

# *Occasional Paper*

## **India's Defense Budget: Can It be Reduced?**

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## India's Defense Budget: Can it be Reduced?

*Neeraj Kaushal*

Peter Brook's epic film *Mahabharata* gives a touching portrayal of "civilized war." The battle of Kurukshetra is a civil war between the Kauravas and the Pandavas, cousins of a ruling dynasty. All the kings and the satraps of Bharat, as India was once known, join one or the other of the belligerents. On the appointed day, the two armies assemble face to face. Arjuna, the third Pandava brother, and the most skillful warrior, whose chariot is driven by Krishna, the godman, looks around and sees in front of him an array of grandfathers, teachers, cousins and friends. He lowers his bow and arrow, descends from the chariot and tells Krishna that he would not fight and kill people he had learned to respect, love, and regard as family superiors. After he is convinced by Krishna that in fighting the war he was only performing his dharma, the battle begins. The supreme commanders of the two sides stand face to face, each attended by his aides. Duryodhana, commander in chief of the ruling Kaurava clan declares, "No fighting after sunset, no killing of the poor and the disabled. No killing of women and children." Yudhishtira, supreme commander of the Pandavas, adds, "No hitting below the belt, no hitting when a warrior is in distress, none to be hit in the back." Peter Brook breaks in with a sharp commentary: "this is probably the most civilized war in the entire literature of the world."

Even in that "most civilized" war, countless men were killed and a whole kingdom was devastated. So much so that when the Pandavas won the battle, Yudhishtira, the eldest brother, refused to be crowned king. "What shall I do with a kingdom in which everyone is dead and the kingdom itself lies reduced to ashes."

The concept of "civilized wars" reigned in Europe until the outbreak of World War I, which was the first modern total war and led to a colossal loss of life and property. Within twenty-one years of its end came the far more devastating World War II that ended with the first use—and fortunately the last to date—of two nuclear bombs on Hiroshima and Nagasaki. There was no formal peace treaty to end World War II. As if by a perverse scientific law it extended to half a century of Cold War. An awesome thermonuclear deterrence kept peace at the center of the international system. But three hundred wars were fought in the peripheries, popularly known as the third world. There was no attempt to "civilize" this warfare.

Three of the wars in the peripheries were fought between India and Pakistan, the first two sovereign nations to be born of the historic decolonization process that began as the Cold War consolidated over the political profile of eastern Europe. India and Pakistan did not start an arms race before the India–China border war of 1962.<sup>1</sup> From 1963 onward for almost a quarter century, India furiously armed itself with generous help from the Soviet Union and Pakistan equally furiously, with generous help from the United States and the People's Republic of China. All this was done in the name of peace or defense against war. The South Asian subcontinent remained removed from the pluses of détente and gradual nuclear disarmament that were initiated between the United States and the USSR in the 1970s and reached a significant level of progress in the 1980s.

In the 1990s an unprecedented political earthquake shook the world. The Soviet Union collapsed under the pressure of its many internal and external contradictions one of which was the enormous military expenditure at the cost of meeting the basic consumer needs of its people. The collapse of the Soviet Union brought major changes in international politics that included a significant reduction in the importance of military power and a corresponding increment in the importance of economic power and the emergence of two other powers at the center stage of human affairs: science and technology and information and multimedia. Overarching all this is the emergence of the global market as the new focal point in international relations. This market has spawned a series of relationships varying from

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<sup>1</sup>. Chris Smith, *India's Ad hoc Arsenal: Direction or Drift in Defense Policy* (Oxford: Oxford University Press in association with SIPRI, 1994).

integration of markets and technologies to competition to rivalries. A country's position in the global market is now the real measure of its status as a global or regional power. And it is important to note that military strength is not one of the determining indicators of the emerging new world order.

### Theories of Defense versus Development

The literature on defense *and* development that commanded the field through the 1970s and the 1980s became in the 1990s a literature on defense *versus* development. Here again a caveat has to be entered: the debate on defense and development rages mostly in the developed countries and not in the developing ones. In India, for instance, the mainstream argument is that defense has no contradiction with development; in fact, it helps development.<sup>2</sup> Only recently have scholars and opinion makers tried to show the tensions that exist between high military expenditure and the priority for development.<sup>3</sup> Some have argued that the defense profile can be streamlined with a major reduction in the size of the armed forces by changing their very character and by wiping out a lot of fat and large nests of corruption in defense production and military procurement.

