

India

Status Index (Democracy: 7.95 / Market economy: 6.46)	7.21	Management Index	6.00
HDI	0.602	Population	1,070.8 Mio.
GDP p. c. (\$, PPP)	2,892	Population growth¹	1.9%
Unemployment rate	11.1%	Women in Parliament	9.3%
UN-Education Index	0.61	Poverty²	34.7%
		Gini-Index	32.5
Source: UNDP: Human Development Report 2005. Figures for 2003 – if not indicated otherwise. ¹ Annual growth between 1975 and 2003. ² Population living below \$ 1 (1990-2003).			

A. Executive summary

India is a country with a long-standing democratic tradition, where the state monopoly on the use of force is assured apart from some conflict zones and where national identification goes unquestioned by relevant actors. The country can boast a nearly continuous record of free and fair elections, frequent and peaceful power transfers, and strict civilian supremacy over the military. Freedom of association and opinion are assured

Horizontal division of powers (especially the independence of the judiciary) is assured; vertical separation of powers suffers from frequent destabilization of state governments by interested political actors. The slow functioning of the courts and the massive accumulation of unfinished litigations hamper the dispensation of justice. There are also some deficits in law enforcement, police neutrality and the safeguarding of civil rights in tension-prone areas. Political parties are highly fragmented, weakly institutionalized and unstable. Associations are plentiful but are rather weak, whereas social movements have become visible and assertive.

Economically India is still a lower income country. After 1991 the country became a full-fledged market economy with only very few restrictions for local and foreign enterprise. The country is still protected against foreign competition by high tariff barriers, however. Internally reservations for the small business sector, the existence of state banks and state enterprises (only reluctantly privatized), the regulation of agriculture, massive infrastructural deficits and an overly detailed and protective labor, land and insolvency regime still stifle competition and economic dynamism. In spite of this unfinished agenda, the economy is booming, inflation is moderate, exports are buoyant and the balance of payments and debt situation are comfortable. However, the budget deficit is still massive, crowding out private investment to a certain degree. Social and ecological sustainability of Indian development is still not assured, as absolute poverty, social exclusion and ecological degradation are still severe and only partly administered by the government.

Difficulties regarding the development of a market democracy are moderate. There are some problems for the government to rein in Hindu radicals or leftist coalition partners, but the steering capability of the government has proved adequate. Available resources were not always used wisely: untargeted subsidies abound, welfare expenditures are far too low and corruption is still widespread. The government cultivates an attitude of utmost national autonomy and international cooperation, and is therefore circumscribed.

B. History and characteristics of transformation

Economic and political transformation in India occurred at very different times. Self-government and democratization preceded economic liberalization by decades. Democratic participation was introduced by the colonial constitution in 1935, largely copied by the constitution of independent India. Democratic continuity since has been uninterrupted, apart from two years of the Emergency Regime from 1975 to 1977. The Congress Party dominated at central and state levels until 1967, making changes to government nearly impossible. Afterwards the party system became progressively more pluralized, and changes in government (first at the state, later at the central level) occurred frequently. This went along with increasing mobilization and the articulation of new, lower caste groups, the forceful expression of regional, linguistic and religious identities and therefore also with rising internal conflict levels. The traditional civil society remained underdeveloped and colonized by state and party agencies. New social movements, however, did flourish in the last two decades (1980s and 1990s). Because of the intense political mobilization in the country and the fact that only elections bestow legitimacy to leaders, India has to be reckoned with as a consolidated democracy, even though civil rights and the federal setup were frequently overruled.

India's transformation into a full-fledged market economy is recent. For decades, the country followed the path of import substitution and state-led industrialization, leaving considerable space for private enterprises as junior partners of the state. A first, hesitant liberalization came into effect in 1985 resulting in a deregulation of the internal market and of the high technology sector; a complete market friendly turnaround was propelled by the severe balance of payments crisis during the period 1990 to 1991, forcing the country into an agreement with the IMF. With the subsequent reforms, India became an open market economy with very few sectors restricted for private and foreign enterprise. The economy is still protected against foreign competition by comparatively high tariffs and frequent use of anti-dumping measures, however. Internally reservations for the small business sector and the only partial liberalization of agriculture act to restrict competition.

