared by industrialists. Welcoming me into his austere two-room home, Sat Pal painted the most devastating portrait of British colonial rule. The English began by robbing and plundering soon after they took over Bengal in 1757, he said. Their Lancashire mills crushed our handloom textile industry and threw millions of weavers out of work in the nineteenth century. As a result, our textile exports plunged from world leadership (before the start of Britain's industrial revolution) to a fraction of what they had been. Simultaneously, the indigenous banking system, which financed these exports, was also destroyed. Since the colonial government did not erect tariff barriers, Indian consumers also shifted to cheaper English mill-made cloth and millions of handloom workers were left in misery. In the process, British colonial rule "deindustrialized" India, and from an exporter of textiles, India became an exporter of raw cotton. Sat Pal quoted Sir William Bentinck, a contemporary observer, who had noted that "the bones of the cotton weavers were bleaching the plains of India."

I was about to interrupt my uncle when Vimla, his attractive Kashmiri wife, entered the room with two steel tumblers of buttermilk. She too was an ardent activist, and was now a member of the state legislature. They had met in Lahore during their heady student days in the 1940s. In their charmed leftist circle, Vimla was admired for her good looks, her deep convictions, and her glamorous background. Her father worked for the BBC. Her mother had been trained in Italy in the Montessori teaching system, and taught at Sir Ganga Ram College. They used to meet at the India Coffee House and listen to the poetry of Iqbal and Faiz Ahmed Faiz. It was something of a coup, I thought, that he got her to marry him when she must have been coveted by so many.

As we drank our buttermilk, Sat Pal turned to agriculture. Britain taxed the Indian farmer heavily. It changed the old land revenue system to the disadvantage of the farmer, who had to pay revenue whether or not the monsoon failed. Agriculture lost its capacity to generate savings, and a series of famines followed in the bad years in the last quarter of the nineteenth century. The worst one, in 1896–97, affected ninety-six million people and killed an estimated five million. Food also declined in areas where jute, indigo, cotton, tea, and coffee plantations were set up by the Europeans. Although these cash crops were profitable, the surpluses remained with the Europeans, who transferred them to England. The railways commercialized the food crops by moving them over long distances, and the enlarged national market sucked away the surpluses, which the peasants had earlier stored for the bad years. Thus, agricultural production remained stagnant for a century.

After paying the cost of its huge imperial establishment in India, the British government transferred its surplus revenues back home. Since India consistently exported more than it imported in the second half of the nineteenth century and early twentieth century, Britain used India's trade surplus to finance its own trade deficit with the rest of the world, to pay for its exports to India, and to cover capital repayments plus interest charges in London. According to Sat Pal, this represented a massive drain of India's wealth—8 percent of our gross national product was transferred to Britain each year. Thereby, Britain impoverished the Indian masses, and we financed its industrial revolution.

“In that case,” I said, “now that we are free and England has lost its colonies, India will become richer and England will become poorer. Is that right?” He nodded. My uncle had put forth the classic nationalist case for India's poverty during the colonial period. It was compelling. Sat Pal and Vimla's selfless life of integrity and simplicity also left a deep impression on me. After lunch, Vimla brought out an album of photographs of their younger days. One of the pictures was taken in a Bengal village. It showed Sat Pal and Vimla, two idealistic faces, helping out during the terrible famine in 1943. Another photograph showed Vimla in Prague in 1947, where she had gone to attend the first World Youth Festival as leader of the All India Students Federation. There was triumph in her eyes because she had been elected vice president of the World Federation of Democratic Youth. Her face conveyed the wonderful confidence that she must have felt as a youth leader at the peak of the international communist movement. At that moment she had every reason to believe that right was on her side and communists would rule the world one day. I thought of that spring day in 1968 when Soviet tanks had moved to crush freedom in Prague as I looked again at Vimla's happy face in the picture.

My meeting with Sat Pal and Vimla spurred me to read economic history and I found that the scholars mostly confirmed my uncle's classic analysis of India's poverty. Britain's trade policies, they agreed, had encouraged the import of manufactures and the export of raw materials. And by heavily taxing the farmer, Britain contributed to the stagnation of Indian agriculture.

