

Foreword

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India embraced democracy first and capitalism afterwards, and this curious reversal explains a great deal about us. India became a democracy in 1950, with universal suffrage and extensive human rights, but it was not until 1991 that it opened up to a freer play of market forces. In these forty-one years the pressures to redistribute the pie won out over the pressures to bake it. By 2004, when this book is being published, we have experienced a dozen years of slow incremental economic reform during which we have gradually dismantled some of our damaging socialist institutions. Yet a vast agenda remains before we can call ourselves a robust capitalist democracy. Moreover, an election is approaching again, and we find that the leaders of both our main political parties are still reluctant to campaign on a platform based on liberal economics reforms. They seem convinced that any defence of capitalist institutions is a sure road to political failure.

Our animus against capitalism may have diminished after communism's fall; increasingly, some Indians may also agree that markets do indeed deliver greater prosperity; but most Indians still think that capitalism is not a moral system.

Hence, this book is timely. We have already tasted significant benefits of competition in recent years; we have also experienced enough economic liberty for a decade to be more receptive to the ideas of this book.

Since capitalism is not perceived to be moral, most people think that morality must somehow depend on religion. This is a mistake, and greater reflection will show that human self-interest will go a long way to ensure good behaviour in the marketplace. A seller who does

not treat his customers with fairness and civility will lose market share. A company that markets a defective product will get a bad reputation and will lose customers. False claims will lower sales. A firm that does not promote the most deserving employees will lose talent to its competitors. A purchase manager who does not buy at the right price will soon make his company uncompetitive and it will not survive. Lying and cheating will ruin a firm's image, making it untouchable to creditors and suppliers. Hence, the free market does offer powerful incentives for ethical conduct, backed by state institutions that enforce contracts and punish criminal behaviour. The idea that one needs to appeal to religion for morality is wrong.

If the market is based on an inbuilt morality, why are there so many crooks in the marketplace? I think the answer is that in every institution and in every society there is a natural distribution of crooked people, and the market has its share. This is why we need effective policemen and judges. Liberal institutions, however, are able to prevent bad behaviour because of the way they are designed, and when they cannot deter crooks they can catch them efficiently without harassing the rest of the population.

Some Indians believe that capitalism has come to us from the outside. Others think that the imperial West has forced it on us. This too is a mistake. Friedrich Hayek, the Noble laureate, pointed out that the market economy is a spontaneous order.¹ It is natural for human beings to exchange goods and services, and every society has evolved money, laws, conventions and morals, which guide behaviour in the marketplace. Most of our moral and social rules are thus the natural product of human endeavour and were not created by God. Although religion remains a powerful force in the world, human beings everywhere have found ways to behave and conduct themselves based on shared *human* values.

Morality in the marketplace, thus, begins with idea of freedom—the freedom of the individual to choose to buy or sell any product that he or she wishes too; it also includes the freedom of the individual to work or get a job where his or her talents or inclinations might lead. While there is freedom, there is also competition in the market

1. Friedrich Hayek, *Law, Legislation and Liberty*, volume 1, Chicago: University of Chicago Press, 1973, 17.

for the best products and the best individuals. If the ability to compete is important in the market economy, so is the ability to cooperate with fellow employees and other associates. Teamwork and cooperation are vital since one is so inter-dependent in modern enterprise. David Hume pointed out that even two farmers who do not particularly like each other learn to cooperate when it is in their interest to do so.²

Part of the reason, I am convinced, why capitalism is so disliked lies in linguistic confusion. Many in India and elsewhere glibly equate capitalism with selfishness. However, when Adam Smith wrote about self-interest he had in mind ordinary people going about making sensible decisions in their day-to-day lives. When I go out to buy bananas, for example, I naturally want the best quality at the lowest price. This is not being selfish; it is merely being self-interested. In buying and selling each person gains by benefiting others, and an “invisible hand”, to use Adam Smith’s famous phrase, ensures that everyone gains from self-interested behaviour. A selfish person, on the hand, is not morally neutral—he promotes his interest at another’s expense, and that is wrong.

People are suspicious about capitalism partly because they mistake “self-interest” for selfishness. Self-interest is not a social attribute and can be practiced in solitude on a deserted island. For example, if it rains, I will carry an umbrella—nothing selfish about that. Selfishness is a social attribute, on the other hand, and a selfish person often transgresses on the rights of others. Friedman wrote that self-interest is the pursuit of whatever is in one’s interest—a scientist pursues science, a doctor pursues medicine, and an artist pursues art.³ There is nothing selfish in that, which is why Adam Smith called it rational self-interest. In the *Theory of Moral Sentiments*, he said that what is *rational* is not only from the viewpoint of the person involved but also from that of a disinterested rational observer. “We endeavour to examine our own conduct as we imagine any other fair and impartial spectator would examine it,” he wrote. “To feel much for others and little for ourselves...to restrain our selfish, and to indulge our benevolent affections constitutes the perfection of human nature.”⁴

2. David Hume, *A Treatise on Human Nature*, ed H. Aiken, New York: Macmillan, 1948, 612.

3. Milton and Rose Friedman, *Free to Choose*, New York: Harcourt Brace Javanovich, 1980, 27.

4. Adam Smith, *The Theory of Moral Sentiments*, Indianapolis: Liberty Classics, 1969, 204.

Finally, my social activist friends, many of whom work in non-government organisations in India, do not tire of reminding me about the social responsibility of business. Some of the essays in this book address this very question. I still believe that Milton Friedman had the last word on this issue in his brilliant essay in the *New York Times*. I agree with him that the only social responsibility of business is to increase its profits. I believe that the employees of the company have a contractual duty to the shareholders of the firm to maximise financial returns or shareholder value. For them to use company resources to advance social goals on behalf of the poor, or of art, or of any laudable philanthropic cause is wrong. They would be, as Friedman says, going beyond their mandate to engage in commerce, and they would be engaging in the political function.

Having said that, it is laudable when individuals engage in philanthropy and exercise their social responsibility as individuals. Hence, it is important not to confuse the actions of the corporation and of individuals. We ought to rightly applaud Bill Gates when he decides to give away most of his fortune to worthy causes, but we ought to be critical if Microsoft were to do that, and it would be tantamount to theft against Microsoft shareholders.

We live in a liberal age, and whether we like it or not, India is headed in the direction of some sort of democratic capitalism in the 21st century where our future will be one of competition and decentralisation. Our challenge is to put in place liberal institutions, which will have the direct consequence on day-to-day governance. This is precisely the agenda of the economic reforms. If we keep reforming, then we face the very real prospect of conquering the pervasive poverty that has characterised the lives of the majority of the people in the past. We have, thus, good reasons to expect that the lives of the majority of Indians in the 21st century will be freer, more humane and prosperous than their parents' and grandparents' lives. Never before in recorded history have so many people been in a position to rise so quickly.

5. Milton Friedman, "The Social Responsibility of Business is to Increase its Profits", *New York Times Magazine* 1 September 1970. Reprinted in Tom Beauchamp and Norman Bowie ed, *Ethical Theory and Business*, Englewood Cliffs, NJ: Prentice Hall, 1993.