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Why Punjab has Suffered Long, Steady Decline

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Introduction

Punjab has historically been one of the fastest-growing and richest states of India, with one of the lowest poverty rates. Punjab's farmers are the best in India, boasting the highest rice and wheat yields. The state was at the very heart of the green revolution which, starting in the mid-1960s, ended Indian starvation and heavy dependence on food aid. Punjab was among the first states to provide weather-proof roads and electricity to all villages, these being important facilitators of the green revolution. Electricity was required to provide irrigation through tubewells, and good roads were essential to move inputs to farms and produce out to markets. Punjab has always boasted a tradition of entrepreneurship and willingness to travel to other states and countries in search of work. This has produced a large return stream of cash remittances, estimated to be the second largest of any state after Kerala.[1]

However, since the 1980s the state has lost its economic leadership among states and steadily slipped behind other states. In the budget speech introducing the state budget for 2011-12, the Punjab Finance Minister said, "I must mention that on the basis of per capita income, Punjab which was at one time the top State in the country has slipped to number four among the bigger states and to number eight if all the states and union territories are reckoned. Punjab cannot be satisfied with anything but the first place in this regard."[2]

Since the 1990s (see Table 2.1), Punjab's GDP growth has been lower than the national average. According to government data (CSO estimate, November 2011), the state's GDP growth in 1994-2002 was 4.32 per cent per year, against the national average of 6.16 per cent; and in the period 2002-2011, Punjab's rate was 6.61 per cent against the national 7.95 per cent. By global standards, these were reasonable rates of growth. But relative to other Indian states, Punjab kept slipping.[3]

TABLE 2.1

Growth of State GDP

(Per cent)

	1994-95 to 2001-02	2002-03 to 2010-11
Punjab	4.32	6.61
Rajasthan	7.36	6.83
Gujarat	6.45	10.42
Haryana	6.47	9.17
Chhattisgarh	3.16	9.19
Himachal Pradesh	6.81	7.91
Uttrakhand	4.61	12.21
All India	6.16	7.95

Source: Central Statistical Organisation Databook, November 1st, 2011.

A major weakness has been a high fiscal deficit, which is the highest among all major states—budgeted at 3.4 per cent of GDP for 2011-12. The high fiscal deficit arises mainly out of huge unwarranted subsidies, the chief culprit being free power to farmers. One consequence is that the government is not even able to pay all salaries on time. This leads to demoralisation and cynicism among staff, who look for avenues to make money illegally.[4]

As measured by the Economic Freedom Index (EFI) in this report, Punjab's rank has slipped badly from 6th position in 2005 to 12th position in 2011. This does not reflect a major deterioration in its freedom rating, which has dipped just marginally from 0.41 to 0.39. But it has failed to keep up with other states, many of whom have improved their freedom ratings dramatically. Gujarat, the freest state, has gone up from 0.46 to 0.64. Haryana, which used to be the most backward part of Punjab until it split away in the 1960s, has improved its index value from 0.47 to 0.55, and has consistently ranked as the fourth-freest state from 2005 to 2011. This drives home the overall story of Punjab's steady relative decline, even though in absolute terms its performance has not been too bad.

However, there is one clear silver lining. At the local level, Punjab's cities have created a relatively good business climate. Ludhiana, the biggest city in the state, is reckoned by the *Doing Business* studies of the IFC/World Bank study to have the best business climate among major Indian cities. However, too much should not be read into this—the correct interpretation is that Punjab is less of a laggard than other states, but far behind places elsewhere in the world. India ranks just 134th out of 183 countries in ease of doing business, so being India's best does not mean excellence by international standards.[5]

Some Myths about Punjab's Decline

Why has Punjab suffered relative decline in the last two decades? Politicians and academics in Punjab reel out a long list of reasons but most of these turn out to be exaggerated or downright false.

Myth No. 1: India has fought several wars with Pakistan across the Punjab border and fears of fresh wars have kept industry away from Punjab

Normally, successful agriculture produces lots of consuming power for farmers and workers, and becomes a good basis for industrialisation. Punjab also has a good road network and is not too far from the major metropolis of Delhi. The state's scholars claim that industrialisation has been held back by the fact that it is a border state, next door to Pakistan, with whom India has fought three full-scale wars and several other skirmishes. Because of this, they say, New Delhi has been reluctant to allow major investments in the state, since these would be sitting ducks for Pakistani aircraft in the event of a war. This, they claim, has artificially held back the state's industrialisation and hence its GDP growth.[6]

The claim is manifestly false. Gujarat is also a border state with Pakistan, and is the most industrialised and fastest-growing state in India. Even Rajasthan, another border state that is backward and mostly desert, seriously lacking infrastructure and agricultural potential, has grown faster than Punjab (see Table 2.1). It is worth mentioning that the original Punjab state was in 1965 split into two, with the most backward southern part forming a new state, Haryana. This once-backward portion now grows much faster than the once-advanced portion that is still called Punjab. To be fair, Haryana has a special advantage that other states don't—it surrounds Delhi state on three sides, so Delhi's urban sprawl has spilled over into Haryana.

There was indeed a time, in the 1960s and 1970s, when the central government sometimes seemed hesitant to build major public sector industrial projects in Punjab because of its location next to Pakistan. Nevertheless, it built a railway coach factory at Kapurthala, a unit of Hindustan Machine Tools in Ludhiana, and helped launch Punjab Tractors in Mohali. There have been no hostilities across India's western border with Pakistan (comprising the states of Punjab, Rajasthan and Gujarat) since 1971. In none of the three Indo-Pak wars of 1947, 1965 and 1971 was there bombing by either side of industrial factories—the focus was on military targets.

In any case the public sector has long ceased to be the driving force of industry in India and economic reform starting in the 1980s and accelerating in the 1990s have put the private sector in the driver's seat. The private sector has invested massively in two other border states, Gujarat and Rajasthan, but much less in Punjab. Clearly proximity to Pakistan is not a good excuse for Punjab's slippage in the economic growth table.

New Delhi has permitted Reliance Industries Ltd to put up the largest oil refinery complex in the world in Gujarat, within easy reach of Pakistan's Air Force. Essar Oil has built the country's second biggest refinery complex in the same state. This year, a joint venture of Hindustan Petroleum Corporation Ltd. (a central government-owned company) and Mittal Industries has commissioned a big 9-million tonne oil refinery at Bathinda in Punjab, just 100 kilometers from the Pakistan border. This disproves the thesis that New Delhi's war paranoia has held up industrial projects in Punjab. Indeed, the Bathinda refinery may soon export fuel to Pakistan.[7]

New Delhi has built an international airport at Amritsar, a stone-throw away from the Pakistan border. The state's politicians claim that this international airport has not been allowed to develop because it is just a few miles from the border. The claim is not convincing—if indeed security were such an important consideration, surely New Delhi would never have created an international airport at Amritsar in the first place.

Myth No 2: Sikh terrorism caused Punjab's decline

Sikh militant separatists wanting to create an independent state of Khalistan were on the rampage in Punjab from the start of the 1980s to 1993. The state at one point became so ungovernable that it was placed under martial law. During the insurrection, New Delhi sought some sort of accommodation with disgruntled Sikhs, but failed dismally. Martial law also failed. Then in the 1990s a new Congress government came to power and decided to crack down on militants, using the police, not the army. The police had the local knowledge needed to hunt down the militants, and used some of the same savage tactics that the militants themselves had used. Although this implied major violations of civil rights, it succeeded in finally crushing Sikh militancy by 1993.

Now, it is true that in the heyday of Sikh militancy in the 1980s, industrialists were not keen on opening new factories in the state. Some industries that were located in Punjab (such as Hero Honda, India's biggest motor-cycle manufacturer) built new factories in other states. But Sikh terrorism ended two decades ago, and Punjab's decline has continued nevertheless. Prof Gurmail Singh of Punjab University points out that Sikh militants had a complete grip of western districts but not of eastern districts of the states, yet industrial growth from the 1980s onwards was weak in both eastern and western districts.[8]

Today, many Indian states face Maoist insurrections, which sometimes look as threatening as Sikh militancy once was in Punjab. In the last decade, an estimated 167 out of 600 Indian districts have suffered from some form of Maoist violence. Yet this violence has not come in the way of India achieving its fastest growth in history. The most entrenched Maoist-held areas are in the state of Chhattisgarh, which has huge forests, relatively few roads, and limited administrative breadth. The Maoists control very large areas in the state. Yet Chhattisgarh has been in the last decade one of India's fastest growing states, averaging 9.1 per cent per year between 2002-03 and 2010-11 (see Table 2.1). It is a major producer of steel, sponge iron and aluminum. No doubt it has the advantage of big mineral deposits but Maoists have seriously disrupted this. The contrast between economic growth in Punjab and Chhattisgarh demonstrates that terrorism does not necessarily mean economic decline, and can coexist with double-digit growth. Besides, almost two decades have passed since the end of terrorism in Punjab, so it is a poor excuse for the state's continuing weak performance.

