

Chapter 4

NEHRU'S DANGEROUS GAMBLE

NANGAL (Punjab), July 8, 1954. The foaming waters of the Sutlej gushed forth into the Nangal hydel channel and the Bhakra canals as the Prime Minister, Mr. Nehru, pressed an electric button to inaugurate the world's biggest canal network here today. An estimated 100,000 persons cheered lustily when he declared at a solemn ceremony: "I dedicate the Bhakra-Nangal works to the good of the Indian people." Thousands of balloons were released and crackers were fired by enthusiastic villages as the black sluice gates on the hydel channel rose. Flying low over the site, Indian Air Force planes dipped in salute.¹

The Bhakra-Nangal hydroelectric project was close to Nehru's heart. For several years, while its construction was ongoing, he often went to the project area to review the progress. Once, Nehru became upset when he heard "damage had been done to one of the Bhakra canals." He wrote an agitated letter to Bhimsen Sachar, Punjab's chief minister, complaining the engineers in charge had failed to inform his office of this damage. He was especially upset by the cheeky engineer who questioned Nehru's need to know every construction detail.²

But on that beautiful day, after the Sutlej waters flowed into the canals and Indian air force planes saluted the achievement, Nehru said "a certain exhilaration and excitement" filled his "heart and mind." His government,

he said, had given priority to “big projects” like Bhakra-Nangal (where, eventually, dams would go over the Sutlej at sites in Bhakra and Nangal) and to similar multipurpose irrigation and electricity-generation projects in the Damodar Valley (in the present states of Jharkhand and West Bengal) and at Hirakud (on the Mahanadi River in Orissa). These projects, he emphasized, would generate electricity to run “big factories.” Nehru spoke of other achievements: the “magnificent” fertilizer factory at Sindri, the “big railway engines” produced at the Chittaranjan Locomotive Works located in West Bengal. He spoke of airplanes and oceangoing ships being built throughout the country. Although Bhakra-Nangal was, for him, “the greatest of these big works,” they were all “the temples of today,” he said. They were the new “places of worship.” Honoring them was a “sacred task.”³

Nehru’s “temples” strategy was congenial to his preference for staying above complex administrative and political fray. In comparison with the business of raising agricultural productivity and stimulating labor absorbing industries in urban areas, the temples approach to development had fewer moving parts, and Nehru needed to deal mainly with science and technology experts, many of whom were his peers and friends.⁴

There was a plausible logic to using science to modernize India. India had been on the sidelines of global scientific and technological achievements. Nehru’s temples used advanced science and technology to accelerate economic development. “Ours is the urgent way,” Nehru said at the opening of the National Metallurgical Laboratory in Jamshedpur in November 1950. “I want to tell the scientists assembled here that the burden of today is a great burden.”⁵

Science offered endless possibilities, but it also introduced great risks—particularly as the stakes grew. Contemporaries warned that large dams would silt up, upset regional ecosystems, and inflict severe costs on the villagers they displaced. Among them was Mira Ben (Madeleine Slade, born a British citizen), who had devoted her life to Gandhi and his causes. She wrote in 1949, “We have got to study Nature’s balance, and develop our lives within her laws if we are to survive as a physically healthy and morally decent species.”⁶ She and others were particularly concerned about the displacement of tribal and other forest-based communities,

who had worked the land for generations and operated within its ecological rhythms.

The warnings bore out. As India built hundreds of dams in the cause of modernization, displaced villagers then and later never received fair compensation. The dams caused great damage to the environment around them and silted up much more quickly than anticipated (on account of the accumulation of industrial wastes and deforestation). As the dams silted up, their ability to control floods declined and their lifespans shortened. Irrigation waters caused waterlogging and salination of the land, undermining potential productivity gains and leaving large tracts of the country drought prone.⁷ While farmers certainly needed more irrigation waters, there was ultimately no substitute for better seeds and productivity enhancement through superior water management, soil conservation, and crop-cultivation techniques such as Japanese farmers had practiced without the irrigation waters of huge dams.

In this chapter, I describe Nehru's temples strategy as it moved to ever higher stakes, from science and technology laboratories, to developing the new city of Chandigarh, to its culmination in the promotion of heavy industry with consequences that would echo for decades after.