C. Assessment

1. Democracy

For decades, India has been a fully consolidated, inclusive democracy with no veto player legitimized by the political process. However, there are deficits regarding law enforcement, police neutrality and safeguarding of civil rights in tension-prone areas.

1.1 Stateness

There are virtually no problems of stateness in India. State monopoly of the use of force is nearly complete, apart from some rural conflict zones in central India, areas of separatist activity in Kashmir and some small states in Northeast India. Identification with the nation and the definition of nationality pose no real problems. Only some splinter groups in zones of separatist activity do not regard themselves as citizens of India. The secularist credentials of the country did suffer somewhat under the rule of the Hindu nationalist Bharatiya Janata Party (BJP), which had to moderate its stand to keep the alliance together and to enlarge its voter base. After the takeover by the Congress Party in 2004 a return to more or less undiluted secularism occurred. The country inherited an efficient administration from the colonial government, with recruitment and promotion based on merit. This heritage was to a large degree maintained at the central level. In the administration of the union territories politicization and recruitment according to excessive reservation quota (along caste lines) became more common. Indian police forces are highly inefficient, politically dependent and prone to corruption. Consequently, the conviction rate of criminals is low, police atrocities against civilians are common and the government has to rely on the army to quell internal disturbances.

1.2. Political participation

Since independence India can boast of a nearly uninterrupted record of free, fair and more or less violence-free elections, accompanied by increasing voter turnout (especially among the poorer and least developed population groups) and by frequent and peaceful power transfers. Even in conflict-ridden union territories (for example, Kashmir), elections did have de-escalating effects. The military never acted as a veto power; it is under strict civilian control and conceives its own role in purely professional terms. Freedom of association is guaranteed, the forming of interest groups is legally easy. Most of them are only poorly institutionalized, fragmented, internally hardly democratic and often not really independent. In this regard, social movements of recent origin are different.

1.3. Rule of law

Horizontal separation of power is assured; vertical separation was often overturned by politically motivated replacements or undermining of state governments. Control of the executive by the Parliament suffers from parliamentarians' modest professional competence and lack of scientific support. The Supreme Court enjoys considerable and broad-based competence in the examination of constitutional correctness of laws and as an appellate body concerning violations of human rights. The court has become rather proactive in recent years and it did not abstain from harshly criticizing government neglect. The same can be said about the independent Election Commission, which tightly controlled the upkeep of stipulated election codes.

The courts remained institutionally autonomous, in spite of pressures by the executive, interference in nomination and transfers of politically unpopular judges. Rule of law is restricted by the slow functioning of justice, leading to a massive accumulation of unfinished litigations. This was also caused by low thresholds for initiating and prolonging processes, overly detailed laws and regulations, etcetera. Underprivileged sections of the population shy away from the courts litigation costs are high. Misuse of public office is frequent in India and only intermittingly sanctioned (although more so than in previous times). This has to do with the overregulation of the economy, which recently is receding. The culture of corruption is deeply entrenched in India. Therefore, India is listed at the top of several international rankings on corruption and malpractices. Spectacular cases involving parts of the entire political class brought a slow reorientation, due mostly to judicial activism.

1.4. Stability of democratic institutions

Democratic institutions in India are more or less stable, leaving out the frequent destabilization of state governments (for political ends), the shaky character of multiparty governments in the last decade (which did confer political blackmail power on even minor parties), combined with the endemic defection of parliamentarians to the opposition or new parties to profit from new political equations. This has also delayed important constitutional and economic reform projects. A new anti-defection law (2004) tries to curb defections by limiting the premium for rebels. Institutional efficiency is also hampered by the overregulation of the economy, proliferation of ministries and government agencies and the already mentioned congestion of the judicial system. Democratic institutions are, however, accepted and nurtured by all political parties (even the extremists) and social groups. Their legitimacy is also unquestioned by the population.