Punjab politicians say that the state accumulated huge debts because of low revenues and the high cost of combating terrorism in the terrorist era, and claim that New Delhi has not given enough debt relief to Punjab to get rid of this historical burden. In her 2011-12 budget speech, the Punjab Finance Minister Ms Upinder Kaur said, "Punjab was a revenue surplus State until 1986-87 and its debt burden was only 27 per cent of Gross State Domestic Product. By 1994-95 the debt rose almost to 36 per cent of Gross State Domestic Product owing to successive revenue and fiscal deficits in these eight years. These were the years of militancy in Punjab and the State was under a long spell of President's Rule from 1987 to 1992. The Central Government, which was then running the administration of the State, followed a policy of high non-productive expenditure without raising any resources and to achieve this, it plugged the gap with unproductive and often high-cost loans. The debt burden of the State is a legacy of militancy, long years of President's Rule and an indiscriminate fiscal policy followed by the Central Government."[9]

This is disputed strongly by New Delhi. A former Finance Ministry official who dealt with Punjab's debt problems says that debt relief for the terrorist era has been given in ample measure by the Twelfth and Thirteenth Finance Commissions (these commissions periodically decide on how central government revenues should be shared with the states and what allowances are required for the special conditions in some states). The real problem, says the official, is that slow GDP growth has meant slow revenue growth and its fiscal impact has been compounded by huge non-productive subsidies, mainly for electricity. The official adds that most Punjab politicians got used to having several personal security staff in their entourage during the terrorism era of 1980-1992 and are reluctant to give these up. Punjab has a very high police/population ratio but the police are diverted massively from standard law and order operations to VIP security. This is a huge waste of public funds.[10]

Myth No 3: Punjab is very distant from the sea and so is unable to grow as fast as states with ports

No doubt coastal locations have their advantages. No doubt closeness to a port helps develop export industries. Yet Punjab was just as far from the sea through most of its history, including the first three decades after Indian independence and this did not prevent it from becoming one of India's richest, fastest-growing states. The world over, land-locked states complain that they are seriously disadvantaged, yet many of them grow fast. In South Asia, Bhutan has been the fastest-growing country and has comfortably overtaken India in per capita income. In Africa, land-locked Botswana has overtaken coastal South Africa to become the continent's richest country. After the collapse of communism in the Soviet Union and Eastern Europe, the richest of the ex-communist states has turned out to be Slovenia, which is virtually land-locked (it has only one minor port and exports mainly through Trieste in Italy).[11]

The lesson is clear. Geography is not destiny. Land-locked areas may have disadvantages but are capable of becoming rich and fast-growing if they follow the right policies. Just as badly land-locked as Punjab are the two neighbouring hill states of Himachal Pradesh and Uttarakhand, both of whom have grown much faster than Punjab (see Table 2.1). However, these two states have been aided by tax breaks bestowed by New Delhi.

Until the 1980s, New Delhi followed a "freight equalisation policy" that enabled all states to get industrial inputs like coal and steel at the same government-ordained price. Once freight equalisation was abandoned in the 1990s, Punjab's distance from coal mines and steel plants became a disadvantage. However, many other states were just as disadvantaged in distance from coal mines and steel plants but fared well. The best example of this was Gujarat, which became India's fastest-growing major state even as Punjab kept slipping (see Table 2.1).

Myth No 4: Punjab has no metallic minerals or coal and so loses out to states that do

Punjab suffers from chronic power shortages and this has been an important discouraging factor for potential industrialists. Indian coal has a high rock content, so transporting coal from coalfields—all of which are very distant—means transporting almost as much rock as coal, thus raising generating costs. The main mineral-bearing areas are in central and eastern India. Punjab's politicians claim that a lack of raw materials has placed the state at a serous disadvantage.

However, the mineral-rich central and eastern states have historically been among India's most backward and slow-growing. This is because minerals in India are generally found in mountainous jungle areas with few roads or other infrastructure, inhabited by tribes with some of the highest poverty, lowest literacy and worst health indicators in India. The mountainous terrain makes road and railway building difficult and expensive. Through history, across the globe, vibrant agriculture has been the driver of growth in rich civilisations, not minerals. That has always been true of India as a whole.

One reason for this is that minerals should not be interpreted to be just coal or metallic ores. Good agricultural soil is a form of mineral wealth and this was the driver of all great ancient civilisations from Egypt to China. And Punjab has this sort of mineral wealth in abundance—its soils are excellent for agriculture and rank among the best in India. This is one reason why its agricultural yields are the highest among any state.

Mineral wealth is by no means a key determinant of either industrialisation or GDP. Maharashtra, Tamil Nadu and Gujarat are India's most industrialised states, with high GDPs. None of them has major minerals. Maharashtra has substantial coal reserves for power generation but Gujarat and Tamil Nadu do not. Looking across the globe, we find that countries like Japan, Korea and now China have shown it is possible to import minerals from across the world and yet produce internationally competitive industries and become miracle economies. Punjab itself was the fifth-most industrialised state in India in the 1980s, despite the lack of nearby minerals or coal. The reasons for its subsequent decline have to be found elsewhere.

The Real Reasons for Punjab's Relative Decline

Punjab's relative decline can be traced to several factors, of which the most important is a serious fiscal crunch. This in turn is due mainly to the supply of free electricity to farmers. Other reasons include the agricultural plateau reached by the green revolution; the failure to diversify fast enough out of agriculture; the failure to make the educational investments necessary to induce a switch to service industries like computer software; very high land prices that have discouraged industry; and Central Government tax breaks for neighouring hill states that led to an unwarranted flight of industry from Punjab to these states.

The fiscal crunch

Punjab used to have large revenue surpluses in its glory days in the 1960s and 1970s. But in recent decades it has persistently run a high fiscal deficit, which is currently the highest among all major states (budgeted at 3.8% of GDP for 2011-12). This high figure arises mainly out of huge unwarranted subsidies, the chief culprit being free power to farmers. One consequence is that the government is not even able to pay all salaries on time. This leads to demoralisation and cynicism among staff, who look for avenues to make money illegally.

Like other states, Punjab has enacted a Fiscal Responsibility and Budget Management Act, which aims to reduce the state's revenue deficit to zero (that is, borrowing will be used only for capital spending, not current expenditure). In fact the revenue deficit has increased from 1.8 per cent of GDP in 2011-12 to 2.75 per cent in 2011-12. The state has often argued that it ran into huge revenue losses in the period 1986-1992 when Sikh terrorists launched a major insurrection. However, as noted in the previous section of this chapter, the state has been given debt relief by three Finance Commissions in a row and besides terrorism ended two decades ago. So this excuse wears very thin. The major problem lies in runaway subsidies, above all the supply of free electricity to rural areas.

The original composite Punjab state was split into Haryana and a truncated Punjab in 1965. Haryana was at the time regarded as the most backward part of the original state, yet it has forged ahead and boasts strong revenue growth and a surplus on current budget account, in contrast to Punjab's weak finances. Some Punjab academics say the state's tax administration is weak because of high levels of corruption.[12]

In his speech presenting the Punjab budget for 2012-13, Finance Minister Dhindsa said, "The actual revenue deficit for 2011-12 has shot up to ₹ 6,838 crore ($1,368 million) against ₹ 3,379 crore ($676 million) in the Budget estimates. The slippage in the target is mainly on account of no additional resource mobilisation measures and increase in salary and pensions." The minister further said "the committed expenditure on account of salaries, pensions, interest payments and power subsidy is likely to be ₹ 30,560 crore ($6,130 million) in 2012-13—amounting to 80.44 per cent of the revenue receipts of the year. The level of debt is also not sustainable. The gross borrowings for 2012-13 will be ₹ 13,204 crore ($2,641 million), which will mainly go into repaying the principal amount and interest, leaving only ₹ 2,936 crore ($587 million) in the hands of the state. More than 80 per cent of the net borrowings are going into meeting revenue deficit, leaving only 20 per cent for capital expenditure. The interest payments as percentage of revenue receipts have increased to 23.5 per cent in 2011-12—this is one of the highest for any state in the country."[13]

The ruling coalition of the Akali Dal and Bharatiya Janata Party has also resorted to other subsidies to win votes. These include subsidised *atta* (wheat flour) and dal (lentils and gram), free bicycles to all school children, and a marriage grant (*shagun*) to new brides. Punjab is hardly alone in distributing freebies. Other states like Tamil Nadu have given voters colour TVs and laptops. Yet these other states are able to generate a revenue surplus, while Punjab cannot. The main problem is its exceptionally high burden arising from free electricity.[14]

The curse of free rural electricity

Competition between political parties for farmers' votes has led over the years to electricity being supplied by the Punjab government to farmers free of charge since 1998. Canal water is also virtually free in canal-irrigated areas. At one time, subsidised electricity was seen as a way of promoting the green revolution, which required assured irrigation. But, as Ashok Gulati says in a separate chapter in this report, "since demand for such subsidised inputs greatly exceeds the supply, the quantity farmers get is rationed by government agencies. Rationing limits the number of connections, hours of electricity supplied, and days on which canal water is released into canals. Where states charge for electricity, it is generally as a flat monthly rate per horse-power, with no meters. The marginal cost of pumping becomes zero. This induces farmers to growing inappropriate water-intensive and electricity-intensive crops such as paddy and sugarcane even in low-rainfall areas. For example, paddy in Punjab and Haryana requires roughly 225 centimeters of irrigation water per crop. But the annual rainfall is only 60 centimetres. So, farmers have to pump huge amounts of ground water for thirsty paddy, depleting the water table at an alarming rate (33 cms per year, according to NASA satellites during 2002-2008)."