The Laboratories: The Small Stakes

On January 4, 1947, several months before independence, when he was still the *de facto* prime minister as vice president in the Viceroy's Executive Council, Nehru inaugurated the flagship National Physical Laboratory in Pusa, then on the outskirts of Delhi. In April 1947, when the prime minister of the state of Bombay laid the foundation stone of the National Chemical Laboratory, Nehru sent his message to be read during the formal proceedings. In his message, Nehru called on Indian scientists to weld themselves into a "band of selfless workers" dedicated to freeing millions of Indians from "material, economic, and social bondage."⁸

Nehru had taken a degree in the natural sciences from the University of Cambridge, and science fascinated him. In August 1947, ten days after India achieved independence and while the "orgy of Hindu-Muslim" violence was raging in Punjab, he squeezed in time to chair a meeting of

the Council of Scientific and Industrial Research (CSIR). This was the umbrella organization under which the various research institutes fell. Nehru would remain the president of the CSIR from 1947 to 1964, his entire tenure as prime minister.⁹ He traveled across the country, laying foundation stones or delivering inauguration addresses at new institutes and laboratories, including one for paleobotany (the study of fossil plants) in Lucknow, the first of its kind anywhere in the world.

The ceremony of laying foundation stones and inaugurating the institutes allowed Nehru to declare a job well done, but his hope that the institutes would harness science and technology in the service of Indians was never realistic. There was a fundamental disconnect. The institutes functioned as elitist islands of excellence. Economic development requires resolution of social conflicts and efficient administration of multifaceted and messy tasks. Nehru was comfortable in the elite world, not in the messy one.

Nehru revealed his elitist approach to development in an unguarded moment in early 1947, when he said he wanted Indian scientists to work in “the Brahminic spirit of service.” He recognized quickly that singling out the Brahmin caste—sitting on top of India’s caste hierarchy—might be an endorsement of inherited superiority and privilege. He then backtracked, clarifying that “the Brahminic spirit” was “something entirely apart from the Brahmins” and referred only to “service and learning.” However, he kept revealing his affinity to the best and brightest. Only a few individuals could produce high-quality science, he said; larger numbers inevitably led to “mediocrity.”¹⁰ Thus, Nehru relied on Shanti Swaroop Bhatnagar, an eminent industrial chemist and first director general of the CSIR, and on Homi Bhabha, nuclear physicist and global leader in the advancing widespread use of atomic energy. Nehru was friends with the Indian physicist and Nobel laureate C. V. Raman and with the one and only Albert Einstein.

In a low-key development on May 29, 1951, an advertisement in Indian newspapers announced an “Indian Institute of Technology” (IIT) to be established in Kharagpur in the state of West Bengal. The new institute would admit all high school students who had studied mathematics, physics, and chemistry, with classes beginning in July. In its first batch, IIT

Kharagpur admitted 210 students, with a plan to grow the student body to 1,320 in five years. Four other IITs, distributed across the country, would follow in the next decade.¹¹

Although the research laboratories and especially the IITs rightfully added to Nehru's aura, their benefits to India were limited. Given their elitist premise, their distance from the nation's economic and social problems remained large. In addition, their isolation from the existing educational system restricted the benefits to the chosen ones. The astrophysicist Meghnad Saha protested at the time that the new science and technology institutes might absorb the best-prepared students, attract the most distinguished teachers, and receive the bulk of the funds, leaving the broader university network to languish.¹²

As Saha had warned, an educational cocoon did emerge. Rich Indians and senior civil servants sent their children to privileged private high schools, whence they either traveled abroad for university or launched into elite liberal arts colleges, the IITs, and the best medical colleges. From there they joined the civil services, found scarce high-paying private-sector jobs, or went abroad to work.

Millions of potential Indian geniuses remained undiscovered, as even the best Indian universities—including those at Allahabad, Bombay, Calcutta, and Madras—struggled to maintain scholarship and educational standards. The most egregious example was Allahabad University, which unraveled from the “Oxford of the East” into a shambolic mess due to a severe lack of funds.

Today, Allahabad University barely educates many of its students, for whom it serves primarily as a degree certification center. Students live in the university's hostels to attend coaching centers in the city, which prepare tens of thousands like them for exams that help select handfuls for a “dream government job.”¹³ Put simply, for every IIT graduate who shines brightly in California's Silicon Valley, thousands of poorly educated Indians with graduation certificates stand in the tortuously long queue for government jobs.