The first study on the impact of defense spending on growth in the post-World War II era was conducted by Emile Benoit in 1973.<sup>4</sup> Based on a sample of forty-four developing countries, Benoit concluded that there was a positive correlation between economic development and defense expenditure in these countries from 1950 to 1965. His study became the Bible for those scholars who have been systematically arguing for high defense expenditure. The study unleashed a series of studies by defense analysts. A group of Massachusetts Institute of Technology (MIT) experts<sup>5</sup> tested the validity of his findings on sixty-nine countries from 1952 to 1970 and arrived at a conclusion that contradicted Benoit's findings. Military expenditure, they found, had a clear negative impact on growth. In the case of India, they found a high correlation between the defense burden and the investment-gross domestic product (GDP) ratio. The relationship between defense burden and agriculture output was negative. Overall, however, a high defense burden was anti-growth.

There were several other studies to test the validity of Benoit's study. Three of the prominent ones were: Deger and Smith's,<sup>6</sup> for the period 1965 to 1973 based on a sample of fifty developing countries; Frederiksen and Looney's,<sup>7</sup> for 1950 to 1965 based on a sample of forty-four developing countries; and Ravenhill's,<sup>8</sup> on thirty-three African less-developed countries (LDCs) from 1960 to 1973. None of the findings of these studies supported Benoit's conclusion. The studies' broad conclusion was that defense siphons away funds from investment and leads to slower growth. In another landmark study, Nicole Ball<sup>9</sup> concluded that higher growth rates in the Benoit study might have been caused by higher bilateral aid and not military expenditure. Ball argued that during the period covered by Benoit the policy followed by many developing countries was to attract foreign investment and aid for development.

Adam Smith, the man who fathered economics, held the view that armed forces were unproductive and did not add value to the national wealth. Subsequently, however, economists chose to ignore defense expenditure. For several of them this was a necessary evil. Theoretically, defense expenditure has both a positive and a negative impact on economic growth. The principal argument for its negative influence on growth is that it siphons away resources from other more productive uses and therefore has

<sup>2</sup>. The strategist, K. Subrahmanyam, has been the leading exponent of this view. See Subrahmanyam, *Defense and Development* (Calcutta: Minerva, 1972).

<sup>3</sup>. For two important recent studies see D. D. Khanna and P. N. Mehrotra, *Defense Versus Development: A Case Study of India* (New Delhi: Indus Publishing House, 1993); Kanti Bajpai and Varun Sahni, "Secure and Solvent: Thinking About an Affordable Defense for India," Paper for Rajiv Gandhi Institute for Contemporary Studies, New Delhi, 1994, RGICS (11).

<sup>4</sup>. Emile Benoit, *Defense and Economic Growth in Developing Countries* (Lexington, Mass.: Lexington Books, 1973).

<sup>5</sup>. Riccardo Faini, Patricia Arnez, and Lance Taylor, "Defense Spending, Economic Structure and Growth," *Economic Development and Cultural Change*, 32 (3) (April 1984): 487-498.

<sup>6</sup>. Deger Saadet and Ron Smith, "Military Expenditure and Growth in Less Developed Countries," *Journal of Conflict Resolution* 27 (2) (June 1983): 335-353.

<sup>7</sup>. Nicole Ball, *Security and Economy in the Third World* (Princeton, N.J.: Princeton University Press, 1988).

<sup>8</sup>. Ibid.

<sup>9</sup>. Nicole Ball, "Defense and Development: A Critique of the Benoit Study," *Economic Development and Cultural Change*, 31 (April 1983): 507-24.

direct opportunity costs in terms of investment, educational and health expenditure, and consumption. Besides, high defense expenditure can cause two types of problems: first, it can pose a heavy burden on the fiscal exchequer. Secondly, if weapons required for defense are imported, a high defense import bill may cause balance of payments problems. However, if the level of aggregate demand in the economy is less than the potential supply, military expenditure can bridge the gap leading to higher employment and improved utilization of capital. But excess reliance on the defense industry can create problems especially if there is no demand for defense production. Evidence: the problems caused by defense cuts on the American economy.

Increased defense spending may also cause inflation that may have both a positive and a negative impact on growth. Inflation may lead to “forced savings” or to increased profitability, which will induce higher investment. On the other hand, expectations of continuing inflation may cause a spending boom, conspicuous consumption, and investment in overseas assets in low priority sectors that have no growth potential. Cross sectional studies reveal no strong bias in either direction.<sup>10</sup>

Proponents of high military expenditure often point to the positive effects of military expenditure on economic growth. They highlight some of the indirect effects of a high defense buildup. For instance, roads built to bolster defense and security have an important developmental role. It is also argued that Research and Development (R&D) in defense has technological benefits for the civilian sector.<sup>11</sup> In most countries including India, however, defense R&D is kept under close security wraps. As a result the products of defense R&D cannot be used by civilians.