Apart from this destruction of acquifers, free farm electricity has now become the biggest cause of the state's fiscal troubles. S.S. Johl, former head of Punjab Agricultural University, says that the state's total debt is ₹ 78,000 crore ($15.6 billion) and contingent liabilities through guarantees are another ₹ 40,000 crores ($8 billion). He estimates that 90 per cent of this debt burden has arisen from the enormous cumulative impact of electricity subsidies, currently running at over ₹ 5,000 crore per year. He says one of the consequences of the fiscal crisis is that salary payments are delayed by months in most government departments and also in Punjab Agricultural University.

Johl says that, when he was advisor to former Chief Minister Amarinder Singh, he negotiated a loan of ₹ 1,000 crore ($200 million) from the World Bank for revamping the state's marketing systems and run-down power transmission system. But this was tied to reforms, including the reduction of power subsidies. Initially, the state government was willing to limit free electricity to small farms but as the next state election drew close, the government made electricity free for all farmers, abandoning all pretense of reform. The World Bank refused to proceed with the loan, so the state lost a badly-needed project.

Johl says that the so-called subsidy to farmers is actually passed on to consumers, and so does not benefit farmers at all. The Commission on Agricultural Costs and Prices determines the minimum support price for different crops every year based on actual input costs. The subsidy on rural electricity leads to a correspondingly lower support price. This benefits consumers of grain, not farmers. Yet Punjab's political parties find it politically impossible to charge farmers.

Some farmers have huge holdings and up to 150 tubewells each, says Johl, so the rich are benefiting disproportionately from the subsidy. He estimates that 83 per cent of farms are smaller than 2 hectares (5 acres). These small farmers initially installed centrifugal pumps costing around ₹ 30,000 ($600). But these stopped working when the water table fell. Farmers now have to install submersible wells costing up to ₹ 200,000 ($4,000) and only better-off farmers can afford this. They in turn cream off the bulk of the subsidy. And they are mainly responsible for the calamitous fall in the water table. This needs to be combated by a switch to sprinkler irrigation and drip irrigation, both of which conserve use of water. But this switch will not be possible till farmers have to pay for water and so have an incentive to use water-saving technologies.

Meanwhile fiscal strain means the state government has been unable to build any new power plants for several years. In the early 1980s, says Johl, Punjab spent up to 60 per cent of its budget on increasing power generation and transmission, and this helped drive the state's growth. Those days are over. The state's transmission and distribution (T&D) system is in terrible shape and badly needs rehabilitation and upgradation to cut transmission losses. Acute power shortages have discouraged new industries from investing in the state.

Thus, the political decision to subsidise farm electricity has become an unwitting tax on industry and has hobbled the state's development

Punjab is now trying to overcome the problem by asking private sector companies to generate power (historically, power generation, T&D was a state monopoly). Several new private sector power plants are expected to be commissioned in the next two years. The state will soon get 1,940 mw from Vedanta (at Talwandi Sabo), 1,400 mw from L&T (at Rajpura) and 540 mw from GVK (at Goindwal). This should improve the very tardy pace of industrialisation. But experience in other states shows that bankrupt state governments tend to renege on deals with private power generators and so convert ostensibly profitable power projects into unprofitable ones. Many states have refused to allow tariff increases to compensate for higher fuel costs and many are in arrears of payment to private suppliers for the electricity they buy in order to distribute free to farmers. The electricity outlook remains clouded.[15]

The green revolution tapers off

Punjab pioneered the green revolution in India through the use of high yielding seeds, accompanied by high doses of fertiliser and water. Punjab Agricultural University (PAU) modified high-yielding seeds from Mexico and other sources to suit Punjab's agroclimatic conditions. However, by the 1990s, gains from the new dwarf varieties of rice and wheat introduced in the 1960s had mostly worn off. PAU, which had developed the first seeds for the green revolution, has failed to keep up the good work by creating ever-better varieties. Its researchers are demoralised by the state's priorities of wooing farmers and other with massive subsidies, leaving the state government with insufficient money to pay salaries on time, or to fill vacant posts. S.S. Johl says that politicians criticise PAU for not producing enough new high-yielding varieties in recent years but how can demoralised researchers without salaries be expected to produce research breakthroughs? Many good scientists have left for greener pastures.

Private sector agricultural research cannot make good this gap in full. Private seed companies can and have produced excellent new varieties of hybrid maize and genetically modified cotton, because for such crops farmers have to buy seeds afresh from the companies every year and the companies can thus recover their research costs with a profit. But in the case of self-pollinating crops like wheat and rice, farmers can simply save grains from the last harvest and use these as seeds for the next season, without buying seeds afresh from companies. Companies will not do any research for such crops because they have no way of recovering their research costs. For such crops, public sector research is inescapable. PAU used to be at the very fore of R&D in self-pollinating crops like rice and wheat and its decline has therefore affected the growth of agricultural productivity in the state.

Fast-expanding tubewell irrigation was initially the driving force of agricultural growth, but once 95 per cent of the land had come under irrigation, this ceased to be a source of dynamism. Excessive tubewell pumping, perversely encouraged by the supply of free electricity to farmers, has in some districts exhausted sweet ground water but farmers started pumping the brackish water underneath. This led to salt deposition on the soil, rendering some areas infertile.[16]

The state government also had a historically efficient network of canals but land along these canals has tended to get waterlogged and saline, because of imperfect drainage. The supply of virtually free canal water has deprived the state of revenue to maintain canals and ensure proper drainage. Large areas need reclamation with chemicals to restore yields, and one such reclamation project has been done at Kandi in Hoshiarpur district with World Bank assistance. Watershed development was actively followed in earlier decades in the hilly areas of the state to conserve water. But now most of the tanks and reservoirs built in the watersheds have silted up and have not been restored. The problem is that these tanks belong to and are operated by the state government. Had they been handed over to local communities, they might have fared better.[17]

The state attempted after the 1980s to diversify into fruit and vegetables. But the shift was never fast enough and constant power cuts in rural areas meant that good cold chains—essential for preserving fruit and vegetables—were not possible. The central government limited active procurement at guaranteed support prices to rice and wheat and farmers were therefore reluctant to shift to other crops whose prices were far more volatile. The state did indeed develop a vibrant dairy industry. *Basmati* rice has a much lower yield than high-yielding dwarf varieties but fetches a premium price. However, the bulk of the state's farm area continues with an ecologically destructive rotation of high-yielding wheat and rice, which has lowered the water table disastrously. Traditional drinking water wells have all run dry because of this. Many shallower tubewells of small farmers have also run dry as the water table keeps falling. Of the state's 127 development blocks (this is an administrative unit), no less than 105 are now called "dark areas" where the fall in the water table is completely unsustainable. In some areas the sweet water is all gone and only brackish water remains. This has affected the state's agricultural dynamism.

Failures in agricultural marketing

Punjab, like most other Indian states, has an Agricultural Produce Marketing Committee Act that makes it mandatory for farmers to sell most sorts of agricultural produce only in government-organised markets called *mandis*. The Act was supposed to protect farmers from exploitation by private traders offering throwaway prices. The state government itself procured major crops like wheat and paddy at specified minimum support prices. However, there is in practice no government procurement of other crops at specified support prices. In the case of these other crops, the *mandis* have obtained a trade monopoly that is mercilessly exploited by a limited group of traders with political connections. Former Chief Secretary S.C. Aggarwal says that many bureaucrats have attempted to end the monopoly of *mandis* but met with severe political resistance—traders are prominent politicians and are also traditional financiers of leading political parties. The state government extracts almost 14.5 per cent in various levies from the *mandis* and this is a major source of revenue.

Traditionally, the grain procurement agencies of the central and state governments made payments to the big middlemen at the *mandis*, who then paid farmers with a lag. This often led to disputes and heartburn among farmers. However, with the rapid spread of cellphones into rural areas, it is now feasible to get farmers to open bank accounts and get payments online directly into their accounts. New Delhi has asked all states to try and make payments directly to farmers if possible, and this has been adopted by some states, including historically backward ones like Madhya Pradesh. But Punjab has not done so despite having one of the highest rates of rural cellphone penetration. It still makes payments through the big traders, once again underlining their political clout.