Most seriously, adulation of the temples strategy obscured the necessity for mass primary education. The priority in Meiji Japan, strikingly, was the opposite. During the first thirty years after the Meiji Restoration,

the Japanese government focused on making primary education widely available. When they approached that goal toward the end of the nineteenth century, Japan had one (yes, one) university. Only over the first two decades of the twentieth century, as Japan achieved universal primary and secondary education, did the number of Japanese universities increase.¹⁴

Raising the Bet: Chandigarh

In 1959, University of Chicago economist and sociologist Bert Hoselitz described Indian cities as “parasitic” rather than “generative.” Most urban residents worked in dead-end jobs, commonly as “casual labor” with no certainty when they might work next, or as “self-employed” shopkeepers and vendors, idle for much of the day. Hoselitz noted that the cities were populated by an excess of young men and hence often lacked the stability of families and communities. “Ill-health, crime, prostitution, and illiteracy” were common. Writing about Calcutta a few years later, anthropologist Nirmal Kumar Bose also highlighted the excess of “lone men” who lived “without the barest minimum of housing, sanitation, comfort, and privacy.” India’s unanchored urban population hampered the community cohesion required for a healthy urban life.¹⁵

An unexpected opportunity to build a new city attracted Nehru. The Indian state of Punjab required a new capital, having lost its glamorous capital Lahore to the part of pre-partition Punjab incorporated into Pakistan. Hindu and Sikh refugees fleeing from Pakistan also needed new urban homes. For Nehru, Punjab’s new capital city offered an opportunity to create a model of urban development.

The site for the new capital, Chandigarh, had fertile agricultural land “dotted with groves of mango trees, spread over seventeen villages.” Its pristine setting fit perfectly with Nehru’s temples strategy. As he said, “The site chosen is free from the existing encumbrances of old towns and old traditions. Let it be the first expression of our creative genius flowering on newly earned freedom.”¹⁶ That was key: “free of the existing encumbrances.” Who then would deal with those encumbrances?

Nehru chose Swiss-born French architect Charles-Édouard Jeanneret (better known as Le Corbusier) to plan and design the new city. Nehru

saw in Le Corbusier a “modern-day prophet of the Second Industrial Age,” who could usher Indian cities into the international vanguard of urban development. He developed a close personal relationship with Le Corbusier, just as he had with the scientists Shanti Swaroop Bhatnagar and Homi Bhabha. Nehru almost always intervened in Le Corbusier’s favor whenever he had to battle the Punjab government.¹⁷

Le Corbusier visualized Chandigarh “constructed on the principles of a garden city, with ‘no heavy or obnoxious industries.’” He mixed mystical spirituality—symbolized by the open-hand monument to receive and distribute newly created wealth—with a futuristic view in the Museum of Knowledge, home to a “modern-day video arcade.”¹⁸ It was a grand vision.

Chandigarh’s wide boulevards and elegant cubes and rectangles have made it one of India’s more livable cities. Yet Chandigarh could not escape the social and demographic pressures that caused other Indian cities to turn parasitic. Slums appeared on the city’s periphery and unauthorized commercial construction and street vendors took root in various neighborhoods. Unhygienic uses of low-income housing became common, as dwellings meant for one family often housed a family in each room.¹⁹

The idea that Chandigarh would provide a model for Indian urbanization proved fanciful. India urgently needed to breathe new life into its old cities, with all their encumbrances. In 1960, the World Bank wrote, in somewhat stark language: “one of the most dangerous weaknesses of [Indian planning] is the continued neglect of problems of urban development in Calcutta.” Having been part of the international bureaucracy myself for a quarter century, it seems to me a miracle that the phrase “dangerous weaknesses” survived multiple rounds of internal document review, with each round designed to soften the words and blur the message. The city of Calcutta, the World Bank continued, was impeding economic growth in a crucial industrial region. As the World Bank explained, Calcutta was not serving the needs of its own population or of its economic hinterland:

Overcrowding, degradation of housing, health hazards, primitive water supplies, lack of space for new industries, traffic bottlenecks, power shortage, a still unsolved refugee problem—all are increasing the cost

of moving goods and providing the many services that a growing industrial region demands of its metropolis. . . . Nor is there any alternative to Calcutta as a port, financial and administrative center and major market for the heavy and light industries that should develop, and are in fact developing, on the basis of the coal/steel complex in West Bengal, Bihar, and adjoining areas of Madhya Pradesh and Orissa.²⁰

This seems to be the earliest statement on the crucial importance of cities to India's economic development. In agreement with the World Bank report, the anthropologist Nirmal Kumar Bose described Calcutta as a "premature metropolis." In population and physical area, Calcutta was about the size of the world's great metropolises such as London and New York. But Calcutta served neither the social nor economic function of a metropolis.²¹

Urban development was not one single objective achieved in a single project, as Jane Jacobs explained. Indian cities needed multiple forms of infrastructure, including housing and local community amenities. Coordination of these many efforts made urban development much more complex than building standalone "temples of new India." With the passage of time, urban development became harder as local politicians staked out territories within the cities, armed with henchmen to intimidate and even "eliminate" those they viewed as competitors.²²

Across the country, Bombay, the capital of the western state of Maharashtra, was also a premature metropolis. In 1963, the acclaimed writer-moviemaker Khwaja Ahmad Abbas, famous for portraying the Bengal famine in *Dharti ke lal*, told a story about life in Bombay. In this new film, *Shahar aur Sapna* (The city and the dream), a young couple meet when forced to take refuge in a drainpipe; once they marry, they share a dream (or rather, a nightmare) of bringing up their first child in that drainpipe. Tensions ran high in Bombay for the same reason as in Calcutta: the scarcity of essential resources and the lack of jobs.