1.5. Political and social integration

The Indian party system is stable, the parties themselves only weakly institutionalized, and party discipline is low despite measures against defections. Formal organizational structure is often replaced by informal procedures, “clientele-ism” and identity politics. The communist parties and the BJP, with its disciplined frontal organizations, represent an exception to this pattern. The Congress Party has become deinstitutionalized to a large degree. Membership to associations in India goes into the millions of people, but interest groups are rather weak, fragmented across ideological and party lines and they often fight against each other rather than their opponents. This is also, why labor relations are prone to conflict. Because of the long-standing dominant economic role of the state, labor unions and employers’ federations are only partly autonomous. Economic liberalization brought the emergence of new, professional associations. Social movements (for instance women’s, environmentalist or human rights, etcetera) have become more visible and assertive. Members of the middle class dominate these movements. Lack of associational links between the population and interest groups is to some degree compensated for by direct links between parties and social groups.

2. Market economy

India has seen a far-reaching, rapid and successful transformation of its economic order since 1991. There still exist some transformation deficits in the realm of privatization, the dismantling of subsidies, the creation of a market-friendly labor, land and insolvency regime and concerning the reduction of the massive public deficit.

2.1. Level of socioeconomic development

According to commonly used development indicators, India is still regarded as a lower income country, albeit progressing quite rapidly. Its development level, measured by the HDI, nevertheless does not assure every citizen’s basic needs or freedom of choice. India is still the country with the largest number of people living in absolute poverty (approximately 26% of population). Incidence of poverty has declined since the middle of the 1970s (lately at a decreasing rate) but lately has become increasingly concentrated geographically. Development progress was uneven; the gap of social indicators between union territories increased in the 1990s. Poverty and social exclusion is concentrated in some sectors (agriculture, informal sector), some social groups (lower castes, tribal groups, Muslims) and union territories with poor economic dynamism and bad governance. There is no equal opportunity in spite of moderate inequality and

numerous schemes for poverty eradication and assertive action on behalf of the underprivileged.

2.2. Organization of the market and competition

Market competition is assured in most parts of the economy. The formerly high regulation density has decreased with the exception of agriculture, the labor and land markets; implementation procedures are still cumbersome. Several hundred products are still reserved for exclusive production by the small business sector. Regulation of foreign and big local companies was abandoned. The investment regime is now among the freest in Asia. Sector concentration indices are still high, despite government endeavors to the contrary during the last few decades. Legal procedures for the restructuring and liquidation of ailing or public companies are inadequate, time-consuming and inefficient. The weak protection of shareholders encourages risky company strategies. Trade barriers are still considerable, notwithstanding massive tariff cuts and the nearly complete abrogation of non-tariff barriers, the average tariff rate stands at about 26% (2004) and is supported by the frequent use of anti-dumping measures. Customs clearance is more time-consuming than in competing economies. Privatization was proceeding at a rather slow pace in the 1990s but accelerated after 1998, albeit with the nearly total exclusion of enterprises at the state level.

The Indian financial system is highly developed and has a high coverage. It was thoroughly reformed after 1991. State banks are still dominant, however the public sector absorbs a considerable share (41%) of bank resources and around 40% of bank credit is still directed to priority sectors. Banks' equity capital is nearly sufficient to cover potential losses of non-performing credits (whose share has come down).

2.3. Currency and price stability

In India, a consequent policy of price stability was followed for political reasons (tolerance for inflation was traditionally low). This did not change much during the period under scrutiny, although high public deficits and mounting oil prices made the containment of inflation difficult. The Central Bank of India always pursued a cautious monetary and currency policy, supported by strong internal mobilization of savings (by private households) and increasing inflows of foreign capital and remittances. Currency reserves reached a very comfortable level. The level of external indebtedness is high but not dangerous because of its long-term character.