As the years went by, however, a new generation of historians emerged who began to challenge the classic picture. These serious scholars expended great time and effort interpreting the historical data. One of them concluded that the land tax had not been exorbitant—by 1900 it was only 5 percent of the agricultural output, which was less than half the average per capita tax burden. Another agreed that there had been a “drain of wealth” from India to Britain, especially in the nineteenth century, but it was only 1.5 percent of GNP every year. The revisionist historians argued that India's payments to Britain were for real military and civilian services and to service capital investments (which increased India's wealth). Also, the overhead cost to maintain the British establishment—the so-called home charges—was in fact quite small. If India had maintained its own army and navy, it might have had to spend more money. They conceded that India did have a balance of payments surplus which Britain used to finance its part of its deficit, but they said that India was partially compensated for it through the import of gold and silver into India. Only a part of that precious metal was minted for coinage and most went into private Indian hands. Indians have always been mesmerized by gold and silver. Even the Roman Pliny had observed this, and had called India the “sink of the world's gold.”

The revisionists' most serious challenge was to the nationalist thesis that Britain had deliberately

deindustrialized India. They agreed with my uncle that Indian industry declined in the nineteenth century. They calculated that India enjoyed 17.6 percent of the world's industrial production in 1830, while Britain's share was 9.5 percent. By 1900, India's share had declined to 1.7 percent while Britain's had grown to 18.6 percent. But this decline, they argued, was caused by technology. The machines of Britain's industrial revolution wiped out Indian textiles, in the same way that traditional handmade textiles disappeared in Europe and the rest of the world. Fifty years later Indian textile mills would have destroyed them. India's weavers were thus the victims of technological obsolescence.

Handlooms all over the world gave way to mill-made cloth, and weavers everywhere lost their jobs no less than in India. Unfortunately, there were more weavers affected in India because India was the largest maker of textiles in the world. This is not to take away from the great misery and enormous suffering caused by their impoverishment. If the British Raj had been sensitive to their plight, it might have erected trade barriers in India. This might have cushioned the impact and Indian handmade textiles might have survived for a period. (It is true that the British government did put up barriers in eighteenth-century England against Indian textiles.)

After 1850, Indian entrepreneurs began to set up their own modern textile mills. By 1875, India began to export textiles again and slowly recaptured the domestic market. In 1896, Indian mills supplied only 8 percent of total cloth consumed in India; in 1913, 20 percent; in 1936, 62 percent; and in 1945, 76 percent. Both British and Indian capitalists made large profits during the First World War. While the British businesses remitted their wartime profits to England, Indian businessmen reinvested theirs in new industrial enterprises after the war. Thus, Indian industry began to grow rapidly after the war. G. D. Birla, Kasturbhai Lalbhai, and a dozen other entrepreneurs built significant industrial empires in the interwar years. Manufacturing output grew 5.6 percent per annum between 1913 and 1938, well above the world average of 3.3 percent. The British government finally provided tariff protection from the 1920s. This helped industrialists to expand and diversify. The Birlas went beyond textiles and jute into sugar, cement, and paper. Hirachand, the construction magnate, diversified into shipping; Shri Ram, in the north, went into sewing machines; and Tatas, in Bombay, started an airline which later became Air India.

By the Second World War, the pre-First World War supremacy of British business was broken and Indian entrepreneurs were now stronger and in a position to buy out the businesses of the departing foreigners. The share of industry in India's GNP doubled from 3.8 percent (in 1913) to 7.5 percent (in 1947). The composition of India's trade also changed—the share of manufactures in its exports rose from 22.4 percent (in 1913) to 30 percent (in 1947), while the share of manufactures in imports declined from 79.4 percent to 64 percent. Industrial employment, however, did *not* grow in tandem. Modern industry could not make up for the loss in jobs suffered by handloom weavers.