Bombay had its unique features. The prohibition of alcohol in 1952 created a profitable illicit liquor trade. Also profitable was the smuggling of gold and watches, and Philips transistors were always in demand for

piped-in film music and live cricket commentary. From small beginnings, criminal activity quickly spread. Varadarajan Muniswami Mudaliar, who started with the liquor trade, became overlord of the Dharavi slum, where he allocated land to migrants and used his clout with the local administration to get residents ration cards and illegal electricity and water connections. Haji Mastan had a flourishing smuggling business. Karim Lala specialized in the eviction of tenants and leaseholders. From the docks through the slums and streets, musclemen dotted the city. They became the *dadas*, local goons who acted as intermediaries between the people and a corrupt bureaucracy and as arbiters in private disputes.²³

Neglect of Bombay continued. A 1971 World Bank report detailed Bombay's need for more and better transport, investment in public utilities, and better land-use and housing policies. The report emphasized that Bombay needed an administrative institution to "represent the interests of the whole region," a body with "real power" and fiscal authority.²⁴

At the opposite end of large metropolises, University of Chicago economist Milton Friedman made the case for small cities that would serve as the locations of industrial clusters, in much the same way as economist Alfred Marshall had advocated in the early twentieth century. During a 1963 visit to India, Friedman was exhilarated by his tour of Ludhiana, the medium-sized town in Punjab. An entrepreneurial energy infused "the thousands of small and medium size workshops, with [their] extraordinarily detailed specialization of function." Known primarily for its knitted goods, Friedman saw in Ludhiana "a major centre for the production of machine tools, bicycles, sewing machines, and similar items."²⁵

The all-hands-on-deck approach needed for energizing Indian cities and industrial clusters did not blend with Nehru's personality. He continued his passionate rhetoric while avoiding development tasks that required summoning the collective energies of Indians. He focused on new science and technology institutes, rather than strengthening existing universities or, even more important, building a strong base of mass education. He lavished attention on building a new city—Chandigarh—rather than reinvigorating the existing cities that were falling apart.²⁶

That same temples strategy bet India's future on heavy industrialization.

The Big Bet: The Second Five-Year Plan

In the years of the First Five-Year Plan, 1951 to 1956, India's per capita GDP, the average income per person, grew by 1.8 percent annually. This was a performance to celebrate after near stagnation—GDP per capita growth of 0.1 percent a year—in the half century before independence.²⁷ Nehru, however, misjudged India's post-independence achievement, particularly in agriculture. With the exception of the drought of 1950–1951, the rain gods had cooperated. Nehru read that good luck as: “We have achieved considerable measure of success in agriculture and food production.” And although the Community Development Program and the associated technical extension services, initiated in October 1952, had failed utterly, Nehru believed that the effort had been a success. He was better aware of the land reform failures, recognizing that the *zamindari* and other reforms had not achieved more equal landholding. He understood that “many loopholes” in the reform legislation and “great deal of evasion” had allowed the vast rural inequalities in income and wealth to persist. But knowing not what else to do, he gave up on the cause of agricultural development and decided it was best to move on.²⁸

“The time had come,” Nehru said, “to advance rapidly on the industrial front.” He emphasized that the “urgent necessity for us to industrialize as rapidly as possible” meant “the development of heavy industries which would lay the foundations for future growth.”²⁹

What explains Nehru's fascination—indeed, obsession—with heavy industrialization? The most consistent reading of Nehru—when seen in combination with his championing of large-scale dams, scientific laboratories, advanced engineering and medical institutes, and the city of Chandigarh—is that, as Nehru himself put it, he was building the temples of modern India. Nehru could direct such activity with the help of a small number of gifted Indians while remaining distant from the rough and tumble of grassroots mobilization of people and resources.