2.4. Private property

Property rights are adequately defined, although the constitution allows restrictions in the public interest. Private property, the prerogative of private initiative and necessary to attract foreign investment, is unquestioned by state governments and important political parties. The labor market is still highly regulated, mass dismissals or company closures are practically impossible. This applies also for agriculture. Free transport, storage or price setting is possible only in market niches. However, privatization of public companies made some recent advances.

2.5. Welfare regime

In India, there is only a rudimentary system of social security for the privileged workers of the state and formal sectors, although the government is now planning an employment guarantee for the poor. These guarantees are assisted by a gamut of central and state schemes, subsidized food items, employment during crisis periods, self-help programs and projects of integrated rural development. These schemes are still badly targeted spreading significantly to the non-poor, despite improvement efforts. Public expenses for basic social services are inadequate by international comparison and do not guarantee universal coverage, not taking into consideration the question of their mostly poor quality. Therefore, India is not a frontrunner in improving social indicators, which show a wide variation between union territories and social groups. In consequence equality of opportunity is not assured: social indicators correlate positively with income, position in the caste order and urban environment. Women are disadvantaged in a systematic way, especially in the “Hindi belt”, demonstrated by the extremely low numbers of women in the population. Low castes, tribal groups and Muslim people are discriminated against in terms of land ownership and – despite reservations – in their access to positions in the public sector.

2.6. Economic performance

The Indian economy has been growing at a rapid pace since the middle 1980s; market-oriented reforms after 1991 increased this rate despite several gaps. There was a slight deceleration in the late 1990s – due to reform resistance – but there has been a remarkable pick up of late. As of this writing, India is now among the fastest-growing economies in the world and could grow even more, provided some overly regulated markets are liberalized, and subsidies and public deficits are successfully contained. This would also increase the labor intensity of growth and support export dynamism.

2.7. Sustainability

Extremely low expenses for health and education affects social sustainability of Indian development. This also applies for research and development, operation and maintenance, and expenses for upgrading the physical infrastructure. In addition, social expenditures are biased toward the tertiary sector (elite institutions and universities, urban specialist hospitals).

The quality of the environment leaves much to be desired and is deteriorating. The economic costs of environmental degradation are considerable; according to World Bank estimates, costs are between 6% and 8% of the GDP. This is mainly due to unsafe water, air pollution and soil degradation. Most victims of this environmental degradation are the poor. There is no lack of either specific laws or ecological movements to keep the environment safe. In this respect, more activism has recently been acknowledged. Adequate funding for environmental programs, inspection and monitoring of progress (or breaches of legal stipulations) and sanctions for infringement are missing from the equation. The total area of natural parks did increase, however, and a new forest policy was implemented. In addition, emission levels for enterprises have been reduced and courts have become more proactive in prosecuting polluters. An effort was also made to replace diesel with natural gas engines in automobiles.

3. Management

3.1. Level of difficulty

Difficulties with regard to democratic consolidation in India are not severe. This is a result of the long tradition of popular participation, the deep roots of democratic institutions, the missing veto power of other political actors and the balancing influence of multi-positional social, regional and religious conflict lines. On the other hand, the majority parties heading the government faced the difficult task of holding a coalition of minor parties together and furthering the diverging interests of rather small constituencies without much regard to the common good. The Hindu national BJP had to balance the often-aggressively formulated objectives of its front organizations (Rashtriya Swayamsevak Sangh or RSS, Vishva Hindu Parishad or VHP) for cutting to size the minority communities (by demanding a universal civil code, dismantling the autonomy of Kashmir, replacing Mosques with Hindu temples, etcetera) and the interests of its alliance partners to safeguard the federal setup and secular basis of the state. In return, the new Congress-led government was under pressure from its partners on the left to revise the market-friendly economic policy of the prime minister and his team, to decelerate privatization and increase spending for social programs without dismantling subsidies or aggressively lowering the public deficit. State governments with far-reaching efforts to improve governance where often voted

out of office. Compared to moderate difficulties on a general level, problems at the implementation level were significant.

