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EDITORIAL ANALYSIS

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CONSISTENT COMPREHENSIVE AND CREDIBLE

UNIQUE AND BEST IN QUALITY

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Indonesia's model of inclusion is a lesson for all

Its inclusive nationhood stands out even as the idea is under threat globally with the rise of Right-wing populism. The idea has survived democratic backsliding and blasphemy laws

Sameer Arshad Khatlani

Prime Minister Narendra Modi visited the 10th-century Prambanan Temple dedicated to Hindu gods Brahma, Vishnu, and Shiva, on the last day of the Indonesian leg of his three-nation tour of the Indo-Pacific region. He called the temple a testament to the close cultural ties between India and Indonesia. A day earlier, Modi addressed the Indonesian parliament and said that the relationship between the two countries is rooted in local versions of the Hindu epics, *Ramayana* and *Mahabharata*, and monuments such as Borobudur, the world's largest Buddhist temple, around 50 km from Prambanan. He referred to Indonesia's national emblem, Garuda, which is Lord Vishnu's mount in the Hindu tradition.

Modi spoke about traders and Sufis from his home state of Gujarat, who brought the message and values of Islam to Indonesia, the world's most populous Muslim nation and home to roughly one in eight Muslims worldwide. He highlighted aspects of Indonesia, the world's third-largest democracy and Southeast Asia's largest economy, that are not spoken about as much as they should be.

Indonesia is among the most underestimated countries. Its inclusive nationhood stands out even as the idea is under threat globally with the rise of Right-wing populism. The idea has endured despite democratic backsliding and blasphemy laws, which the US Commission on International Religious Freedom has described as a religious freedom violation and prone to misuse against minority groups. It is based on sound foundational principles, *Pancasila*, such as humanitarianism, democracy, and social justice. Indonesia is a refutation of many Orientalist tropes and generalisations dominating the discourse around Islam.

The coexistence of Islam, democracy, and pluralism in Indonesia is based on concepts such as *Ummatan Wasatan*. A Quranic term, *Ummatan Wasatan*, literally means the middle community of moderation and balance. Indonesia has embedded *Wasatiyyah* — Islamic moderation — in national identity, education, and governance. The concept is promoted through premarital counselling programmes, etc and is part of Islamic studies in Indonesia, with a special focus on critical thinking, mysticism, Islamic cultural history, and reform.

Indonesian Muslim leaders have played a key role in popularising *Wasatiyyah*. In the 1940s, they accepted *Pancasila's* compatibility with Islam after the first president, Sukarno, proposed it as an ideological basis for a pluralistic Indonesia, which now has almost as many Muslims as in the Islamic heartland of West Asia and North Africa combined.

Pancasila has been likened to the *modus vivendi* the Prophet Muhammad established through the seventh-century Medina Charter, recognising all groups as one nation together with Muslims. American sociologist Robert N Bellah has called this effort depicting the early Muslim community as a type of egalitarian participant nationalism "by no means entirely an unhistorical ideological fabrication". Indonesian intellectual Azyumardi Azra called *Pancasila* an expression of Indonesian Muslims drawing on the Medina model.

Nahdlatul Ulama (Reawakening of the Islamic Scholars), or NU, the world's biggest Islamic organisation, backed Indonesia as a pluralistic State, falling back upon *ijtihad*, the Islamic idea of independent reasoning. It reached a consensus on the nature of the State after a dialogue with secular scholars who shared a nationalist and anti-colonial vision. NU draws parallels between *Pancasila* and the Medina Charter.

The 2002 Bali bombings, which coincided with the chaotic transition from the Suharto dictatorship to democracy, threatened Indonesia's foundational idea. This, coupled with the rise of ISIS globally in the following decade, prompted NU and other Muslim organisations such as the Muhammadiyah to double down — in tandem with the State — to prevent extremism from taking root in society.

