An Agenda for Indian Economic Reform

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Last October, thirteen of us, all economists, got together in the hope that as the country gears up for elections, we could start a conversation by identifying a set of policy ideas that might help inform party manifestoes and policy visions. While our views stretch across the spectrum from right to left, we found surprising agreement on the challenges India faces and the reforms it needs now.¹ Two of us sifted through the set of ideas, picking what we felt were the top challenges and proposals to address them.

As we see it, rethinking government is key. Government capacity is limited. We need to target it better while trying to enhance it. Stability in government policy is important so that our farmers and firms can plan better, and markets can play a more effective role. Co-operative federalism, the center and states working together and learning from each other, is essential.

1. The massive aggregate fiscal deficit of the states and center combined, leaves fewer, costlier, resources for private investment. We should aim to hit the FRBM-suggested 5% by 2023, but not by creative accounting or off-balance-sheet transactions. Instead, we must increase revenues, both through better compliance and more progressive taxation, and target spending better. State deficits have grown, partly because markets assume that the center will bailout over-extended states and therefore do not charge them higher interest rates. To incentivize better behavior, any state’s borrowing above agreed limits should be funded through special bonds that are explicitly free of any federal guarantee. A center-state council modeled on the successful GST council could supervise fiscal federalism.

2. Three sectors that are distressed today are agriculture, power, and banking, despite massive past government intervention, and often because of it. For example, periodic export bans and large-scale imports to keep food inflation down have radically moved the terms of trade against agriculture, while reducing the farmer’s ability to plan. Cheap or free power to farmers have depleted the water table to the point of disaster. Farmers do need assistance. However, the instruments used – loan waivers, inflated MSPs without adequate procurement, and input price subsidies— often exacerbate the problem. In addition to enhancing investment in new technologies and irrigation, a government move toward lump sum payments to farmers for holding below a certain limit, in the spirit of Telengana’s Ryathu Bandhu scheme, will be an improvement.

Similarly, distressed state-owned power distribution companies stand between power producers who want to sell more and consumers who want more reliable power. The solutions are well-known – better metering, less distorted pricing of both power as well as

¹ The list of proposals is at https://www.uchicago.in/events/press-briefing-an-economic-agenda-for-the-next-five-years/
energy inputs, and the use of new, cleaner technologies for distributed production and decentralizing distribution. All these require rethinking the government’s role, as will any sustainable solution to banking sector distress.

3. We need a better business environment – whether to create the jobs for those leaving agriculture, urban schools, or our universities, or to ramp up our woefully inadequate exports. We need to learn from state experiences about what works in areas like land acquisition, industrial regulation, provision of power and logistics, and environmental clearances. A Center-State Productivity Council can be useful for this; such a Council could revive the idea of Special Economic Zones where coordinated land, environmental clearances and transportation infrastructure are available on a “plug-in” basis. Such zones, not necessarily targeted at exports, may also be used to experiment with reforms such as changes in labor laws before an all-India roll-out, to provide the evidence needed to build consensus for them.

4. Sustainable growth requires more effective but less burdensome regulation. Our cities are choking and climate change is upon us. Municipalities need the powers and funding to deal with these challenges, which means more decentralization. In other areas, we need more centralization: for instance, a new and technically beefed up environmental regulator, combining powers that are currently with multiple bodies, setting fees based on careful analysis of tradeoffs, and enforcing them.

5. Government has to provide for benefits, but is not always best-suited to deliver them. To reduce the implementation burden and free up its ability to take on new challenges, government should move towards cash transfers. As a first step, beneficiaries of all specific government subsidy programs should have the choice between cash transfers and benefits in kind.

Many of our challenges also have to do with enhancing the capabilities of our people.

6. We need more skilled personnel in government -- at higher levels in technical areas like digitization, trade negotiation, and environmental regulation but also at lower levels outside the larger cities. More lateral entrants, merging into the permanent civil service, are desirable near the top. At lower levels, too many youth waste years taking competitive exams for government jobs that most will never get. One alternative that will give them skills and work experience is a multi-year paid government internship at salaries comparable to entry level market wages (much less than what the government pays) for those under twenty-six to work as support staff in government offices/public sector enterprises where needed. Performance on these could help entry into permanent government jobs, though political pressure to make these internships permanent should be resisted.

7. The Right to Education Act’s focuses on input requirements for schools that have little bearing on learning outcomes, which have deteriorated alarmingly. Learning must be our central focus, with all schools, public and private, responsible for delivering a minimum level
of basic skills to every child. Bringing those falling behind up to par through remedial teaching will be critical.

8. We must address the coming explosion of Non-Communicable Diseases, which will require engagement with the frontline providers. The vast majority of these have no formal qualifications, but the evidence suggests they can be trained and pushed towards practicing better medicine. Since they have the patients’ ears, the health system should use them better rather than ignoring them.