Profile of the Political System

Regime type:	<i>Democracy</i>	Constraints to executive authority:	5
System of government:	<i>Parliamentary</i>	Electoral system disproportionality:	3.3
		Latest parliamentary election:	13.05.2004
		Effective number of parties:	4.8
Head of State:	<i>Abdul Kalam</i>		
1. Head of Government:	<i>Atal Bihari Vajpayee</i>	Cabinet duration:	03/98-05/04
2. Head of Government:	<i>Manmohan Singh</i>	Cabinet duration:	05/04-present
Type of government:	<i>coalition majority</i>	Parties in government:	12
		Number of ministries:	40
		Number of ministers:	37
<p>Source: BTI team, based upon information by country analysts, situation in July 2005. Constraints to executive authority (1-6 max.) measures the institutional constraints posed by a federal or decentralized state, a second parliamentary chamber, referenda, constitutional and judicial review and the rigidity of the constitution. Electoral disproportionality (Gallagher index) reflects the extent to which electoral rules are majoritarian (high values) or proportional: $\sqrt{\frac{1}{2} \sum (v_i - p_i)^2}$; v_i is the share of votes gained by party i; p_i is the share of parliamentary mandates controlled by party i. Effective number of parties denotes the number of parties represented in the legislature, taking into consideration their relative weight (Laakso/Taagepera index) = $1 / (\sum p_i^2)$; p_i is the share of parliamentary mandates controlled by party i. Number of ministries/ ministers denotes the situation on 1 January 2005.</p>			

3.2. Steering capability

In the face of these difficulties the government led by the BJP, as well as its successor, showed remarkable capability to steer the country through difficult waters. The BJP had to placate its radical followers by verbally supporting their claims (for instance, in questions of religious identity), delaying any final and necessarily polarizing solution. However, this proof of steering capability occurred sometimes by default, namely through coalition partners' pressure on the BJP to follow a more neutral course in questions of identity politics. This was also related to the volatile path of electoral outcomes at the state level.

The National Democratic Alliance's economic policies were more straightforward. Privatization was pursued more aggressively (against opposition in the coalition), measures to rein in the massive public deficit were enacted (albeit not imposing hard sanctions against state deficits) and big infrastructural schemes (construction of highways) were launched. The government was, however, unable to introduce a universal valued added tax against opposition in its own ranks.

The succeeding Congress-led government was less constrained to follow a secular, balanced political course and did indeed grasp the opportunity. The economic policies of the new government were more ambivalent and included the continuation of market-oriented reforms by giving them a human face (priority for agriculture, social services, employment guarantee program, etcetera) without

mobilizing adequate resources (although the Fiscal Responsibility Act was renewed), and by decelerating privatization, increasing defense expenses and continuing subsidies. Liberalization of foreign investments was done only cautiously, due to resistance by leftist partners.

3.3. Resource efficiency

At the time of this writing, the government continues to use the available financial and personnel resources for the transformation project inefficiently. The budget deficit of the central and state units is still well above 10% (not including shadow budgets, guarantees, and so forth). It is absorbing a big share of savings, crowding out private investment and lowering public investments to a level that does not guarantee capital replacement. The deficit is largely due to massive, partly unproductive and poorly targeted subsidies (for energy, water, fertilizer, food and oil), and increased defense outlays and capital service. The state's tax income suffers from the nearly complete tax exemption of agriculture and the informal sector, from cuts in income and corporate taxes and delays in introducing a full-fledged value added tax. The management of public expenses suffers from poor monitoring, alienation and poor targeting. Earmarking for operation and maintenance of facilities is far too low, contingent liabilities (for pensions and guaranteed) are not adequately dealt with and budget forecasts are often too optimistic. The renewed Fiscal Responsibility Act aims to do away with public deficits until the year 2008 through better tax administration, introduction the value-added tax, limiting state guarantees for credits and ending deficit financing through the central bank.