Indian nationalists have exaggerated the economic importance of India to Britain. They thought that the Indian empire was hugely profitable. They got the idea from Cecil Rhodes, the great imperialist of the nineteenth century, who used to say, "The Empire is a bread and butter question ... [we] must acquire new lands for settling the surplus population of the country, to provide new markets for the goods produced in factories and mines." Churchill was a leading exponent of this view in the

twentieth century. Conservatives certainly believed it, but even the left wing of the Labour Party thought so. Bevin told the House of Commons: "If the British Empire fell ... it would mean the standard of life of our constituents would fall considerably." The truth is that the Indian colony was not terribly profitable to Britain. After the crude period of exploitation in the eighteenth century was over, Britain's rising prosperity in the next century owed more to its free trade with the "new world" and to its investments in America. If there was a "drain," it was by the transfer of dividends by English companies from America. Certainly, a few Englishmen became very rich from India—the owners of the tea and indigo plantations, the shareholders of the East India Company and other commercial firms, the employees of the managing agencies, the railway builders, the civil and military personnel, and others connected with India. But the profit to Britain as a whole was meager.

My uncle's prediction also turned out to be wrong. Britain did not become poorer after losing India. Instead, it enjoyed shocking prosperity in the 1950s and 1960s, at the very time that it was losing its colonies. So did France, Holland, and other colonialists. The fact is that Britain's colonial prosperity was not founded on the exploitation of India. In the end, whether Britain impoverished or enriched India is really an academic question. What is more relevant is why the forces of global capitalism in the second half of the nineteenth century and early twentieth century did not release widespread growth and development in India, as they did, for example, in Japan. The rapid building of railways and canals and the simultaneous expansion of foreign trade should have acted as a strong engine of growth. India had an experienced merchant class which had begun to develop modern industry.

By 1914, India had the world's largest jute manufacturing industry, the fourth-largest cotton textile industry, the largest canal network, the third-largest railway network, and 2.5 percent of world trade. Fifty years earlier, Karl Marx had predicted that the introduction of railways and modern factories into India would transform the subcontinent. Why didn't it happen? India remained largely nonindustrial and extremely poor at the time of Independence. Modern industry contributed only 7.5 percent of national income at Independence, and employed barely 2.5 million people out of a population of 350 million. Why didn't an industrial revolution occur?

My father's English boss and other colonial officials used to blame India's poverty on the otherworldly spirituality of Hindu life and its fatalistic beliefs. Max Weber, the German sociologist, who admired the richness of India, attributed the absence of development to the caste system. Swedish economist Gunnar Myrdal found that India's social system and attitudes were an important cause of its low productivity, primitive production techniques, and low levels of living. According to Myrdal, poor work discipline, contempt for manual work, lack of punctuality, alertness, and ambition, low aptitude for cooperation, and superstition were the result of inhibiting attitudes. These were compounded by unfavorable conditions, such as a debilitating land tenure system, low standards of efficiency and integrity in public administration, weak participation of the people in local affairs, and a rigid and unequal social structure. Myrdal believed that these premodern attitudes and institutions had to be attacked directly, primarily through education, and India could not wait to erase them as a by-product of growth and income. The only agent that could break the forces of stagnation, he felt, was the Indian state. But the Indian government would not be able to do it, he concluded, because it

was a “soft state.” It would not be able to impose the social discipline that this required. He said this in 1967, and the Indian state has become even “softer” since then.

Max Weber is often criticized for saying that Asian societies could not become capitalist. But the criticism is unfair, for he was addressing a different issue: he was trying to understand why modern capitalism, as well as other aspects of the modern world such as natural science and the rational mastery of nature, arose in Protestant Europe and not in traditional India, China, and Japan. After all, China’s level of technology was higher than that prevailing in Europe in 1500, as Joseph Needham and others have shown. But China lacked what the West later developed—the scientific method of experiment and empirical observation which helped Europe to conquer nature. The scientific method came about by an intellectual temper which sought the causes behind physical principles through abstract reasoning.