A commonly held but lazy view says Nehru's “Fabian socialism” led him to public sector–driven heavy industrialization. Was Nehru a Fabian socialist? How, for example, did he match up with Clement Attlee who, as Britain's first postwar prime minister from 1945 to 1951, was historically

the most important practitioner of Fabian socialism? Attlee nationalized coal mining, the iron and steel industries, and public services, including the railways, electric power, and gas supply. These nationalizations come closest to Nehru's reliance on the public sector to accelerate industrialization. But Nehru was his own man. His nationalization included fertilizer factories and, importantly in his own mind, electrical and non-electrical machinery. In contrast, Nehru stayed away from Attlee's true socialism, powerfully reflected in the United Kingdom's comprehensive National Health Service, free secondary education for all children, and extension of social insurance. These investments in human capital and social security, as historian Jim Tomlinson has written, "marked major changes in British society."³⁰

Nehru thus discarded the socialism of Fabian socialism—healthcare, education, and social security, all of which gave people dignity and the possibility of better futures.

Some suggest that Nehru followed Soviet economic ideas, but that makes even less sense. Large parts of the Indian economy—major chunks of industry and especially agriculture—remained in private hands. And as he did with Fabian socialism, he ignored the Soviet Union's greatest achievement: world-class education and healthcare.

Nehru would have agreed that he was not a socialist. In his own words, socialism meant "equality of opportunity" and provision of basic necessities of life—"food, clothing, houses to live in, healthcare and educational facilities"—to everyone. Whether he was inspired by Fabian socialism, Soviet ideology, or his own professed commitment to equality and fairness, he practiced none of them. As Sujatha Rao, a former health secretary (the Indian government's senior-most health official) writes, "It is inexplicable why Nehru did not pay any attention to education and health."³¹

While a fuller account of Nehru's education policies must wait until chapter 6, Nehru kept up his socialist rhetoric while being self-conscious he was not living up to it. In October 1954, he said in a public speech, "I want to provide education and healthcare facilities for everyone in India as quickly as possible. But it is impossible for us to do." In another speech, this time at the foundation-laying ceremony of a women's college

in Madras in January 1955, he acknowledged that education was of “basic importance” and was essential to ensure the enhanced “productive capacity of the nation.” But, he added, “there are still many things of basic importance to do.” And “obviously, we are struggling against the difficulties of finance.”³² Nehru espoused the cause of socialism but always had reasons for why it was not feasible.

Possibly, Nehru’s commitment to heavy industry reflected the then-popular “big push” industrialization strategy advocated by the economist Paul Rosenstein Rodan. The big push strategy called for large-scale investment in core capital-intensive industrial sectors. The promise was that these critical sectors would stimulate demand for inputs from feeder industries, which would demand more of their own inputs, leading to a cascading ferment of new activity and long-term economic growth. Rosenstein Rodan understood that his big push capital-intensive production would create few jobs. But sacrificing immediate job creation, he argued, would pay off with plentiful future jobs, perhaps even “within a generation.”³³ Big push was the original “trickle-down economics,” well before the term was invented. The promise was that economic outcomes in a privileged sphere would eventually flow through to all.

The big push promise was backed by little evidence. Even if it worked perfectly, could India wait a generation for jobs? And what if it went wrong? V. T. Krishnamachari, vice chairman of the Planning Commission, reported a startling statistic: 50 million peasant households had more workers than they could use productively. The ranks of the educated unemployed were increasing. Population growth was adding two million new job seekers every year.³⁴

Recognizing that heavy industry would not create sufficient jobs for India’s needs, Nehru, in desperation, concluded that the “solution” lay in “village industries,” especially those that produced “basic necessities” using raw materials easily available in rural areas. Village industries were a nod to the Gandhian vision of self-sufficient villages. The hand-spinning wheel, the *charkha*, was intimately associated with Gandhi, who used it both as a symbol of self-sufficiency and as a meditative tool. Many traditional handloom weavers produced coarse cloth; others were brilliant artisans who produced exotic textiles.³⁵

Recognizing, however, the technological obsolescence of the handloom sector, Nehru also feared that reliance on traditional handicrafts might lead to “slavery and starvation for India.” In any event, the highly inefficient village—or “cottage”—industries could not compensate for the overall bias toward heavy industry. Planning Minister Gulzarilal Nanda made it clear that the Second Plan would fall “substantially short” in generating job opportunities. That they nevertheless proceeded with the Second Plan tells us that Nehru and others around him were stuck in an intellectual trap.³⁶

It took an outsider to highlight the policy incongruity. Milton Friedman, during his October 1955 visit to India, which occurred well before he had seen the entrepreneurial energy of Ludhiana's small firms, forcefully criticized Nehru's combination of heavy industry and handicrafts. That combination, he said, “threatens an inefficient use of capital at the one extreme by combining it with too little labor and an inefficient use of labor at the other extreme by combining it with too little capital.” Friedman insisted that “the best use of capital is in general somewhere in between.” India, he explained, must focus on a “a widely diversified and much expanded light industry.”³⁷

Just as he had given up on agricultural development, Nehru gave up on any prospect of rapid industrial employment. However, one hurdle to heavy industrialization remained. India did not have the financial resources to implement the capital-intensive strategy. A fateful conversation Nehru had on Christmas Day in 1954 proved pivotal for the Second Plan and for India's economic future.