3.4. Consensus-building

Democratic procedures and principles are not questioned by any important political party or group. This does not mean, however, that the details of political tolerance toward minorities or in relation to the cultural identity of the state or the pace of economic reforms are universally agreed in India. In cultural matters, the BJP-led government tried to steer a moderate Hindu nationalist course by rhetorically backing the position of their more radical followers. At the same time, they tried their alliance partners by excluding offensive items from the government program and by leaving the solution of difficult questions with the courts, civil mediators or the legislature (where consent of the opposition was necessary). Blame for a lack of performance could so be laid on others. The National Democratic Alliance had fewer problems forming a consensus on a more constructive dialogue with Pakistan, as its nationalist credentials were not in question. It did indeed exploit this opportunity skillfully. Consensus-building efforts of the new Congress-led government were successful in the treatment of secessionist movements in northeastern India and Kashmir (supported by massive

financial assistance for the concerned regions) and in carefully continuing the market-friendly course by simultaneously giving in to leftist partners on minor questions, namely the precise level of foreign participation in several sectors of the economy.

3.5 International cooperation

International development cooperation has only a very limited part in the initiation, implementation and financing of market reforms or in the pursuance of the democratic progress. The Indian government intends to do without foreign aid in the future (also with regard to the handling of natural disasters) and it is cultivating a self-confident posture in contact with donors. That does not mean that the union or state governments are not cooperative. Quite a few union territories initiated far-reaching reforms in the educational, health and infrastructural sector or in regard to the overall approach of market-friendly reforms, supported by international organizations. In principle however, there is no chance for a political dialogue dictated unilaterally. Liberalization and regulation of foreign direct investment is also more done with an eye to the local constituencies (and therefore hesitantly) than to foreign partners, although the necessity to attract more foreign investment is acknowledged by governments of all political shades. The government is also following, after the disastrous experience of the early 1990s, a cautious policy of incurring foreign debt, building up massive international reserves as a cushion against financial risks. The government tried to become a reliable partner in the combat of international terrorism, thereby naturally also pursuing own interests concerning the condemnation of Pakistan-sponsored terrorist groups.

4. Trend of development

	2000	2001	2002	2003	2004 (a)
Growth of GDP in %	4.4 ¹	5.8 ¹	4.6	8.0	7.7
Export growth in %	12.2	21.7	2.7	14.0	n.a.
Import growth in %	11.0	2.2	0.2	8.8	n.a.
Inflation in % (CPI)	3.8	3.7	4.3	3.9	4.7
Investment in % of GDP	23.9	23.4	22.8	23.8	n.a.
Tax Revenue in % of GDP	7.5	8.1	8.1	8.4	n.a.
Unemployment in %	n.a.	11.1	11.1	11.0	10.9
Budget deficit in % of GDP	-5.2	-5.7	-5.9	-5.7	-5.7
Current account balance in billion \$	-4.7	-3.6	0.8	3.7	n.a.

(a) Provisional estimates for 2004 are based on information available up to October 2004.

Source: IMF: Statistical Appendix India. 2003. Internet: <http://www.imf.org>; German Asia-Pacific Business Association: *Wirtschaftshandbuch Asien-Pazifik 2004/05*. Hamburg. 2004; Government of India: *Union Budget & Economic Survey 2003-2004*. Internet: <http://indiabudget.nic.in>

4.1. Democratic development

The relatively good ranking of India in terms of the state monopoly on the use of force, efficiency of the administration, independence of its judiciary and high esteem of democratic procedures did not diminish in the period from 2003 to 2004. This was partly by default, as the main party of the coalition governing until the early summer of 2004 was unable to carry through a less secular agenda against the resistance of its smaller minority partners. Controversial projects such as the elaboration of a universal civil code (harming Muslims), rewriting history textbooks and the “Hindu-ization” of education, ban of cow slaughter and conversion, revision of the constitution and so forth had to be stalled. The government often was slow or unwilling to combat Hindu chauvinism, but in general kept a balanced stand and focused its energy on maintaining adequate governance and continuing economic reforms.