Many private sector corporations would like to buy produce directly from farmers—this will eliminate layers of middlemen and prove a win-

win for both farmers and consumers. But trading interests have been able to sabotage this move. Ashok Gulati writes in a separate chapter in this volume, "Crops like fruits and vegetables need to be freed from marketing controls ordained by obsolete APMC (Agricultural Produce Marketing Committee) laws. Indeed, the APMC Act needs to be changed to encourage direct sourcing by retailers from farmers' groups, to compress supply chains by removing unnecessary middlemen, and to invest in back-end infrastructure. For this organised retailers, both domestic and foreign, need to be encouraged and incentivised."

Failure to catch the services revolution

When Punjab was among the very forefront of states in the 1970s, it had every opportunity to prepare for a switch out of agriculture into industry and services. It was already among India's foremost states in roads, rural electrification and per capita income, and could have invested in education to produce the skills needed for further economic development. The Central government had in 1963 set up one of its prestigious Indian Institutes of Technology (IIT) at Ropar in Punjab. Now, such IITs helped spark the computer software revolution in Bangalore, Mumbai and several other Indian cities. But not in Punjab.

One reason for the state's neglect of higher education and information technology was that its politicians never evolved from a mind-set that emphasised agriculture above all else, and focused on buying the votes of farmers through subsidies rather than diversification out of agriculture. Punjab did indeed compete with other states in trying to attract industry but hardly at all in trying to attract high-tech services. So Punjab was left far behind the states in southern and western India that spearheaded the IT revolution.[18]

In 1965, the current Punjab state was carved out of the composite historical one as a Sikh-majority state which would institute Punjabi in the Gurmukhi script (used by traditional Sikhs) as the state's official language. This religion-based emphasis on promoting Punjabi meant that the state educational system had insufficient interest in pushing for English language education. Other states saw that good English skills were vital to reap the benefits of globalisation, most obviously in the form of business outsourcing and call centres. The Punjab government failed to emphasise English for so long in government schools that desperate parents started sending their children to private schools that cost more than free government schools but taught English.[19]

Free electricity and the consequent fiscal crunch have seriously impeded growth of public spending on education and health, which has historically been below levels in other Asian developing countries (see Table 2.2). Despite this low base, such spending has grown more slowly in Punjab than in almost any other state in recent times. In public education, Punjab's average growth rate was just 7.7 per cent per year in 2004-2010 against the national average of 14.9 per cent, and 21.2 per cent in Haryana, which used to be the backward portion of the original composite Punjab. In health, Punjab's growth was just 5.5 per cent per year against the national average of 14.4 per cent and Haryana's 28.4 per cent. Adjusted for inflation, there was hardly any real growth at all in Punjab's social spending. This neglect of education is one reason why Punjab has failed to climb onto the services bandwagon that most other advanced Indian states managed to do.[20]

TABLE 2.2

Growth of Public Spending on Education and Health (% per year, 2004-2010)

	Public Education	*Public Health*
Andhra Pradesh	12.1	14.3
Assam	9.1	25.7
Bihar	16.7	22.4
Chhattisgarh	20.6	17.2
Gujarat	10.6	10.9
Haryana	21.2	28.4
Jharkhand	21.4	18.4
Karnataka	14.6	12.1
Kerala	12.2	19.8
Madhya Pradesh	13.2	11.5
Maharashtra	13.4	13.2
Orissa	17.2	11.2
Punjab	7.7	5.5
Rajasthan	14.0	21.6
Tamil Nadu	15.6	10.8
Uttar Pradesh	19.8	12.4
West Bengal	10.7	5.1
All India	14.9	14.4

Source: Rao, M. Govinda (2012). *States' Fiscal Development and Implications for Regional Development*. National Institute of Public Finance and Policy. August.

Prof Gurmail Singh complains almost half the posts of teachers in government have not filled because of the fiscal crisis: retirees are simply not replaced. Many teachers have not been paid for months. Teacher absenteeism is high in all Indian states but Bihar and Punjab are the two worst. The quality of teaching was poor even in earlier times when salaries were paid regularly but non-payment would have further reduced whatever incentive there was to teach properly.

The Tribune, Chandigarh, reported in February 2012 that 840 headmasters were not receiving their salaries. Of 500 senior teachers recently promoted to the rank of headmaster, 380 were not receiving their salaries and so were regretting their promotion. The situation is as bad in medical colleges and health centres. Prof Surinder Shukla of Panjab University says she went to Muktsar district to study teacher absenteeism in schools. She was surprised to find that most teachers were totally disillusioned and demoralised. Interestingly, the majority of them were looking for ways to migrate to jobs abroad. Punjabis have always been globe-trotters, and the state even has a TV channel devoted to emmigration and allied issues.

The curse of high land prices

Prosperous rural areas have high land prices and it is natural for Punjab land to be expensive. It is also natural that Punjabis going overseas have for decades sent remittances home and these have typically been used by families to keep buying more land, pushing up prices. However, land prices in Punjab (and indeed in most Indian states) have been artificially inflated by perverse tax and administrative laws. Unlike other assets, farmland is exempted from capital gains tax and this distortion attracts a flood of money. Moreover, buying land is a hassle- free way of laundering black money in India. Because of high stamp duty, rural land is typically registered at a tiny fraction of the contract price in order to reduce stamp duty payment. Often half or more is paid in cash under the table and this means that black money can easily be laundered into respectable land. Such money laundering has sent land prices skyrocketing everywhere in India but the rates are highest in areas with flat fertile land, as in Punjab. This is good for land speculators but bad news for industries that need large parcels of land. Other states have plenty of relatively cheap rocky land and barren land that can be offered to industries to set up factories. But Punjab has very little such land and so is unable to provide land cheaply for industry.

Corporations are used to demanding and getting land very cheaply from state governments, which typically acquire land, using their power of eminent domain and then sell or lease this land at a highly subsidised rate to industries. Punjab has not only high land prices but also serious fiscal problems, which limit its ability to subsidise land for industry. S.C. Aggarwal, former Chief Secretary of Punjab, says that the Tata group initially wanted to set up its plant for its famous Nano car—billed as the cheapest car in the world at $2,500—in Punjab. But Tata wanted lots of cheap land for its factory and ancillary suppliers, plus tax breaks and Punjab could not afford to provide this. Aggarwal calculates that the net present value of tax breaks and cheap land demanded by the Tata group would have been ₹ 1,200 crore ($240 million), whereas Tata's own investment was just ₹ 700 crore ($140 million). Tata looked elsewhere, got excellent terms from the Gujarat government and located its plant there. Again, Reliance Industries Ltd was very keen on establishing a large food retail chain in Punjab, procuring produce directly from farmers. But Reliance wanted a lot of cheap land for warehousing and the state found it impossible to meet this demand, so Reliance went to other states.

In one case, says Aggarwal, the state had to pay one crore rupees ($200,000) per acre for acquiring land near Mohali for a technology park. No industry was likely to buy land at this rate but high-tech industries (including information technology companies) would find it possible. Even in deep rural areas, the price of land is ₹ 50 lakh ($100,000) per acre, too costly to attract most industries.

Flight of capital to neighbouring states getting tax breaks

Punjab complains that tax breaks given by New Delhi to industrial units in the nearby hill states of Himachal Pradesh and Uttarakhand have resulted in a flight of industry out of Punjab into the hill states. In 2003, New Delhi announced a special scheme of exemption from excise duty for units established in hilly states, including Himachal Pradesh and Uttarakhand, which adjoin Punjab. This created an industrial boom in both hill states—major industrial groups including Tata, Bajaj, Nestle, Mahindra, Hindustan Unilever, Britannia and LG set up new units to take advantage of this tax benefit. Any unit starting production between 2003 and 2010 was guaranteed excise duty exemption for 10 years after starting production. The implicit subsidy (foregone tax revenue) to industrial units has been estimated at over ₹ 10,000 crore ($2 billion) per year. Several Punjab industrialists set up new units in these states rather than expand in Punjab itself.

This preferential tax break was unwarranted. It was ostensibly aimed to offset the difficulties of establishing industries in hilly regions. Yet the industries that actually came up were in the narrow plains regions of these states, not the hilly areas. Punjab can fairly argue that the tax breaks diverted some Punjabi capital to these hill states. But the biggest investors in these states came from the western and southern India, and industrial growth in those two regions was not adversely affected at all. This factor alone cannot explain Punjab's slow rate of industrialisation. That is better explained by chronic power shortages, neglect of higher education, high land prices, corruption and fiscal problems. Punjab's investment rate used to be above the national average but has fallen below it since the 1990s. Prof Ranjit Ghuman of CRRID, Chandigarh, estimates that the state would have received an additional ₹ 9,500 crore ($1.9 billion) of investment had it simply matched the national investment average between 1995-96 and 2008-09.[21]

Some industry is nevertheless coming up. The 6 million tonne oil refinery at Bathinda is the biggest new unit and it could add a big chemical unit. New power plants built by the private sector will soon reduce the chronic power shortage. A pharmaceuticals cluster has come up at Mohali. Several companies have built or expanded factories for tractors, combine harvesters and other farm machinery. Abhishek Industries has put up a big mill making paper from agricultural waste. Nevertheless, Punjab remains an industrial under-performer.