Nehru had traveled to the Indian Statistical Institute in Calcutta to meet with the experts Mahalanobis had assembled for advice on the Second Plan. Among the experts was Ragnar Frisch, a Norwegian economist who would share the first Nobel Prize for economics in 1969 in recognition of his contributions to mathematical economics, especially as applied to long-term planning. “I have been to the Indian Statistical Institute today,” Nehru wrote in notes to himself that night. “Professor Frisch was unfortunately unwell and in bed. However, I met him in his bedroom.”³⁸ Two of Frisch's comments excited Nehru. The first proposition was: “techniques were now available for solving almost all the problems that [arise]

in planning.” Nehru liked the assurance. Mathematical techniques could lay out blueprints for economic progress. With the blueprints in hand, social consensus and political compromise were of secondary importance. The second proposition gave Nehru even greater comfort: planning needed to focus on physical production targets, not on financial number-crunching. In his notes, Nehru wrote that he interpreted Frisch as saying that consideration of financial resources “should come in at a later stage when the physical objectives were defined.” Nehru had permission to set his production objectives and worry about their funding later.³⁹

Frisch seduced Nehru. Neither was in touch with reality. Brazil had also fallen victim to the big-push seduction. In July 1954, six months before the Frisch-Nehru meeting, the World Bank wrote that in pursuing too rapid a course of industrialization, Brazil had suffered “severe crises of industrial indigestion.” The “indigestion” caused chronic inflation, wasted investment, and shortage of foreign exchange reserves.⁴⁰

Although Indian policymakers likely did not know the details of Brazil’s problems, they had good reason to worry that attempting too rapid a pace of industrialization could place severe stress on the Indian economy. In December 1955, the governor of the Reserve Bank of India—India’s central bank—warned the Finance Ministry that the Second Plan, by adding enormous new demand, would cause “serious inflationary pressures.” In January 1956, the Reserve Bank’s Board also voiced fears about “so large an investment programme.”⁴¹

Plan implementation began in March 1956, and the World Bank’s wide-ranging critique of the Second Plan arrived a few months later, in August 1956. The World Bank report agreed with India’s need to expand its production of steel, cement, and fertilizers but cautioned that “the scale may be somewhat ambitious.” The report frowned on premature investment in producing heavy electrical and non-electrical machinery, for which it said India lacked both capital and technical skills. Instead, the report recommended more resources for “less complex” goods produced with labor-intensive techniques. Like the Reserve Bank’s Board earlier in the year, the World Bank also came to the “inescapable” conclusion that the plan was “too large.” Particularly worrying were the foreign exchange needs for imports of equipment and raw materials to fulfill the

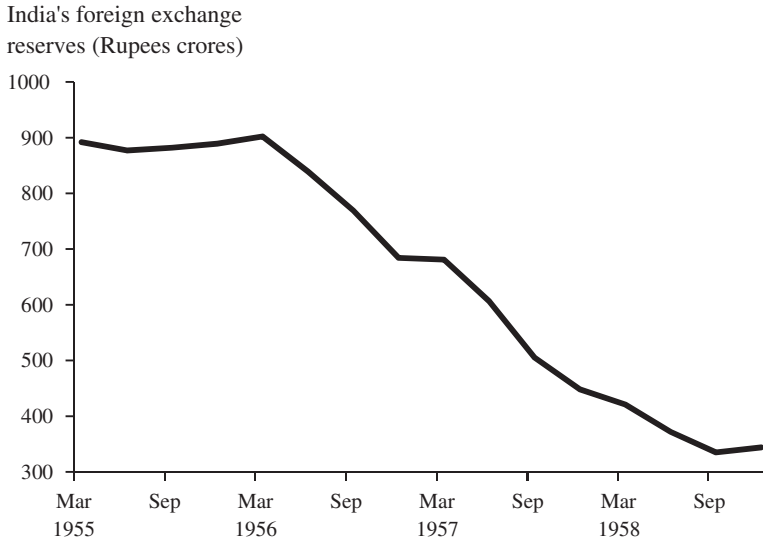


FIGURE 4.1: India's foreign exchange reserves evaporate. (Rupees crores)

Note: 1 crore equals 10 million; exchange rate: 4.76 rupees/dollar.