Misinterpreting the popular mood, the government led by the BJP called for early elections. The victory of the Congress-led new alliance in 2004 was completely unexpected; it was a kind of vengeance brought about by sections of the population left out by progress (the poor and farmers) and people uncomfortable with policies of communal agitation. Above all it was the result of effective alliance building by the Congress Party and the success of this alliance in some union territories, whereas the old coalition was left behind by some of its adherents.

New prime minister became Manmohan Singh, the architect of India’s economic reforms. He was supported by a liberal team, but curbed in activism by market-skeptic coalition partners and the outside support of the communists. The Common Minimum Program of the new coalition sought to bring about social harmony, the return to genuine secularism and labor-intensive growth. There were some efforts by the BJP to stop the political process after the defeat by obstructing parliamentary proceedings. More troublesome were attempts of the leftist coalition partners to undermine progress in economic reforms (privatization, liberalization of foreign investments, engagement of foreign experts, reform of the Provident Fund) by veiled threats to break with the government, which became more secure after the first batch of election victories in union territories.

4.2. Market economy development

Economically, the period of 2003 to 2004 was a near unmitigated success. Growth climbed to East Asian rates in every sector (supported by good monsoons) and bullish export growth (especially in services). Growing remittances and foreign investment brought a further strengthening of the balance of payments position bringing about a massive accumulation of foreign exchange reserves (sufficient for the import of one and a half years). These had to be sterilized by the Reserve

Bank to subdue inflationary pressures (remaining moderate) and the appreciation of the currency. The traditional weak spots of economic development did remain: massive budgetary deficits, unreliable and inadequate power supply, congestion of roads and ports and above all the accentuation of disparities between leading and lagging states as well as a near jobless growth.

D. Strategic perspective

It is the aim of the Indian government to convert the country to the status of a developed economy by 2020 and correspondingly to a major player on the global scene. The chances for reaching these aims are not bad. Supported by wide-ranging reforms, India has experienced rapid growth over the past decade and the external position has improved dramatically. The rapid growth of information technology service exports and high remittances have resulted in considerable current account surpluses. Together with increasing (albeit modest) capital inflows, this has generated a substantial increase in external reserves. Low levels of short-term external debt give the country a cushion against speculative attacks.

In parallel with faster growth, India has made progress in reducing income poverty and on many other social indicators. However, the performance has been uneven: average income remains low and there has been little movement on some critical social indicators. There also remains a substantial disparity of opportunity, particularly in the education, health and economic prospects of vulnerable groups. A growing gulf has emerged between the richer and poorer states within the country, resulting in a growing geographic concentration of poverty.

A strategic shift is necessary to ensure that the fruits of growth are shared more evenly. The people-friendly program of the new Indian government is therefore heading in the right direction; this should be complemented by fiscal restraint, efforts to broaden the tax net and rebalancing of expenditures (by cutting unproductive subsidies) to make room for the rehabilitation of infrastructure, basic services, support of agriculture and maintenance. Sustaining past growth will also require dramatic improvements in basic infrastructure and the investment climate. Major changes will need to be made to ensure effective delivery of basic services to all citizens. A long-term strategic challenge is to ensure environmental sustainability in the context of diminishing water availability and increasing pollution.

The democratic credentials of the country are not in doubt but could be improved by stricter observance of the federal setup and efforts to clear the massive backlog of litigations in the courts. The judicial system and the election committee have followed a pro-active course in prosecuting malpractices. This should be encouraged because it will restrain corruption in general together with better transparency of governmental procedures (supported by freedom of information

acts). Policies of reasonable accommodation of truly locally based rebel groups (in the Northeast) should be encouraged by the international community, and efforts of foreign sponsored terrorist groups in Kashmir to destabilize peace efforts should be unequivocally condemned as well as the prosecution of minorities (Christians, Muslims, and other groups) by Hindu radicals.