Lack of trade with Pakistan

In the 1970s, Indian policy aimed at self-sufficiency and discouraged foreign trade. That robbed India's coastal states of an important locational advantage but did not affect Punjab. To that extent, Punjab gained relative to other states. But when the economy was liberalised in 1991, the coastal states boomed, with flourishing exports and imports. Punjab was unable to register similar gains because it was far away from any port. However, being land-locked and far from the sea is not necessarily fatal. For instance Austria and Switzerland are land-locked but are prosperous trading economies. This is because[22] they have excellent road and rail connections with neighbouring European states, with whom they share a free trade zone. By contrast, trade between India and Pakistan has been blocked or banned since the war of 1965 and existing trade is limited to relatively few items. This has deprived Punjab of the usual gains of international trade.

India has long offered Pakistan Most Favoured Nation (MFN) treatment under WTO rules but its non-tariff barriers (NTB) remain substantial. Pakistan has long refused to offer India MFN status, saying there could be no normalisation of trade or commercial relations until the Kashmir dispute between the two countries was settled. Only a limited number of Indian items were listed for import by Pakistan. Much of what was traded went by sea, not across the Punjab land border. There is still no provision for trucks and railway wagons to pass seamlessly from one country into the other. One consequence has been that South Asia is one of the world's least integrated regions in trade. The world over, regional trading agreements have facilitated rapid economic growth. But war, terrorism and political suspicion have prevented this from happening in South Asia. This has been especially detrimental to Punjab.[23]

However, recently Indo-Pak relations have shown signs of improvement, and Pakistan has indicated that it wishes to normalise trade relations. India has welcomed the change. This is a dramatic development, even though the process will probably be gradual. Till now, Pakistan has had a list of only 2,000 items that can be imported from India and of these only 137 could be imported through the land border with Punjab—the rest had to go by sea. This is to be replaced by a Pakistani negative list of 1,123 items (which cannot be imported) and this allows more than 7,0000 items to be imported from India. India has asked Pakistan to permit all these items to go through the land border. Too much not be expected quickly. But it means that Punjab's trade and economic prospects will brighten considerably. Already there is talk of expanding the HPCL-Mittal oil refinery from 6 million tonnes to 9 million tonnes to meet Pakistani demand for petroleum products like gasoline and to build a pipeline to Pakistan to transport the products.

Instead of being a deeply land-locked state with poor international trade prospects, Punjab could become the major Indian gateway to Pakistan. Most Indo-Pak trade currently goes by sea to the port of Karachi. But 55 per cent of Pakistan's population is in the Pakistani state of Punjab, a long way from Karachi but just across the border from Indian Punjab. So, Indian Punjab is well placed not only to become a supply base for Indian exports but as the gateway for Pakistan goods to enter India.

Some Positive Trends

The opening of trade with Pakistan is not by any means the only positive item in Punjab's future outlook. There are other bright spots too.

First, the tax breaks for Himachal Pradesh and Uttarakhand have ended in 2010. Even though reports of capital flight from Punjab to these states were exaggerated, whatever flight did occur has now ended.

Second, the fiscal crisis in the state has obliged ruling politicians to find finances outside the budget to finance essential infrastructure and services. So it has gone for public-private partnerships (PPPs) in a big way in areas that were formerly government monopolies. Electricity, roads, bridges, hospitals, schools, bus transport and other areas once reserved for the government have now been opened to PPPs or outright private investment. This promises to ease infrastructural bottlenecks, especially in electricity, with five new private sector power plants coming up. This will end the crippling power shortages that have long discouraged industrial investment in the state. The quality of hospitals, buses, schools and colleges is also expected to improve with private sector participation. The PPP model had also brought in new sources of revenue, for instance from fees paid by private bus operators on routes that were once government monopolies.[24]

However, PPPs in all states have been afflicted with allegations of corruption, and Punjab is no exception. Several bus routes and bus categories (like luxury buses) have been monopolised by a cartel of companies widely believed to be owned by politicians. If any independent operator attempts to enter the fray and break the cartel, he is physically threatened, and gets no protection from the state. Most private sector bus licences have been given for air-conditioned and luxury buses. The Tribune, a leading state newspaper, complains that the tax on conditioned buses has been halved, and on luxury buses has been cut from ₹ 7.50 ($0.15) to just ₹ 0.50 ($0.01) per km. This represents the worst sort of crony capitalism. Yet, at the end of it all, bus services have greatly expanded in quality and quantity, and government revenue from transport has also risen. The shift in service provision from the public sector to the private sector, warts and all, has produced major gains.

Third, the state set up an Administrative Reforms Commission in 2008, and some of the recommended reforms have been implemented. They promise a big improvement in governance.[25] The first phase of the reforms included a Right to Service Act that empowers citizens to demand and get better services from a corrupt, slothful bureaucracy. Implementation of this is spotty. But to a fair extent, citizens have been empowered to demand and get various services and certificate without the usual delays and bribes. Ration cards for subsidised food now have to be issued within 6 days of application. Citizens can complain against the police for non-action on grievances. The need for affidavits and other documents has been reduced. The ruling Akali Dal-BJP coalition government believes that the Right to Service was an important reason for its election victory in 2012. It has now launched the second phase of administrative in August 2012, with further measures to make the police and bureaucracy accountable to citizens through grievance redressal procedures.[26]

Fourth, the state has become one of the first to overhaul obsolete land policies to freely allow and record long-term leases. It has not placed any time limit on leases, leaving this to be decided mutually by owners and lessors. Since independence, all state governments have sought to discourage tenancy and emphasise “land-to-the-tiller” policies. This might have made sense when feudal lords owned huge areas of land. But today four-fifths of operational holdings are less than two hectares and land fragmentation is worsening as each plot is divided among several children after the death of a father. Once, rich farmers leased in land from poor ones. The opposite is happening now as rich farmers leave for cities and lease out their land to small farmers. But most leasing is informal and unrecorded—the owners are paranoid about losing their land to the tenant if there is any official tenancy record. However, the Punjab government says it will legalise long-term land leases. Many such reforms run into problems in practice but the Confederation of Indian Industry (CII) has hailed Punjab's initiative. Long-term leases will encourage lessors to make investments in the land. Such leases will encourage the consolidation of tiny plots into large economic farms and may usher in a new era of corporate farming.[27]

Fifth, despite problems like high land prices and power shortages, Punjab is widely viewed as a state that is investor-friendly, and encourages industry. As mentioned in the introductory section, Ludhiana, the biggest and most industrialised city in the state, is reckoned by the *Doing Business* studies of the IFC/World Bank study to have the best business climate among major Indian cities. It is worth looking at the study in some detail, as this is among the few sources of comparative data across states.[28]

Ludhiana, Punjab, is India's best city for ease of doing business

The IFC/World Bank produces an annual report on *Doing Business*, comparing countries across the world. India fares very poorly in these reports. In its 2012 report, India ranked a lowly 132nd of 183 countries in overall ease of doing business. In ease of starting a new business, India was even worse—it came 166th. In ease of getting a construction permit —a prime area of corruption—India was 181st, or third last in the world. In enforcement of contract—something supposedly essential for any business—India came 182nd, or second last! So, for all the economic liberalisation since 1991, much remains to be done. Most of these hurdles are at the state government and municipal level: these are the levels in charge of registration of new businesses, construction permits and the police-legal system. The states have clearly lagged well behind New Delhi in embracing economic reform.

The *Doing Business* series does not compare different states of India. But in 2009, it produced a special study called *Doing Business in India* which compared the business environment in different cities of India. This gives a fair idea of business conditions in the 17 major states.

Of the 17 cities it examined, top position went to Ludhiana, Punjab. There is no reason to think that conditions are worse in other Punjab cities. It appears that, among Indian cities, Punjab has created one of the most business-friendly environments. This does not mean, of course, that Ludhiana is particularly good compared with cities in other countries.

TABLE 2.3

Doing Business in Indian Cities: Where is it Easiest?

Rank	*City*
1	Ludhiana, Punjab.
2	Hyderabad, Andhra Pradesh.
3	Bhubaneshwar, Odisha.
4	Gurgaon, Haryana.
5	Ahmedabad, Gujarat.
6	New Delhi, Delhi.
7	Jaipur, Rajasthan
8	Guwahati, Assam.
9	Ranchi, Jharkhand.
10	Mumbai (formerly called Bombay), Maharashtra.
11	Indore, Madhya Pradesh.
12	NOIDA, Uttar Pradesh.
13	Bengaluru (formerly called Bangalore), Karnataka
14	Patna, Bihar.
15	Chennai (formerly called Madras), Tamil Nadu.
16	Kochi, Kerala.
17	Kolkata (formerly called Calcutta), West Bengal.