Defense experts point out another indirect developmental benefit of high defense expenditure. In countries where high defense expenditure is financed through military aid, it is often garbed in a larger economic aid package. However, military aid like all other types of aid has to be paid back with interest. For instance, in 1984, under its overall policy against Afghanistan, the United States gave Pakistan an aid package of \$3.2 billion for a period of six years that included \$2.4 billion of military aid and another \$800 million of economic aid. There is no evidence that the Pakistani economy improved as a result of the aid.

As an offspring of the Cold War, the debate on defense and development has shifted to defense versus development. The defense versus development argument is now seriously recognized by international institutions: the United Nations, the World Bank, the International Monetary Fund (IMF), and the Asian Development Bank. They all argue that defense should be cut to allow more resources for development. This is something that the international financial institutions did not do during the Cold War. Even now they argue, but do not press the point too much, while disbursing loans to member countries.

Writing about defense and development for the post-Cold War period presents a number of problems to the scholar. First, the literature varies from a clear bias for defense to a searing controversy about the relationship between defense versus development. While in the developed countries the bias has distinctly shifted to development from defense, in the developing countries there is still an overall attempt to justify high levels of military expenditure not only on grounds of security but also development.

### The Indian Case

The literature on defense and development relating to India is very limited in scope and praxis. As already noted, it has an overwhelming bias in favor of high defense expenditure. The bias hinges on three factors: one, threat perception,<sup>12</sup> the image of the enemy, its intentions and capabilities, its international connections and clout. Two, power status, the belief that a high level of military power is necessary to command the deference if not the respect of the smaller neighbors as well as the major

<sup>10</sup>. A. P. Thirwall, “Inflation,” *Savings and Growth in Developing Economies* (New York, N.Y.: Macmillan, 1974).

<sup>11</sup>. Khanna and Mehrotra, *Defense Versus Development*, pp. 137–42.

<sup>12</sup>. Lt. General Matthew Thomas (ret.), “An Analysis of Threat Perception and Strategy for India,” *Indian Defense Review*, January 1990, pp. 61–64.

powers of the world. Three, that a high defense profile also means development of frontier military technologies like space, satellite launchers and missiles and nuclear.<sup>13</sup> It is argued that these technologies will have a spin off impact on high industrial technologies, particularly electronics, computer sciences, and telecommunications.

Since the mid-1960s, India enjoyed some special advantages in building its defense profile. The first advantage was a very close treaty-bound relationship with the USSR. Moscow provided three commitments to India that secured India's status as a regional power in South Asia. The first was to supply India the bulk of its sophisticated military equipment, particularly for the air force and the army and later for the navy, on rupee payment that did not touch India's relatively poor forex earnings. The second was that in the case of a war with Pakistan or China, the Soviet Union would stand fully behind India with military support. The third commitment was that India would get political and diplomatic support especially in the UN Security Council where the Soviet veto could protect India from unacceptable political or security damage.

With the advantage of Soviet commitments, India's defense expenditure went up significantly after the 1962 border war with China. The government claimed that it did not hurt the Indian economy because the payment for the acquisition of sophisticated hardware was made in rupees. Some Indians raised the question of an unfavorable rupee-ruble exchange rate and argued that the economy was losing heavily in the long run. But the official position that the defense arrangement with the USSR was very much to India's advantage had almost complete national acceptance.

It was only in the late 1970s when the Janata party came to power that procurement of weapons was diversified. From then on through the 1980s there was diversification with the government buying Jaguar fighters from England, several modern submarines from Germany, and Mirage 2000 fighter-bombers from France. However, even when the Cold War ended India was getting 70 percent of its defense equipment from the USSR (now the republics of the Commonwealth of Independent States (CIS) especially Russia, Ukraine, and Belarus) and the former communist regimes in Eastern Europe, particularly Czechoslovakia. It was only when the Soviet Union broke up and no spares for the Russian military equipment were available (despite consistent governmental commitment from Russia and Ukraine) that India faced a major problem in meeting its defense expenditure from a relatively poor hard currency kitty.

During the 1980s India embarked upon an unprecedented spree of acquiring conventional weapons. Its defense budget increased by 50 percent from 1983 to 1987. In the following year, the defense bill rose by 23 percent. In 1987, one-fifth of the arms exported to third world countries were sold to India.<sup>14</sup> According to the Human Development Report, from 1987 to 1992, India was the largest importer of conventional weapons. Of the total import bill during this period, 15 percent or \$18.7 billion went into the purchase of conventional weapons.

This military power was demonstrated in the region in a manner that, in Indian eyes, confirmed India's status as the regional superpower. Others saw it as a regional super-bully. During this period India sent peacekeeping forces to Sri Lanka and Maldives at the explicit request of the presidents of the two countries. Indian military forces were also engaged in large-scale military exercises—Brasstacks—in Rajasthan and Punjab in 1986–87 that bordered on brinkmanship with Pakistan. Later in 1987 the Indian armed forces held another series of military exercises—Checkerboard—that almost led to a confrontation with China along the disputed India–China border in the northeast.