Source: Balachandran, Gopalan. 1998. *The Reserve Bank of India, 1951–1967*. Delhi: Oxford University Press, Table 14, 693.

plan's targets. World Bank staff added that most Indian officials privately agreed that the plan was not feasible.⁴²

The outcome lived up to these warnings. The Second Plan failed almost as soon as it started. Foreign exchange reserves plummeted from 900 crore rupees (\$1.90 billion) in March 1956 to 680 crores (\$1.40 billion) in March 1957, a decline of \$500 million in one year—with no end in sight (Figure 4.1). The sharp fall in Indian foreign exchange reserves, as the International Monetary Fund made clear, was due preponderantly to a “spurt in investment activities occasioned by the inauguration of the Second Five-Year Plan.” Public-sector companies required huge imports of equipment to meet the ambitious production goals of steel and coal, and for the expansion of railways and electric power. Many public enterprises made multi-year commitments to buy equipment and materials, ensuring that a high level of imports would continue.⁴³

To bolster access to foreign currency, India in early 1957 asked the IMF for \$200 million. The IMF was not happy to receive the request. Its task,

set out at Bretton Woods in the summer of 1944, was to help member countries tide over “temporary” balance of payments problems. Some members of the IMF’s Executive Board protested that India’s problems were not “temporary”; rather, they were the result of an unsustainable long-term development strategy. The Board, however, had little choice—recognizing India’s urgent need, it authorized the \$200 million loan.⁴⁴ Even so, the Second Plan’s steep import requirements and India’s stepped-up food grain imports because of a drought in 1957–1958 continued to drain foreign exchange reserves.

Those who had warned that the plan would aggravate inflation were also proved right. Prices—especially of food grains—rose rapidly. In June 1957, as a Government of India committee reported and the IMF paraphrased, “the rise in investment outlay financed by the [government’s] deficit spending and credit expansion, interacting with a shortfall in food production” caused food prices to spike.⁴⁵

The False Narrative of Socialism Persists

At the Congress Party session (convention) in January 1955, Nehru drafted a resolution calling on the party to work toward “a socialistic pattern of society.” The word “socialistic” gave endless headaches to all who tried to decipher its deep meaning. The *Times of India* remarked that obscure words fit well with Nehru’s “distaste for details and a penchant for soaring well above the earth, if not in the clouds.” When asked how “socialistic” differed from “socialist” or “socialism,” Nehru irritably responded, “As a matter of fact, there is no difference in these words.” The goal, he said, was to give everyone an equal opportunity to improve their standard of living while ensuring that wealth was not heavily concentrated.⁴⁶

The rhetoric of socialism and greater opportunity did not impress the average Indian, who was beginning to see the rot set in. Reflecting the increasing corruption and cynicism in the country, filmmaker Raj Kapoor moved further away from his idealism. His 1956 movie *Jaagte Raho* (Stay awake—stay vigilant) was set at night in a crowded apartment building. Residents aggressively chase away an anonymous peasant when he knocks on their doors, anxiously seeking a cup of water. In one apartment,

an apparently legitimate businessman churns out counterfeit notes. In every apartment, residents engage in their own forms of deception. The mystified peasant shakes out of his nightmare when he hears a haunting female voice singing *Jaago Mohan Pyaare, Jaago* (Get up, dear Mohan, get up) to awaken the baby Lord Krishna. The call to wake up was a call on Indians to start again.

Although many Indians recognized Nehru's socialist rhetoric as empty, the narrative of Nehruvian socialism stuck because of the severe import controls instituted by the Indian government to stem the drain on foreign exchange reserves. Such draconian controls were new to India. Even subsequent critics of Indian economic policy, including the economists Jagadish Bhagwati and Padma Desai, recognized that India was liberalizing imports before the start of the Second Five-Year Plan. The IMF dated the events more precisely. In the second half of 1956 when foreign exchange reserves were in their initial free fall, Indian import policy was only modestly restrictive, with some controls on the import of consumer goods while allowing liberal imports of raw materials and machinery. But, by early 1957, "Severe import restrictions [had] affected supplies of raw materials and component parts."⁴⁷

The imposition of import controls in late 1956/early 1957 was decidedly not a moment of socialist conversion, as many have since insisted. As Indraprasad Gordhanbhai ("I. G.") Patel, perhaps India's most distinguished economic policymaker in the post-independence era and one of the authors of the Second Plan, later made clear: "No one consciously initiated the policy." Import controls were based on "no theory or philosophy," Patel added emphatically. The simple truth, he explained, was that "everyone was surprised by the severity of the exchange crisis which hit us in 1956." Controls were a panicked defensive reaction to looming national bankruptcy. In Patel's words, "Necessity was the mother of invention of import controls."⁴⁸