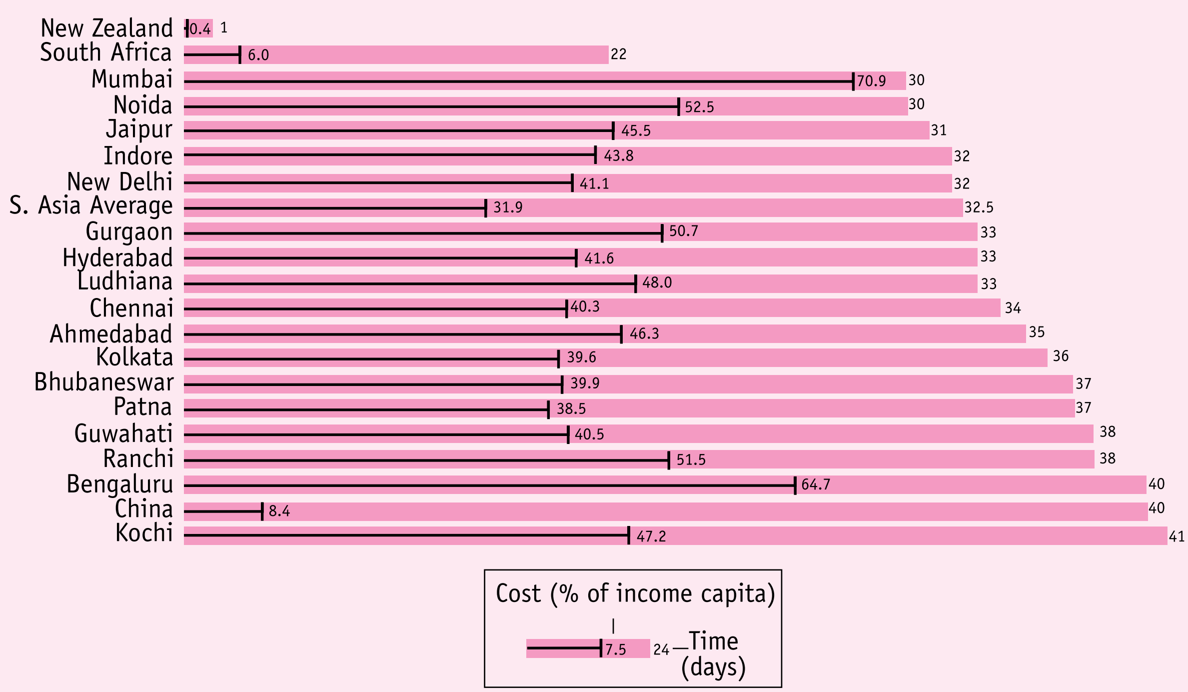
Table 2.3 is an eye-opener. Gujarat and Tamil Nadu are widely cited to be the best states for business, yet their top cities rank at only 5th and 15th position respectively. Maharashtra is India's most industrialised state. Yet its capital Mumbai comes way down the list at 10th position. This suggests that in some of the top destinations, the political-bureaucratic system is often designed to create hurdles, requiring the payment of "speed money" for clearances. Some of the more advanced states can get away with this: they are confident that corporations simply have to invest there. This has left some scope for the less popular investment destinations to offer a better business climate. Punjab is at the forefront of this.

Starting a business

The 2009 report looks at several different aspects of doing business. A key issue is the ease of starting a business. The report measures this by estimating the time and cost of all starting steps including permits, inscriptions, notifications and inspections. New Zealand is champion in this respect—starting a business requires only 1 procedure and takes only 1 day. Eastern Europe and Northern Africa are not far behind. Georgia has 3 procedures that take just 3 days and Egypt manages in 7 days. But in Indian cities, the average number of procedures is 12. These take on average 34 days and cost 47 per cent of per capita income (against 0.4% in New Zealand, 6% in South Africa and 8% in China). In Ludhiana, starting a business takes 33 days, somewhat more than in Mumbai (30 days) but far better than Kochi (41 days) or Bengaluru (40 days). Surprisingly, China's average is worse than even India's (40 days against 34 days), despite its reputation for getting things done in fast autocratic fashion (see Figure 2.1).

FIGURE 2.1

Time and Cost to Start a Business in India and Selected Economies



Source: *Doing Business* database.

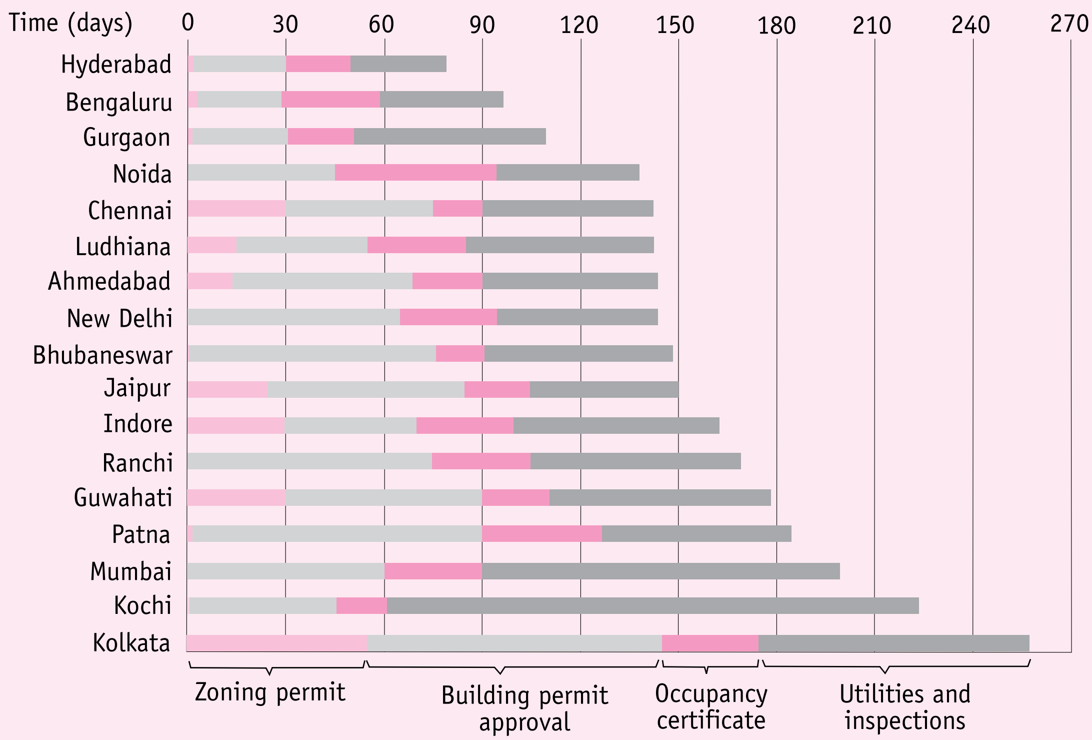
Getting construction permits

This is a major hurdle in all Indian cities. The average for the 17 cities was 20 different procedures taking 158 days and costing 772 per cent of per capita income. However, this is better than in neighbouring South Asian countries, where getting a construction permit takes 246 days and costs 2,341 per cent of per capita income.

Ludhiana, Punjab, comes 7th of the 17 cities. It has 17 procedures taking 143 days. Bengaluru fares far better with 15 procedures taking 97 days. But Ludhiana is far better than Kolkata and Mumbai, which have 27 and 37 procedures respectively and take 258 and 200 days respectively. The total cost as a proportion of per capita income is 623 per cent in Ludhiana, compared with 2,718 per cent in Mumbai (see Figure 2.2).

FIGURE 2.2

Building Permit Approvals and Utility Connections: The Biggest Bottlenecks



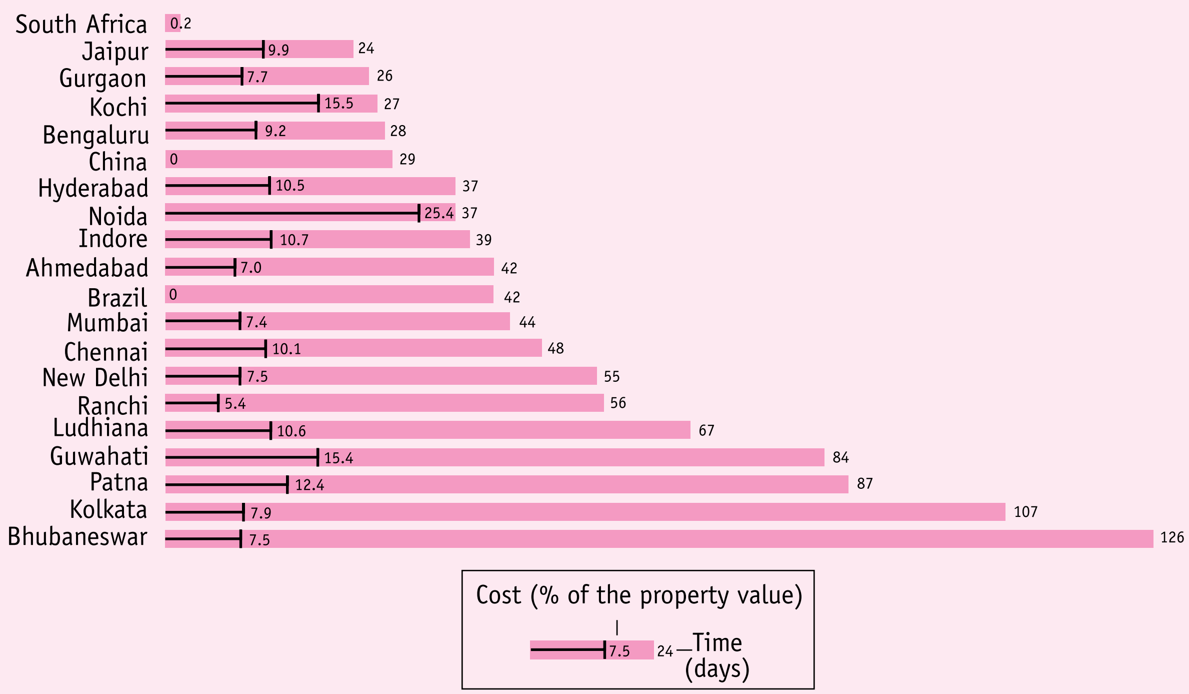
Source: *Doing Business* database.