When Mikhail Gorbachev visited Delhi in 1986 he made it clear that in a future war with China, India could not count on the Soviet Union. This led to the most extensive and in-depth reviews of the dynamics of the Indo–China–USSR relations to be undertaken by any government in Delhi and, after the high border tension of 1986–87, to purposeful improvement of relations with China. Two

<sup>13</sup>. Nicole Ball, *Defense and Development*.

<sup>14</sup>. United Nations Development Program, *Human Development Report*, 1994 (New York, N.Y.: Oxford University Press, 1994).

unprecedented peace initiatives were undertaken by India in the next five years. First, during his visit to Beijing in 1988, Prime Minister Rajiv Gandhi told the Chinese leaders that the border was negotiable, a point that the then Prime Minister Jawaharlal Nehru had stubbornly refused to concede to Premier Zhou Enlai, when the latter had visited Delhi in 1960. And, second, on his visit to Beijing in 1993, Prime Minister P. V. Narasimha Rao conceded the interim validity of the Line of Actual Control pending a negotiated settlement of the Sino-Indian border.

Along with these agreements a series of confidence-building measures were taken in the Northeastern frontier between China and India including mutual withdrawal of troops to a certain limited distance from where they had been positioned, regular communication among the field commanders to prevent any incident that might trigger a deterioration of the situation, an agreement to define the line of control with modern cartography, and continuing discussion for a settlement of the border issue. The result has been India's ability to transfer three divisions of troops from the Northeastern frontier with China to other areas, particularly the Western front with Pakistan.

Subsequent annual reports of the Defense and External Affairs ministries since 1989-90 have discarded references to a Chinese threat and have mentioned progressive relaxation and improvement of Sino-Indian relations. However, this did not lead to a decline in defense expenditure. In fact, Beijing's nuclear capabilities have been used by the Indian strategic community to keep alive a potential threat from China and to argue that India must have missile power as well as a nuclear option to deal with a possible conflict with the Chinese. This argument is used when Indians talk to the United States on nuclear or missile issues and recent U.S. statements (by the Deputy Secretary of State Strobe Talbot and Senator George Mitchell, leader of the Democratic Party in the Senate) indicate that the United States recognizes the legitimacy of India's long-term security concern with China.

The threat perceptions of Pakistan remain as dark as ever, significantly darker in view of Pakistan's involvement on behalf of the insurgents in Kashmir with weapons, mercenaries, and political and diplomatic support in international fora. Half a million Indian troops guard the Indian borders in Kashmir and Punjab.<sup>15</sup> Minimum confidence-building measures have been taken to prevent an accidental war but the threat perceptions remain very high. Pakistan's procurement of missiles from China argue strongly for a viable and superior Indian missile program. The recent plan of the United States to transfer F-16 aircraft to Pakistan (in exchange for some unspecified capping of the Pakistani nuclear program) has revived the perception of the United States as the provider of Pakistan's military power. The fact that the F-16s can be used only against India and that they have a comparative edge over any Indian aircraft and can be used to deliver nuclear weapons, further strengthens these Indian threat perceptions. There are reports in the Indian press that Pakistani intelligence operatives are helping insurgencies in the small states on the Indian Northeastern border: Nagaland, Manipur, and Mizoram.<sup>16</sup> "As a result, there is a crescendo of public demand, articulated particularly on the floors of Parliament, that India maintain an adequately high level of effective and operational military power.

The government of Prime Minister P. V. Narasimha Rao has responded to this demand by increasing military expenditure in its successive four budgets. India's defense expenditure, going by the Budget of the Government of India, rose by 46 percent from \$5 billion in 1990-91 to \$7.3 billion in 1994-95, with the defense budget increasing by a steep 20 percent in 1994-95 alone. After discounting for an expected rate of 8 percent inflation during the year, this accounts for a 12 percent increase in defense spending. This is a sharp reversal of a trend set in since 1990-91. After a steep rise from \$2.5

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<sup>15</sup>. The exact number of troops operating in Kashmir is not known. No official figure is given. Most Indian reports speak of half a million troops being deployed. According to Pakistan Prime Minister, Benazir Bhutto, there are 600 thousand Indian troops in Kashmir. On the other hand, a report in the New York Times in May spoke of about 400 thousand soldiers, border troops, and parliamentary police. For Mrs. Bhutto's statement see *The Statesman*, 28 June 1994. See also John F. Burns, "Rebels in Kashmir and Indian Army Ready for Long Fight," *New York Times*, 16 May 1994. According to Burns, by western estimates there are 15 thousand "active rebel fighters divided into several rival groups." He also quoted Indian commanders and guerrilla leaders for casualty figures—10 to 20 thousand fighters and civilians killed.