Capitalism developed in the East when India, China, and Japan confronted the technology and social prowess of the West and shed some of their inhibiting institutions. China got rid of political Confucianism and its imperial system with its mandarin class of gentleman scholars. Japan dropped its old class divisions and redirected its samurai warrior ethic towards the market. India shed its Brahminical contempt for modern learning and critically re-examined its traditional institutions in the nineteenth century. Thus, capitalism developed in the Eastern countries only when they came into contact with the West and its ideas of economic modernity.

Deepak Lall, another economist, has similarly explained economic stagnation in terms of a low-level “Hindu equilibrium” around the caste system which bought stability in the context of political warfare, monsoon failure and climatic uncertainty, labor shortage, and an under-valued merchant class. Lall argues that “India’s social organisation and agriculture system were a second-best Pareto-efficient response to its specific environment.” David Landes, the economic historian at Harvard, has recently reopened the politically incorrect controversy relating to geography and the weather. He blames India’s enervating heat. For this reason, rich countries lie in temperate zones and the poor in the tropics and semitropics. Although air-conditioning and tropical medicine, he says, have leveled the playing field somewhat after the Second World War (and made possible the prosperity of the American South), the unpleasant truth is that “nature like life is unfair, unequal in its favors” and “geography brings bad tidings.”

I am always skeptical of easy cultural or geographic explanations. In my experience, successful Hindu entrepreneurs can be both extremely religious and aggressive in business. The Indian farmer responds quickly to market-based incentives, as the green revolution demonstrates. Brahmins will plow their own land in traditional Uttar Pradesh if they have to, and conservative Rajput Thakurs in Rajasthan will shed their feudal ways for the sake of a commercial opportunity. Moreover, there are substantial non-Hindus in India and these communities have also been stuck in the same rut of stagnation. Other Asian countries such as China and Indonesia were equally backward, but they had no “Hindu equilibrium” to explain away their stagnation. Tropical, enervating Singapore has achieved Western levels of prosperity despite the unfairness of nature. I cannot help but conclude that these cultural stereotypes, and the dirigiste prescriptions that flow from them, stem from a paternalism bordering on contempt for the masses of the Third World. How could these wretched and ignorant

peasants behave like rational consumers and producers of classical economics? But they do behave in that way, as empirical evidence has shown beyond doubt. The 1982 Development Report of the World Bank points out, “All farmers—small, medium, and large—respond to economic incentives. Far from being ‘tradition-bound peasants,’ farmers have shown that they share a rationality that far outweighs differences in their social and ecological conditions.”

Economic historians no longer seek explanations of India’s economic backwardness in culture—the otherworldly values of the Hindus or the immobilizing effects of the caste system or the conservative habits of the merchant caste. They look to economic factors that motivate a businessman to invest in a business—the size of the market, the capability of suppliers, the costs of production, the distribution hurdles, the availability of technology, and the state of competition. Amiya Kumar Bagchi argues that it was lack of effective demand that limited business opportunity. Indians were just too poor, he says, to buy modern goods and services. With weak purchasing power the market remained tiny, and this prevented entrepreneurs from investing. I am not convinced, however, that the lack of demand provides a sufficient cause. If the domestic Indian market was small, the entrepreneur could have supplemented it by producing for overseas markets. Morris D. Morris, the economic historian, says that backwardness is the result of supply constraints. An Indian entrepreneur, he feels, was beset by formidable uncertainties because of a shortage of technology, skilled labor, and capital—all of which raised his cost of production. According to the Calcutta historian Rajat Ray, the Indian businessman did not export because he could only make inferior-quality products, which were not acceptable to the world market. And he did not have the technology to make superior products. In his view, the single biggest failing lay in the technological backwardness of Indians. Ironically, a hundred years later, the same situation persists.

Thus, there is no easy answer to India’s backwardness. Unlike the nationalists, I do not believe that there was a British conspiracy to deliberately underinvest in India, or to sabotage Indian business interests (despite G. D. Birla’s difficulties with the Scottish jute lobby). The nationalist thesis is weak because British business was not a homogeneous force. Bombay’s textile mills in the nineteenth century were built with credit, technical assistance, and machines from the British textile machinery makers even when these mills were a competitive threat to Manchester’s mills. Burn and Company, a full-blooded European company, had no hesitation to start making steam vessels in India when it found it cheaper than importing them from Britain. Businessmen invest whenever and wherever profit is to be made, and their decisions have little to do with nationalism or racial considerations. Companies only look to their bottom line and do not fly the flag of their parent countries.