Registering property

This is another area marked by cumbersome procedures, delays and corruption. In Saudi Arabia, property can be registered in just 2 days at zero cost. Brazil and China also have zero cost of registration, through they take 29 days and 42 days respectively. But in India, the average registration time in the 17 cities is 55 days, and the cost is a whopping 10.6 per cent of the property value. These costs arise out of high stamp duties, registration costs and lawyers' fees (see Figure 2.3).

FIGURE 2.3

Time and Cost to Register Property in India and Selected Economies



Source: *Doing Business* database.

Ludhiana, Punjab, is a laggard in this respect, coming 11th of 17 cities. The time taken in Ludhiana is 67 days. This is far behind Jaipur (24 days) but far ahead of Bhubaneshwar (126 days).

Paying taxes

Businesses pay a wide range of taxes at the central, state and local levels. There are taxes on production of goods and services, on the sale of goods and services, on transportation, on income. There are vehicle taxes, profession taxes, municipal taxes, environmental imposts and so on. *Doing Business in India 2009* also includes government-mandated contributions to employee provident funds and insurance funds. However, the calculation excludes value added taxes because these do not affect accounting profits.

In Hong Kong, a business spends on average 80 hours in 4 payments per year, adding up to 24.2 per cent of profits. But India ranks 169th of 183 countries in this respect. The average Indian business spends a whopping 278 hours on 65 different payments per year, adding up to 68.4 per cent of company profits. India's South Asian neighbours have only 37 payments per year aggregating 44.4 per cent of profits but this can take more time—336 hours per year.

Tax payments are a major irritant in Ludhiana too but the silver lining is that it is the best of the 17 Indian cities (see Table 2.4).

TABLE 2.4

Where it's Easiest to Pay Taxes in 17 Indian Cities

Rank	*City*
1	Ludhiana, Punjab.
2	Jaipur, Rajasthan.
3	NOIDA, Uttar Pradesh.
4	Mumbai, Maharashtra, and Ranchi, Jharkhand.
6	Guwahati, Assam.
7	Gurgaon, Haryana.
8	New Delhi, Delhi.
9	Bhubaneshwar, Odisha.
10	Indore, Madhya Pradesh.
11	Ahmedabad, Gujarat.
12	Bengaluru, Karnataka.
13	Hyderabad, Andhra Pradesh.
14	Kochi, Kerala.
15	Patna, Bihar.
16	Kolkata, West Bengal.
17	Chennai, Tamil Nadu.

Ludhiana is joint number one with Bengaluru, Mumbai and NOIDA in the number of tax payments per year—59. A major industrial centre like Ahmedabad requires 75 payments and Hyderabad 78.

Trading across borders

Merchandise exports are around 15 per cent of GDP in India. Imports are almost 20 per cent of GDP. Ease of export and import is an important business consideration. Some cities are far inland, so businesses in such cities have to import and export goods through a distant port in another state. So, the ease of trade depends on central government regulations as well as those in the port states and inland states.

In this respect, Ludhiana comes only 12th of 17 cities. This reflects in part its land-locked position: being far inland handicaps it relative to port cities. Other cities close to Ludhiana rank lower—Jaipur and New Delhi rank joint 14th, NOIDA (on the periphery of Delhi) comes 16th, and Gurgaon (also on Delhi's periphery) comes 17th. So, Punjab can claim that it beats the nearby competition (see Table 2.5).

TABLE 2.5

Where it's Easiest to Import and Export

Rank	*City*
1	Bhubaneshwar, Odisha.
2	Chennai, Tamil Nadu.
3	Ahmedabad, Gujarat and Mumbai, Maharashtra.
5	Kochi, Kerala.
6	Kolkata, West Bengal
7	Guwahati, Assam.
8	Ranchi, Jharkhand.
9	Bengaluru, Karnataka.
10	Patna, Bihar.
11	Indore, Madhya Pradesh.
12	Ludhiana, Punjab.
13	Hyderabad, Andhra Pradesh.
14	Jaipur, Rajasthan, and New Delhi, Delhi.
16	NOIDA, Uttar Pradesh.
17	Gurgaon, Haryana.

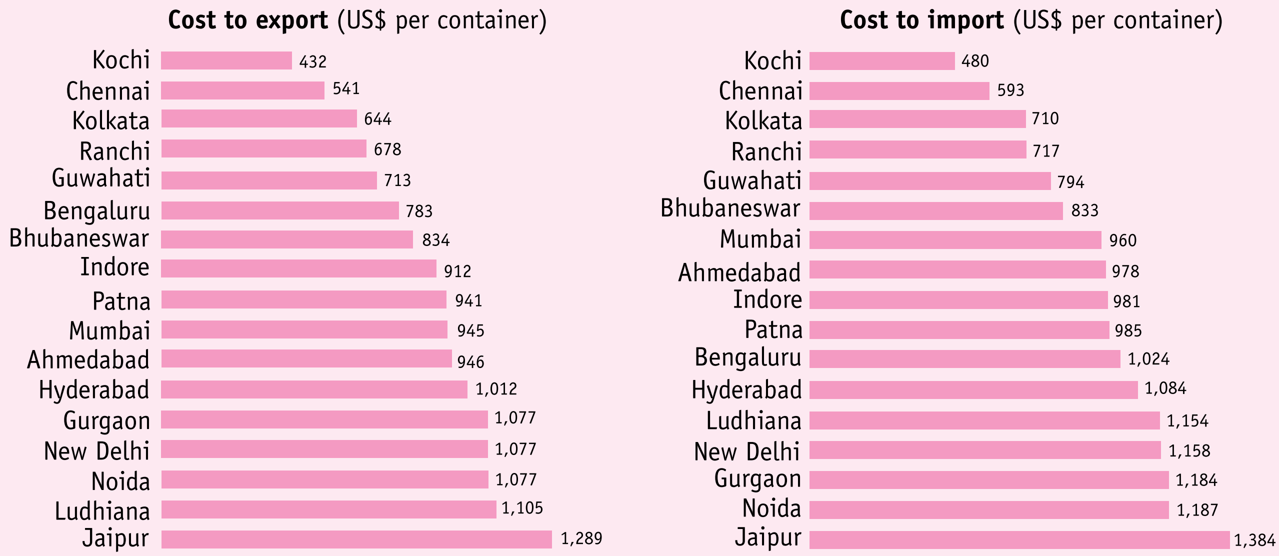
The time taken to export a container of goods from Ludhiana is 21 days, against 22 in Jaipur, and 25 days in Gurgaon, New Delhi and NOIDA. Ahmedabad comes on top with 17 days.

The time taken to import a container of goods is 25 days for Ludhiana, somewhat better than 27 for NOIDA and 28 days for Gurgaon and New Delhi. Bhubaneshwar comes on top with 16 days, while Ranchi comes last with 36 days.

The cost of importing and exporting a container is an important determinant of ease of business. Of all the cities in our list, Ludhiana is the furthest from a port. It comes 16th of the 17 cities with an average export cost of $1,105 per container, and 13th in cost of import at $1,154. Kochi, Kerala and Jaipur, Rajasthan, are the best and worst respectively for both import and export cost. The cost of exporting a container is just $432 in Kochi and $541 in Chennai, but as high as $945 in another port city, Mumbai (see Figure 2.4).

FIGURE 2.4

Cost to Export and Import in India



Source: *Doing Business* database.

Enforcing contracts

Strong enforcement is critical for business. But enforcement is terrible in India. The courts are so slow that most corporations try to settle disputes outside the courts. India is estimated to have barely 10.5 judges per million people, against the global norm of 50. The US has 107 judges per million population, and Canada has 75. Indian judges have to handle almost 4,000 cases each and the backlog of cases is overt one million.