<sup>16</sup>. A. R. Wig, "ISI Targets Punjab, Himachal," and Shekhar Gupta and Pathak Rahul, "Exporting Terror," *India Today*, 15 May 1994.

billion in 1985–86 to \$5 billion in 1990–91, defense expenditures rose rather moderately in the following two years. After discounting for inflation there was, in fact, a modest fall in real terms.

### Realistic Assessment of Indian Defense Expenditure

The defense budget of the Indian government does not present a true assessment of the country's defense expenditure. It does not include several items of expenditures that should normally be regarded as part of the country's defense effort. Four major items of defense expenditures *excluded* from the defense budget are:<sup>17</sup>

- defense pensions;
- expenditures incurred by the Ministry of Defense;
- expenditures incurred by the Home Ministry on various paramilitary forces such as the Border Security Force, Indo–Tibetan Border Police, Assam Rifles, and Indo–Bangladesh Border Works, adding up to a million men in arms; and
- elements of the space and nuclear programs that relate to military, and some items under the heading “strategic electronics” such as radar research that fall within the expenditure of the department of electronics. However, it is difficult to ascertain what proportion of these allocations actually go into defense.

Table 1 shows that in 1994–95 the Indian government plans to spend at least 20 percent more than what is claimed in the Union Budget. The estimate does not include nuclear and space related defense expenditure. This compares well with the estimate for “extra defense expenditure” calculated by Sandy Gordon for 1991–92 at \$1 billion, which works out to 20 percent of the defense expenditure. His estimate, however, includes part of the nuclear and space related defense expenditure. In other words for every dollar that the central government spends, 18 percent is allocated for defense in 1994–95.

Can the economy afford such a high defense bill? Not in the long run. A high defense bill creates two types of problems for the Indian economy. One, it imposes a high burden on the exchequer that could result in a fiscal crisis. For instance the high defense debt in recent years had a significant bearing on the fiscal crisis of the late 1980s and early 1990s. From 1990–91 to 1992–93, the fiscal deficit in proportion to GDP was reduced from 8.4 to 5.8 percent partly by reining in the growth in defense expenditure that actually fell by around 5 percent in real terms more than in 1992–93. And now with the revised defense expenditure rising by 23 percent in 1993–94, the fiscal deficit has also climbed to 7.3 percent (see Table 2).

Second, high defense expenditure may cause a balance of payments crisis. Unfortunately, the government does not publish the hard currency expenditure on defense. In recent years, as mentioned

Table 1: Defense Expenditure: A Realistic Estimate

	1992–93	1993–94	1994–95
Defense expenditure (based on the budget)	\$560 (R)	\$685 (B)	\$733 (B)
Defense pension	\$75 (R)	\$81 (R)	\$86 (B)
Table 2 of Ministry of Defense	\$5 (R)	\$8 (R)	\$8 (B)
Expenditure on paramilitary forces excluding central reserve police	\$39 (R)	\$48 (R)	\$50 (B)
Total defense expend (excluding nuclear and space related defense expenditure)	\$682	\$802	\$878 (B)
1988–89	11.4	11.4	11.4
1989–90	17.4	7.8	7.9
1990–91	17.4	7.8	7.9
1991–92	9.2	3.4	3.7
1992–93	9.2	3.4	3.7
1993–94	7.5	5.8	5.8
1994–95	7.5	5.8	5.8
1993–94	22.3	7.4	7.4
1994–95	7.0	6.0	6.0

Source: Union budgets and economic surveys for various years.

earlier, India has emerged as a major importer of conventional weapons. From 1987 to 1992, India was the largest importer of conventional weapons, which ate a quarter of the country's foreign exchange earnings. A significant portion was imported from the former USSR under the Indo-Soviet Rupee agreement. Assuming that 60 percent of this was imported under that agreement, the hard currency imports would still work out to \$7.5 billion for the five year period. Sandy Gordon has estimated that the hard currency defense imports rose from 8 percent of the defense expenditure in 1981-82 to 12 percent in the second half of the 1980s. With the defense expenditure also rising during this period, the total defense burden on the foreign exchange reserves increased significantly, precipitating a crisis. By the end of 1990, the hard currency reserves were not enough to buy even two weeks' imports.