Once "invented," though, import controls led to the explosive spread of other controls. As Gunnar Myrdal explains in an astonishingly insightful chapter in his *Asian Drama*, when a government restricts imports it must also restrict the number of new firms as well as the expansion of existing firms. If too many companies expand production, their demand

for imports could quickly exceed the limits set for certain imports. Thus, every new industrial production license soon came to require backing by import licenses for import of machinery; the industrial license also needed the green light from a “capital goods committee.” Although the Second Plan was clear that the production “targets” it had set for different industries were *not* “fixed and immutable,” and certainly not “ceilings,” licensing authorities used the targets to deny new licenses to some businesses while also raising the targets and ceilings for those who enjoyed the favor of key decision-makers. India’s production and import controls and the severity of import tariffs came to depend on the whims of the officers in charge and the ability of firms to lobby for protection.⁴⁹

The resulting capricious import protection of domestic industry was not designed—as in many now-industrialized economies—to give chosen industries breathing space to learn and grow. Even the “leftist” economist Prabhat Patnaik concluded that the controls and their knock-on consequences “flouted all cannons of economic efficiency.”⁵⁰

The effects were distinctly anti-socialist. Large Indian businesses, especially the House of the Birlas, gained a disproportionate share of the production and import licenses. “It is well known,” wrote an official inquiry into licensing practices, “Large Industrial Houses maintain liaison officers in Delhi [for] business and social contacts with senior persons in the Government and [they thus] seek to influence the exercise of discretionary power in their favour.” These business houses preempted the available licenses, leaving little room for potential competitors. The top executives of big business houses sat on the boards of government-owned or -controlled financial institutions, helping them corner a disproportionate share of (especially foreign currency) lending.⁵¹

Nehru continued in public appearances and writings to assert his commitment to a “socialistic” path of economic development. His ministers demonstrated their allegiance to the same mystical socialism. In May 1956, at the start of the foreign exchange crisis, the brilliant political cartoonist Shankar Pillai showed Nehru looking on indulgently as his flock of reliable geese (cabinet ministers and senior Congress Party leaders) cackled, “Socialism.” The rhetoric, as Myrdal noted, led many Western and South Asian pundits to the conclusion that “reliance on operational controls of

an administrative discretionary type imposes a 'socialist' pattern on the economy." Myrdal placed the word "socialist" within inverted commas, as if in exasperation. Surely, he wearily added, socialism is "a misnomer for a system of policies that broadly tends to give oligopoly power and very high profits to established big business." Pakistan had very similar controls, Myrdal noted, but absent the rhetoric, no one called Pakistan "socialist."⁵²

On the path Nehru set out for India, socialism was neither the intent nor the outcome. Limited job opportunities and high inflation placed greater stress on the very people Nehru professed to be helping. After the loud warning of the foreign exchange crisis in March–April 1956, Nehru had an opportunity to change course: raise productivity in agriculture and promote light industry. However, he stuck to his heavy-industry strategy. As one of Nehru's favorite poets, Robert Frost, wrote: "Oh! I kept the first for another day! Yet knowing how way leads on to way, I doubted if I should ever come back."

The Other Way Began with Rupee Devaluation

At the time, B. R. Shenoy was the only Indian economist arguing for abandoning the entire approach underlying the Second Five-Year Plan. Beginning in March 1957, in public speeches and a *Times of India* op-ed, he called for simultaneously "pruning" the Second Plan and devaluing the rupee.⁵³ Devaluation would make imports more expensive in rupees, thus inducing reduced imports. Bureaucrats would no longer need to decide who could import and how much. Devaluation would also encourage Indian businesses to sell their products abroad because the dollars they earned would convert to more rupees. The decline in the imports and the rise in exports would reduce the balance of payments deficit, perhaps even flipping the deficit to a surplus, as had happened after the rupee devaluation of 1949.

Nehru did not budge. Instead of using rupee devaluation to help Indian businesses sell labor-intensive, light-industrial products abroad, he continued with the original sin of heavy industrialization. Import and other controls grew like a cancer. The controls bred corruption. Private oligopoly power flourished. The inefficient Indian economy became even

more inefficient. Amid surging demand for jobs, employment growth suffered.

The warning signs were flashing going into the Second Plan, and the consequences were immediate, severe, and long-lasting. Even so, an argument can be made that the Plan was not necessarily an error: it blended with globally fashionable big-push industrialization and India's postcolonial exhilaration and yearning for rapid growth. The error was continuing down that path once it was clear that it was unworkable, economically damaging, and destructive of social norms.

Nehru continued down that path because he could. One man helped him perpetuate his reflexive error: John F. Kennedy. In fact, Kennedy helped Nehru double his dangerous bet.