It has barely one policeman per hundred thousand population, half the global norm. Besides, the police are deployed overwhelmingly in security for VIPs and maintenance of public order (India is a land of a thousand demonstrations and riots). Very limited police resources are left for crime detection, or for pursuing cases in courts.

TABLE 2.6

Where Enforcing Contract is Easiest

Rank	*City*
1	Hyderabad, Andhra Pradesh.
2	Guwahati, Assam.
3	Patna, Bihar.
4	Ludhiana, Punjab.
5	Bhubaneshwar, Odisha.
6	Kochi, Kerala.
7	Japiur, Rajasthan, NOIDA, Uttar Pradesh and Chennai, Tamil Nadu.
10	Indore, Madhya Pradesh.
11	Ranchi, Jharkhand.
12	New Delhi, Delhi.
13	Kolkata, West Bengal.
14	Gurgaon, Haryana.
15	Bengaluru, Karnataka
16	Ahmedabad, Gujarat.
17	Mumbai, Maharashtra.

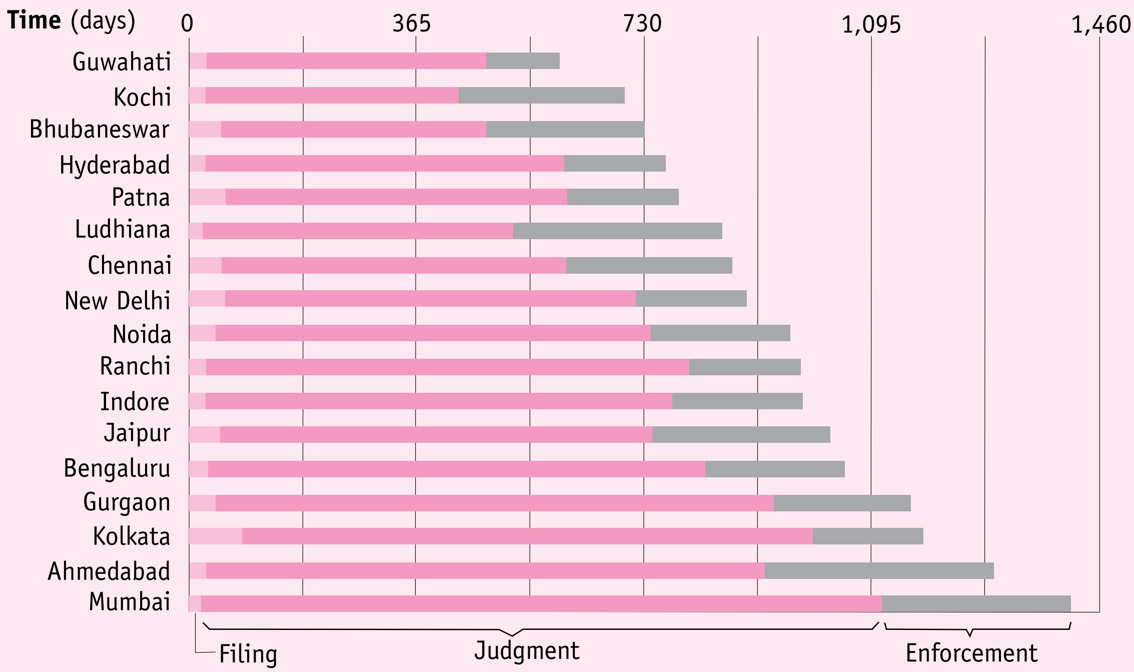
Remarkable, most of India's biggest business centres come at the bottom of this list—Mumbai, Ahmedabad, Bengaluru, Gurgaon and New Delhi. Contract enforcement is, paradoxically, much better in what are often regarded as backward, badly administered states, such as Assam, Bihar and Odisha. Possibly the sheer volume of cases in the advanced, industrialised states overwhelms the judicial process and slows it to a crawl (see Table 2.6).

Ludhiana, Punjab, comes fourth in the list. That sounds good, but in absolute terms it is pretty dreadful. Judgment plus enforcement takes on average almost two and a half years. The fastest in India is Guwahati at 600 days. Mumbai is at the very bottom, at 1,420 days—almost four years (see Figure 2.5).

The cost of enforcing contracts depends on attorney and court fees. Here again the most advanced industrialised states are the worst, while relatively backward states have relatively low costs. Ludhiana comes fourth in this respect, with costs of 20 per cent of a commercial contract. Patna is the cheapest at 16 per cent. Mumbai is the most expensive at 39.5 per cent.

FIGURE 2.5

Lenghty Delays in the Judgement Phase across India



Source: *Doing Business* database.

Ease of closing a business

Capitalism is fundamentally a process of creative destruction. In India, closing a business is so slow and expensive that the normal churning of capitalism is severely hampered. Across the 17 cities, the insolvency process averages 7.9 years and costs 8.6 per cent of the estate's value. The actual amount recovered at the end of the process is a pathetic 13.7 cents in the dollar. In OECD countries the insolvency process takes just 1.7 years, and the recovery rate is five times higher at 68.6 cents in the dollar.

TABLE 2.7

Where it's Easiest to Close a Business.

Rank	City
1	Hyderabad, Andhra Pradesh.
2	Ludhiana, Punjab.
3	Mumbai. Maharashtra.
4	Ahmedabad, Gujarat.
5	Bhubaneshwar, Odisha.
6	Gurgaon, Haryana and New Delhi, Delhi.
8	Bengaluru, Karnataka.
9	Indore, Madhya Pradesh.
10	Chennai, Tamil Nadu and Kochi, Kerala.
12	Guwahati, Assam.
13	Ranchi, Jharkhand.
14	Jaipur, Rajasthan.
15	Patna, Bihar.
16	NOIDA, Uttar Pradesh.
17	Kolkata, West Bengal.

In this respect, Ludhiana comes second in the list of 17 cities. However, no state wants to boast about ease of closure—this is politically not palatable. So Punjab cannot trumpet this as a good reason for businesses to invest there (see Table 2.7).

The overall verdict on Ludhiana is favourable. Despite many shortcomings, Ludhiana's high rank shows that Punjab has made a commendable effort to create a good business climate at the city level. *Caveat*: being the best of Indian cities does not at all mean being good by international standards. India ranks so low on ease of doing business—just 134th of 183 countries—that every Indian city has a long way to go (see Table 2.8).

TABLE 2.8

Ludhina, Punjab: Doing Business

Ease of doing business (rank)	1				
Starting business (rank)	7	**Paying taxes (rank)**	1	**Enforcing contracts (rank)**	4
Procedures (number)	12	Payments (number per year)	59	Procedures (number)	46
Time (days)	33	Time (hours per year)	255	Time (days)	862
Cost (% of income per capita)	48	Total tax rate (% of profit)	67.6	Cost (% of claim)	20
Minimum capital (% of income per capita)	0				
		Trading across borders (rank)	12	**Closing business (rank)**	2
Dealing with construction permits (rank)	7	Documents to export (number)	8	Time (years)	7.3
Procedures (number)	17	Time to export (days)	21	Cost (% of estate)	7
Time (days)	143	Cost to export (US $ per container)	1,105	Recovery rate (cents on the dollar)	15.3
Cost (% of income per capita)	622.9	Documents to import (number)	9		
		Time to import (days)	25		
Registering property (rank)	11	Cost to import (US $ per container)	1,154		
Procedures (number)	4				
Time (days)	67				
Cost (% of the property value)	10.6				

Conclusion, and the Way Forward

Once regarded as India's most dynamic and progressive state, Punjab has slipped relative to other states. It remains reasonably prosperous and fast growing but its growth has dipped below the national average. To regain its place in the sun, its politicians need to abandon old myths about why Punjab is in trouble and face up to some ugly realities. The state needs to tackle its chronic fiscal deficit, something that holds back investment in education, health and infrastructure, and focuses public spending on various unproductive subsidies, the most fiscally crippling of which is free power for farmers. It needs to end perverse incentives that encourage land speculation and push up land prices so high as to make industrial investment uneconomic. It needs to end chronic power shortages and rehabilitate the state's deteriorating transmission system and this cannot be done without charging farmers for power. Agricultural marketing is riddled with controls and needs to be freed from the grip of a trading class with huge political clout.

The positive news is that Punjab has managed to attract private investment in power, so electricity shortages should lessen in coming years. It has also shifted from old public sector monopolies to PPP in health, education and infrastructure, and these promise to improve efficiency and outcomes as well as accelerate investment. Its Right to Service Act is a promising first step in improving administrative efficiency and justice for citizens. Punjab has recently allowed long-term farm leases and this could attract big investments and raise productivity in agriculture. It has a good business climate by Indian standards—Ludhiana is ranked the most business-friendly of the country's top 17 cities. The best recent news is that trade between India and Pakistan looks like getting normalised after decades of bitter hostility and confrontation. Punjab looks like becoming the gateway of Indian trade with Pakistan and that will give its economy a big boost. It needs to build on this.

End notes

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