### Defense and the Foreign Exchange Crisis

However, throughout the 1980s the government underplayed the impact of defense imports on the balance of payments. Until recently, the Government of India did not publish its defense debt figures. It was a closely guarded secret of the Ministry of Defense and the Ministry of Finance. Because defense imports were often made on credit, they secretly burgeoned the debt burden. The actual size of the country's defense import bill was also not published. Although such major defense items as Mirage and Jaguar fighters (by independent estimates, the two alone must have cost the government \$5.8 billion),<sup>18</sup> Harrier VSTOL, and the Bofors guns were imported in the second half of the 1980s, no one knew what they cost. As most defense imports do not enter through customs, the customs accounts did not have any estimate of defense imports either. The first signs of the huge defense import became visible when the gap between the import figures published by the Reserve Bank and those of the Commerce Ministry ballooned. The government initially tried to ignore the issue by saying that the gap was primarily because of the time lag between physical imports and deferred payments. But the gap continued to grow over the years. From \$500 million a year in the first half of the 1980s, the gap increased to \$4 billion in 1990. The gap was \$14.2 billion during 1985-86 and 1989-90 and a significant proportion of it was because of defense imports. It was only in 1993 that Reserve Bank Governor, Chandrashekar Rangarajan,<sup>19</sup> in a report on Balance of Payments placed part of the onus of the foreign exchange crisis on the arms imports during the second half of the 1980s. He suggested that defense loans with payment obligation of more than a year should be formally registered as commercial debt. Those that have to be paid back in a year or less should be registered as trade related debt.

According to the latest estimates, 11 percent of the total debt of \$90 billion is on account of defense debt. Table 3 gives a breakup of the defense debt and its repayment pattern.

In 1994-95 the hard currency import bill is expected to be high. The purchase of sixty-six advanced jet trainer aircraft alone is going to be around \$2 billion. To this should be added the foreign exchange requirement of the radar program of Bharat Electronics and the foreign exchange requirement of the Light Combat Aircraft and Advanced Light Helicopter. Defense imports from the CIS republics will also have to be paid for in dollars or other hard currencies. Last year, India bought defense spare parts from Russia worth \$800 million.

Table 3. Defense Debt

	<i>Defense Debt</i>			<i>Total Debt</i>
	<i>Russian</i>	<i>Dollar Component</i>	<i>Total</i>	
1990	9.9	2.3	12.2	75.9
1991	11.6	2.0	13.6	83.9
1992	9.2	1.6	10.8	85.3
1993	9.2	0.9	10.1	90.4

*Notes:* Defense debt to Russia payable through exports.

*Source:* *Economic Survey*, Ministry of Finance, India.

<sup>17</sup>. Sandy Gordon, "Indian Defense Spending: Treading Water in the Fiscal Deep," *Asian Survey*, XXXII, (10) (October 1992); also see B. G. Verghese, "Getting More With Less," *Indian Express*, 10 March 1989.

<sup>18</sup>. Raju Thomas, *Indian Security Policy* (Princeton, N.J.: Princeton University Press, 1986).

### Potential for Trimming the Defense Budget

The growing defense import bill and the overall defense bill, raises a significant question: is it possible to reduce the defense budget without compromising the security needs of the country? To answer this question we need to first take a close look at the various components of the defense budget.

About a third of the defense budget is spent in paying wages and salaries to both the armed forces and workers in the ordnance factories and those in the public sector producing defense equipment. A significant proportion of this goes into paying salaries and allowances to the 1.2 million strong army, the fourth largest in the world. There is considerable flab in all the three armed forces. For instance, the Indian navy's uniformed strength is supported by an equal number of civilian employees. The average sailor-per-ship ratio in most Western navies is three hundred. In the India navy it is four hundred and fifty. Admiral J. G. Nadkarni<sup>20</sup> has suggested that the size of Indian armed forces could be cut down by 25 percent across the board without affecting the country's combat ability. That's a clean \$637.6 million saving in the defense bill. Indeed, this cannot be done overnight. But it is important to change the recruitment policy in the three forces keeping the above in mind.

In the present recruitment policy, the maximum working life of a soldier is seventeen years, although he draws a pension for an average of at least thirty years. Among officers the maximum service life is twenty-seven years. An officer's average service life, on the other hand, is seventeen years, but for that they get a pension for at least thirty years. To reduce the pension bill Lt. Gen. M. L. Chibber<sup>21</sup> is among those who have suggested compulsory military service for five to fifteen years for officers in various organizations under government control such as banks, public sector, joint sector undertakings, Central government services, railways, port, and telegraph departments. He has also suggested three years of compulsory service for engineers and doctors that would partly act as payment back to the society for the subsidized education they receive.

There is also a significant potential for reducing the work force in thirty-nine ordnance factories and in public sector undertakings that produce defense related goods. The two together hire around 283,862 workers. Ordnance factories alone hire 176,415 workers.<sup>22</sup> The salaries of these workers doubled during 1986–87 and 1990–91 because of overtime payments without any significant improvement in the quality or level of production.