What then is the verdict on British rule in India? Did the British impoverish India? There is no question that in the eighteenth century the British plundered and looted India’s wealth, as all conquerors have done in history. The more important historical question is if Britain systematically exploited its colony by creating ongoing institutions that were to India’s detriment. This has to do with the nature and theory of colonialism. I have already said that the British did not deliberately deindustrialize India. It was the industrial revolution that threw millions of weavers out of work. It would have happened anyway when the new technologies reached India. British government policy could have cushioned the impact by erecting trade barriers, but protecting handlooms would have

been a temporary palliative at best.

Odd as it may seem, Britain did not “exploit” India enough. Had it made the massive investments in India that it did in the Americas, India would have become prosperous and a much bigger market for British goods. An impoverished India was certainly not in Britain’s economic interest. The tragedy is that the failure to develop India was a great loss for Great Britain as well as for India; a richer India would have been even a better customer, a better supplier, and a firmer basis of Empire. Our nationalists have failed to comprehend that capital is a progressive and positive force, however exploitative it may appear. Marx understood this. He knew that capitalism is the only efficient way to accumulate capital, make investments, raise output, and increase productivity. Even today, many Indians, with their phobia of multinationals, do not understand this.

Britain’s main failure was to remain detached when it came to development and economic growth. Unlike the Japanese government following the Meiji reforms after 1868, which actively promoted the country’s development, Britain neglected India. It was an imperial power and had little interest in the people of India. It did not actively encourage investment either by Indians or by Englishmen. It did not try to educate the Indian masses—83 percent of Indians were illiterate at Independence. The British education system in India produced only a thin upper crust of extremely well-educated Indians. The Japanese and the Koreans, at the same time, concentrated on making their masses literate. By 1950, more than half of Japan’s and Korea’s populations were literate. Although it built railways and canals, Britain made no effort to provide credit to entrepreneurs or farmers in a capital-starved country. Nor did it sufficiently protect the infant Indian industry that came up in the nineteenth century (although it did from 1921 onwards). Then “no colonial power helped its colony to industrialise,” says the wise economist Arthur W. Lewis. The crude fact is that Britain did not understand how to make an economy grow. It only knew how to keep the budget balanced.

Indian nationalists have overestimated Britain’s impact on India’s wealth and poverty. To be sure, there was a “drain” of wealth from India to Britain, especially in the nineteenth century. They used our export earnings to finance the transfer of our wealth to Britain rather than reinvesting the trade surplus in India. It is also true that India progressively became an exporter of raw materials and importer of manufactured products. India’s leaders took this to mean that foreign trade and foreign capital were responsible for our poverty, and closed our economy and pursued a policy of self-sufficiency. In the process, they wasted an opportunity. They forgot that India had a centuries-old tradition of trading before the British came, and that it had once enjoyed enormous prosperity through exports and imports. For these and other reasons, we became pessimistic about our ability to compete in the world economy and regain our historic preeminence as a great trading nation. We closed our doors. And our share of world trade declined from 2.4 percent in 1947 to 0.4 percent in 1990. We learned the wrong lessons from history.

How to make a poor nation prosperous is a more difficult question. The answer seems to lie in technology and institutions. Since Britain’s industrial revolution in the late eighteenth century, not only has there been for the first time in recorded history a continuous flow of inventions, but they have been absorbed commercially as profitable innovations. History teaches that a nation’s ability to absorb these innovations and create an industrial revolution depends on having the right institutions in

place—for example, property rights, enforcement of contracts, roads to reach products, schools, and stable governance. In the second half of the twentieth century, Asian tigers demonstrated that it can be done—a poor nation can become rich, and very quickly. They took less than thirty years to transform their societies, whereas the West needed a hundred. Latecomers too are sometimes blessed.