The coexistence of Islam, democracy, and pluralism in Indonesia is based on concepts such as *Ummatan Wasatan*, a Quranic term. AFP

NU leader and Muslim cleric Abdurrahman Wahid, who championed humanitarian Islam and played a key role in Indonesia's democratic transition as the president after a 32-year Suharto dictatorship, believed all religions are essentially the same. A proponent of Islamic universalism, he emphasised the idea of *insaniyyu* (humaneness).

Another NU figure, Yaqut Cholil Qoumas, was behind the initiative to allow regular religious rituals at the UNESCO World Heritage sites Prambanan and Borobudur as the Indonesian religious affairs minister in 2022.

The two historic Hindu and Buddhist sites were previously largely closed to ritual worship. They are located in Qoumas's native Java, Indonesia's cultural heartland, where the Muslim majority has long emphasised Islam *rahmatan li al-'alamin* (source of universal love and compassion).

In September 2018, then-Indonesian President Joko Widodo — celebrating Indonesia's multiculturalism as the inauguration of the world's tallest Vishnu statue in Bali, a Hindu-majority area — underlined that Indonesian society had not only inherited masterpieces such as Borobudur and Prambanan from ancient civilisations but also built a civilisation on such foundations. In 1998, the Indonesian central bank released a 20,000-rupiah banknote featuring Lord Ganesha, symbolising wisdom and knowledge, and Ki Hadjar Dewantara, the country's first education minister. The note was withdrawn in 2008.

In 2013, Indonesia installed a statue of Sarasvati, the Hindu goddess of learning and wisdom, outside its embassy in Washington.

Indonesia's religious freedom, harmony, diversity, intercultural and interreligious dialogue offer a model for other countries. The Indonesian State facilitates inter-religious dialogue, sustaining the largest Muslim democracy and a country of over 240 ethnic groups and more than 300 languages.