Ordnance factory workers are overpaid for the work they do; they cheat on the equipment they procure. There are reports<sup>23</sup> that the central government incurs an annual loss of \$16 million because of the irregularities in procurement that is done under selective tenders instead of open tenders. Procurement of zip fasteners worth \$3.2 million a year is done on the basis of a single tender although there are seven other manufacturers in the country. There is a cartel of manufacturers supplying jersey and socks yarn. To avoid competition each quotes the same rate so that the quantity of the order is divided among them. As a result, the ordnance factories supply a pair of socks at \$1.28. The same can be had at \$0.63 a pair in the market. A jersey that is produced for \$6.38 can be bought in the market for a price of \$3.10.

There are dealing agents for each procurement. They pocket around 10 to 15 percent of the margin. The ordnance clothing factories charge army headquarters \$8 for a blanket that can be bought at \$5 in the market. Army headquarters incur a loss of \$319,000 on the purchase of durries (rough carpets) that are sold by the ordnance factories to the military at \$5 a piece. In contrast, the market price of these durries is a mere \$2 per piece. Merely permitting the Indian service headquarters to buy from the open market and exposing the ordnance factories to competition will bring significant cuts in the defense

<sup>19</sup>. Report of High Level Committee on Balance of Payments (Reserve Bank of India, April 1993).

<sup>20</sup>. Admiral J. G. Nadkarni (ret.), "Straight Talk on the Defense Budget," *Defense Today*, 1 (1), New Delhi (August 1993).

<sup>21</sup>. Lt. Gen. M. L. Chibber, PVSM, AVSM (ret.), "Military Leadership to Prevent Military Coup," *Lancer International*, (1986): 200–201.

<sup>22</sup>. Defense Force Levels, Manpower, Management and Policy, Nineteenth Report (Estimates Committee, 1992–93).

<sup>23</sup>. Atul Chandra, "Ordnance Factories Milking Exchequer," *Pioneer* (18 October 1992); also see Pravin Sawhney, "Answer in Arun Panel Report," *Indian Express*, 21 December 1992.

bill. The Director General of Ordnance Factories takes away about 28 percent of the defense budget allocated to the army and that amount can be reduced by at least a quarter by checking malpractice in procurement by the Ordnance factories. In fact, some of the ordnance factories are run so inefficiently that the Arun Singh Committee on Defense Expenditure<sup>24</sup> recommended the closure of five of them. So far, however, no action has been taken. Some of the other suggestions made by the committee to cut down the defense expenditure are:

- close down low technology defense factories such as those producing clothing because there is enough capacity in the private sector to produce these goods at cheaper rates;
- review the functions of the Director General of Ordnance Factories to see if the organization can be broken into groups according to the products they produce; and
- have the project reports of the director general of Ordnance factories prepared by independent consulting organizations to reduce the chances of inflated cost projections.

The recommendations have not been implemented so far.

The main problem with ordnance factories is that they are not run along commercial lines. Recent cuts in arms orders have slashed their use capacity to 40 to 60 percent in major production lines including tanks, ammunition, and artillery guns. Despite over capacity and surplus manpower, it is ironic that ordnance factories pay between \$15.9 million to \$28.7 million in overtime to workers every year.<sup>25</sup> Another factor that keeps the price of ordnance factory products high is that they have to keep the import content in their production down to less than 20 percent. Foreign exchange content of defense items produced by the defense public sector undertakings are not so low.

Supplying arms and maintenance items at high prices is not the exclusive preserve of the ordnance factories. Public sector undertakings do the same. Evidence supplied by the Arun Singh Committee shows that binoculars that can be bought at \$108 each from the private sector were acquired from the public sector at \$236, more than double the listed price.

During financial year 1994–95, \$2.2 billion, (44 percent of the defense revenue expenditure) has been earmarked “stores” to cover the replacement of worn out items, maintenance of weapon systems, and other maintenance items. About 40 percent of the expenditure on stores is used up in the payment to the ordnance factories. Prudence in procurement from ordnance factories can reduce defense expenditure by at least 10 to 15 percent or between \$318.8 million to \$478.1 million. Prudence in the procurement from the public sector will reduce the defense bill by another \$127.5 million to \$223.1 million. In line with the liberalization policy of the government, defense production should be thrown open to the private sector and procurement by the military should be based on open tenders.

The scope for prudence in the procurement of arms from abroad cannot be exaggerated. Arms purchases are mostly controlled by nonmilitary finance personnel and bureaucrats. The secrecy shrouding procurement, the protection given to loss-making resource devouring defense production units and the whole atmosphere of secrecy that blankets defense in India creates nests of corruption among bureaucracies, suppliers, procuring agencies, and politicians.

