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Nehru's economic policy was not wrong our narrative about it is

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To create more jobs and promote growth, we need to learn from our first prime minister.

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The dominant narrative in India today has condemned Nehru as an amateur in economic policy. Neoliberal Indian economists in Ivy Leagues and those in India influenced by them claim that the country skipped a big chance to play catch-up to the rich West because of Nehru's fatal flirtation with socialism. This infatuation, they insist, put clamps on the animal spirits of India's private enterprise, withdrew the country from the benefits of world trade and plagued it with inefficient and corrupt public sector undertakings for decades.

Even Nehru's supporters – while admiring his insistence on a “scientific temper” and industrialisation – grudgingly acknowledge his economic policy mistakes. Nehru, writes Ramchandra Guha, “at once an Indian Brahmin, an English aristocrat and a European social democrat” naturally despised moneymaking, and hence the profit motive that usually drives private enterprise.

It follows from this narrative that India was finally free once the 1991 reforms were enacted to drastically cut the regulatory framework and substantially liberalise international trade of capital and goods. Besides inspiring a spate of books about “India Rising”, the watershed year of 1991 has not only reduced the complicated Indian economic history to a pre-1991 “socialistic” and post-1991 “free-market” phase in the popular mind, but it underpins the editorials of practically every financial newspaper clamouring the new government for more “structural reforms”.

Building industries

But what exactly was the Nehruvian consensus? Colonialism had equipped India with modernity by fully monetising its economy and building a centralised state that allowed the smooth movement of goods and capital. However, it had used these very instruments to keep India a largely agricultural economy. Excessive free trade made manufacturing in India uncompetitive and the capital markets were dominated by metropolitan capital that was not very hospitable to Indian interests. Whatever little manufacturing India had originated during the brief protectionist phase of World War I. This laissez faire India – the India many of our commentariat clamour for – was responsible for the less than 1% annual growth.

This was the baggage borne by Nehru and the other founding fathers at the time of independence. The Nehruvian economic strategy, therefore, was to pursue an artificial increase in total investment, micromanage that investment through extensive economic planning and licensing of private enterprise, pursue high tariffs for the protection of such industry, and boost infrastructural investment and land reforms for agricultural production. Much of this was enacted improperly. Land reforms, in particular, suffered as they were to be implemented by the state governments, who often depended on the vote banks of the very landlords they were trying to target.

But did this strategy succeed in building an industrial base? Definitely. The average economic growth rate increased to more than 3% in the 1947-1965 period, and India grew a substantial industrial base. However, the growth rate remained low in comparison to the growth of East Asian economies. This dichotomy is often held as an example of free market success versus statist failure.

State support

However, contrary to conventional wisdom, most of the successful East Asian tigers – Japan, Korea and Taiwan – pursued extensive state intervention to boost their economies. Import substitution was the norm, while state subsidies to industries on the basis of exports were encouraged.

For instance, entrepreneur Chung Ju Yung, with no background in car-making, created Hyundai Motors Company in the 1960s. Korea's enlightened despot, Park Hee, understood the need for a strong domestic industrial base. So, Hyundai Motors became a target for cheap credit, state subsidies and a protected domestic market – everything that neoliberals tend to despise. Yet, it was protection that allowed Hyundai to fail, learn and eventually flourish. If Korea had to follow its “comparative advantage”, it would still be selling the world textiles and fish than cars and steel.

Similar collusion between the state and capital has powered the Chinese growth. Academics **Usha** and George **Haley**, in their works of scholarship, have shown that state subsidies, preferential financing and intervention have been central to making China the largest maker of steel, and increasingly the largest maker of solar panels.

Competitive drive

Then what went wrong with India? The cause lies in Nehru's unwillingness to push the domestic capitalist class to do the hard task of building an industrial base by laying all the burden on the public sector, and the refusal to base industrialisation on foreign markets and technology. Japan, Taiwan and Korea, like India, bankrolled their infant industries, but, unlike India, almost always subjected them to an extremely strict export discipline. This way their companies would be subjected to the highest competition, while using the home base to consistently learn and grow.

The legendary MITI (Ministry of International Trade and Industry) in Japan had substantial control over the distribution of foreign exchange earnings and would allocate it to firms on the basis of export performance. Korea's Park Hee would jail leaders of chaebol (a form of conglomerate) if they did not do the hard task of running factories as opposed to easier sectors like retail, trading or construction.

Therefore, Nehru was not at fault in pursuing state intervention in principle. Rather his mistake lay in getting state intervention wrong. Relying excessively on the domestic market for the growth of infant industries would make domestic industrialists lazy, whereas undue licensing and reservation of key sectors for the state killed the important drive that comes from the profit motive. Shunning exports would mean that domestic demand had to be maintained at the cost of investment. However, the pursuit of heavy industries, five-year plans and import substitution was something that virtually every nation playing catch-up to the West had to do.

Our wrong reading

Unfortunately, the reading of Nehruvian years in the popular mind today is largely erroneous. It is considered synonymous with stagnation and incorrect policy choices. If Nehru got state intervention wrong, then probably the idea of state intervention is wrong (or so goes the narrative). Labour regulation, rather the absence of scale, technology, skills and trade protection, is blamed for the alarming absence of manufacturing in India. And almost every call for “reforms” by pundits at home and abroad is a cry for further deregulation, privatisation and liberalisation.

On his 125th birth anniversary, India must learn the correct lessons from history. With a severely uncompetitive manufacturing base and a growth built on services, credit booms and bouts of hot money (which leave as rapidly as they come) – perhaps India would do well with some measure of Nehruvian planning, statism and protectionism, if it is to chart a course of plentiful jobs and sustainable growth.

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