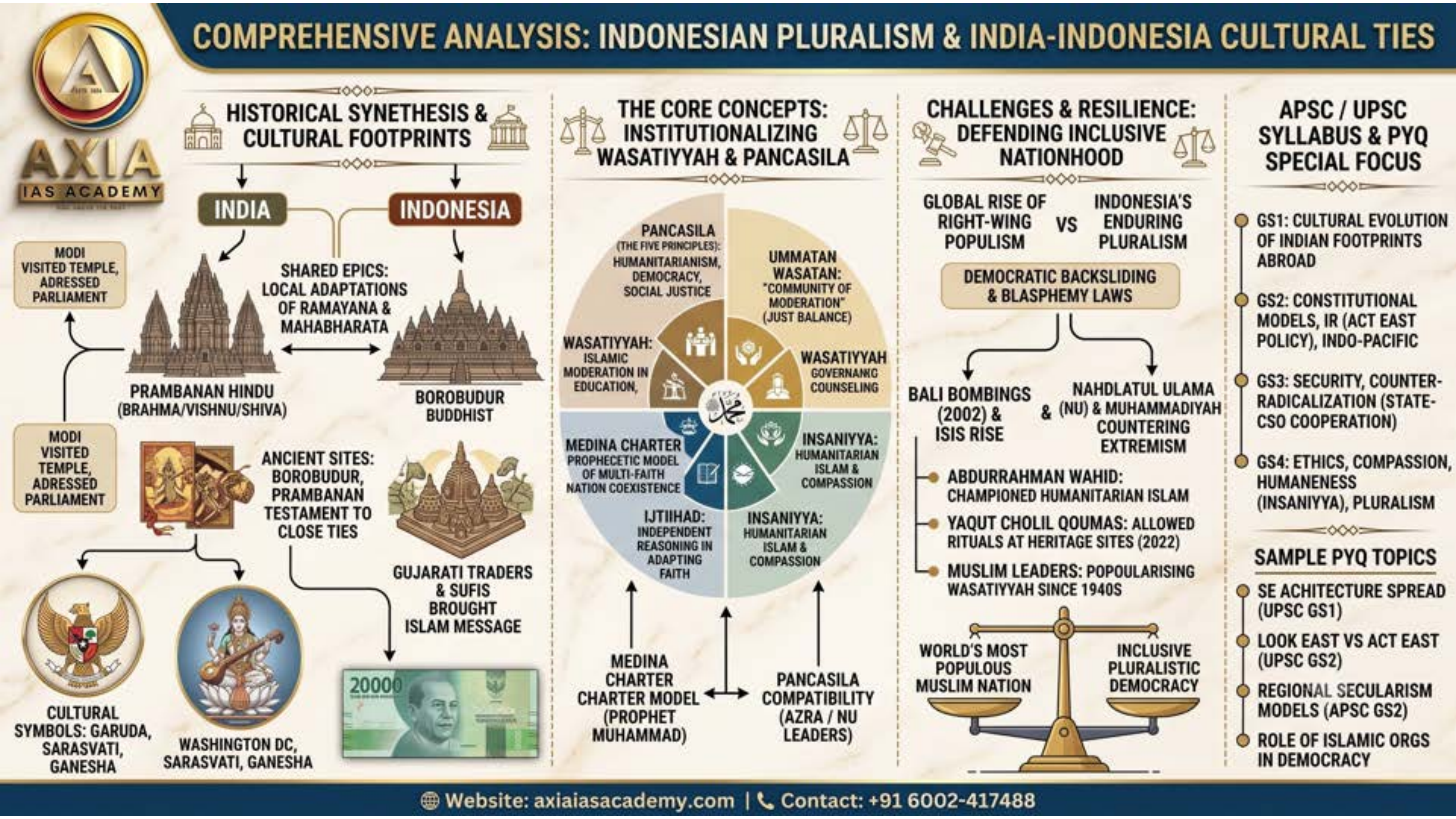
As many as 88% of the Indonesians are Muslims, 9% Protestants, and the remaining Catholics, Buddhists, and Hindus. The Forum Kerukunan Umat Beragama facilitates dialogue and resolves disputes among them. The Indonesian model is about synthesis and not a clash of civilisations, underscoring that there is more to the country than its pre-Islamic history, which many in India appear fixated on.

The views expressed are personal

- **Key Terms and Explanations**
- **Pancasila (The Five Principles):** The official, foundational philosophical theory of the Indonesian state. Formulated by the country's first president, Sukarno, in 1945, it acts as the ideological glue holding a highly fragmented archipelagic nation together. The five interlinked principles are: Belief in the One and Only God, a Just and Civilized Humanity, the Unity of Indonesia, Democracy Guided by Inner Wisdom in a Unanimity Arising Out of Deliberations, and Social Justice for all the People of Indonesia.
- **Ummatan Wasatan & Wasatiyyah:** Derived from Islamic theology, *Ummatan Wasatan* refers to a "Community of the Middle Path" or a "Justly Balanced Nation." *Wasatiyyah* represents the active practice of Islamic moderation, equilibrium, and justice, deliberately eschewing all forms of religious extremism (*ghuluw*).
- **The Medina Charter (Mithaq al-Madina):** A seventh-century constitutional document drafted by the Prophet Muhammad to govern the multi-religious city of Medina. It united various nomadic tribes, Jews, pagans, and Muslims under a single political community (*Ummah*), ensuring religious autonomy and collective defense obligations.
- **Nahdlatul Ulama (NU):** Established in 1926, NU is the world's largest independent Islamic civil organization, boasting tens of millions of members. It champions a traditionalist, culturally integrated, and tolerant iteration of Sunni Islam, deeply engaged in social welfare, education, and counter-radicalization frameworks.
- **Ijtihad:** An Islamic legal term referring to the process of making a legal decision by independent interpretation and reasoning of the foundational sources (the Quran and Sunnah), moving beyond blind adherence to historical legal precedents (*Taqlid*).
- **Insaniyya:** An Arabic term translating to "humaneness" or "universal humanitarianism." Within contemporary governance discourse, it forms the bedrock of "Humanitarian Islam," emphasizing that religious obligations must always serve the preservation of human dignity, compassion, and universal brotherhood, regardless of creed.
- **Islam Rahmatan li al-'Alamin:** A theological doctrine stating that Islam is sent as a "source of mercy, universal love, and compassion to all the worlds." It repositions religion not as an instrument of conquest or exclusion, but as an active force for global harmony and ecological balance.
    - *Example:* The structural policy decision by local religious ministries to open up grand ancient spaces for active, public Hindu and Buddhist rituals, driven by the philosophy of universal benevolence.
- **Forum Kerukunan Umat Beragama (FKUB):** Translated as the "Religious Harmony Forum," these are institutionalized, state-facilitated platforms operating at regional levels across Indonesia. They consist of religious leaders from various faiths tasked with resolving communal disputes, issuing recommendations for building places of worship, and maintaining local peace.
    - *Example:* An FKUB stepping in to mediate neighborhood tensions over the construction of a minority place of worship, resolving the issue through consensus-driven dialogue rather than litigation.