It is well known that defense import deals involve huge kickbacks, therefore, there is a vested interest in defense related imports. Many experts, including former vice chief of the Air Staff Air Marshal S. Raghavendran,<sup>26</sup> believe that the Indian air force does not need an advanced jet trainer that would cost \$2 billion. The indigenous trainer, Kiran, is sufficient for the existing needs of the air force, they insist. But there are reports that the government has already struck a deal for the British Aerospace Hawk.<sup>27</sup> The Government has spent more than \$510 million to produce the first two prototypes of the Light Combat Aircraft (LCA).<sup>28</sup> But no plane is likely to be in sight for the next two years. In fact, the Defense Research and Development Organization (DRDO) is now looking for an international

<sup>24</sup>. Ibid.

<sup>25</sup>. Defense Force Levels.

<sup>26</sup>. Swaminathan S. Anklesaria Aiyar, “Stop the \$2 Billion Scam,” *Times of India*, 24 January 1993.

<sup>27</sup>. Saritha Rai, “Wanted: A Foreign Match,” *India Today*, 31 January 1994, pp. 34–36.

<sup>28</sup>. “Defense Expenditure: Facts and Fancy,” *Economic and Political Weekly*, XXIX (12) 19 March 1994, pp. 662–663.

partner because it doubts that the indigenous LCA can be produced without foreign help. The project is expected to cost around \$1.6 billion. Several experts have suggested that India should abandon this project. No country can afford to produce a fighter aircraft without a guaranteed international market, which India does not have at the moment. The French have failed to produce Mirage 4000 and Rafale fighters, and the Israelis have decided not to go ahead with the Lavi because they do not see a guaranteed market. Will India learn from the French and the Israeli examples?

Indeed, the country can do without a LCA or an Arjun Main Battle Tank (MBT). These are projects expected to enhance “national prestige” more than anything else. The production of the Arjun MBT was cleared twenty years ago in 1974 with an outlay of \$4.9 billion. In 1987 the Cabinet Committee on Political Affairs increased the budget by almost eighteen times to \$89.5 billion, of which \$32.6 billion would be on imports. An *Indian Defense Review* (IDR) Research Team in a critical assessment of the Arjun MBT found that in the past twenty years not even a prototype or a “reference tank” has been produced.<sup>29</sup> Only twelve “models” have been produced. The research team concluded that the tank would not enter service before 1995, by which time the costs will go up even further. The quality of idler wheels, bogie wheels, track links, nuts and bolts, and rubber seals used in the models is extremely poor. An indigenous engine for the tank “has been under development for a decade.□□□ Since we have not been able to make a breakthrough, M/s AVL of Austria were hired for consultancy. What will come out of it is anyone’s guess.” There has been a steep hike in the expenditure on defense R&D, which now accounts for 4.5 percent of the total defense expenditure. Most of the R&D money has actually gone into the LCA and Helicopter projects, the Gas Turbine Engine projects, and the Arjun MBT projects. The outcome of this expenditure is still not visible.

### Conclusion

Significant cuts in defense expenditure—both revenue and capital—are possible even in the present threat environment. Several Indian specialists have suggested measures that can improve the operational efficiency of the armed forces while cutting down substantially the country’s military expenditures. These suggestions can be classified into three categories: (1) the reform and reorganization of the armed forces; (2) the comprehensive overhaul of the exceedingly wasteful defense production apparatus; (3) the entry of the private sector into defense production; and (4) the abandonment white elephant projects that have eaten up enormous resources over the years without producing any weapons. These four together can save the government and the economy between \$1.3 to \$1.6 billion a year, a good 20 to 25 percent of the defense budget. Even with the present size of the armed forces, the defense expenditure can be reduced by \$637.6 million to \$956.3 million.

The level of defense expenditure is always justified on threat perceptions. In India’s case the threat perception comes more loudly from Pakistan, but in real terms more from China. Confidence-building measures have been adopted between India and both of its neighbors. However, these are working more successfully with China than with Pakistan, and agreements such as no attack of each other’s nuclear installations do not actually touch upon the defense budgets. In any case the two countries are not running a nuclear arms race—perhaps they have the capability to make nuclear weapons, perhaps the capabilities have been capped. The military budgets actually relate to conventional weapons, particularly high-tech and highly expensive weapons imported from external sources. This essay has argued that it is possible to save in most areas of conventional weapons. I would like to conclude by suggesting that the mutual reductions of defense budgets will in itself be an effective confidence-building measure, more so if the reductions are agreed upon by both sides, but unilateral reductions will also contribute to confidence building.

We began this essay with reference to “civilized war.” That will never return—war has become increasingly devastating and expensive. Therefore, open warfare has been replaced by low intensity conflicts and guerrilla wars on a global scale. It is all the more necessary, therefore, to reduce military expenditure and control and reduce weapons of mass destruction, both as a measure of security and confidence building. India will then be joining the global process of disarmament and arms control.

<sup>29</sup>. IDR Research Team, “India’s Main Battle Tank: Arjun—Part II, A Critique,” pp. 179–188.