- **Main Arguments and Substantive Parts**
- The structural core of this analysis revolves around the civilizational synthesis, democratic resilience, and institutionalized pluralism of the world's most populous Muslim nation, contrasting its lived reality against reductionist global narratives.
- **The Thesis of Civilizational Synergy**
- The primary assertion highlights that modern state identities in Southeast Asia are not built upon the erasure of pre-Islamic histories, but are active continuations of a deep civilizational synthesis. The relationship between India and the archipelagic region is anchored in deep cultural roots, preserved through local adaptations of the *Ramayana* and *Mahabharata*. The state deliberately integrates classical Hindu-Buddhist iconography into its modern national fabric.
- **The Counter-Narrative to Orientalist Tropes**
- A crucial argument targets Western-centric, Orientalist generalizations that frequently present Islam as incompatible with democracy and structural pluralism. The coexistence of a massive Islamic population alongside robust democratic institutions, a diverse multi-ethnic society (exceeding 240 ethnic groups), and a constitutional commitment to minority rights serves as an empirical refutation of the "Clash of Civilizations" thesis.
- **The Dual Realities of Pluralism and Democratic Friction**
- While celebrating the endurance of an inclusive nationhood, the analysis presents a balanced view by acknowledging systemic internal challenges. The rise of global right-wing populism, instances of democratic backsliding, and the existence of controversial local blasphemy laws present constant friction. These legal instruments, occasionally flagged by international human rights bodies, reveal the ongoing domestic struggle between majoritarian pressures and foundational pluralistic values.
- **Institutionalization of Moderate Theology**
- Pluralism survives in this region because it is systematically institutionalized rather than left to chance. Through the active promotion of *Wasatiyyah* (moderation), the state and massive civil organizations work together to embed tolerance into governance, mandatory premarital programs, and educational institutions. This dual approach of civil society engagement and state policy has acted as a critical defense against transnational radicalization networks.

- **Historical Evolution of the Issue**
- **Pre-Colonial Maritime Transits and Syncretic Islam**
- During the 10th to 15th centuries, maritime trade routes linked the Indian subcontinent, particularly the coast of Gujarat, with the Indonesian archipelago. Traders and Sufi mystics introduced Islam to the region. Unlike iconoclastic variations of the faith, these Sufi scholars adopted an inclusive approach, layering Islamic theology over the deeply entrenched Hindu-Buddhist socio-cultural realities of the Majapahit and Srivijaya empires. This created a uniquely localized, syncretic cultural base.
- **1945: The Pancasila Compromise at Independence**
- As Indonesia neared independence in the mid-1940s, deep ideological divides emerged between factions demanding an absolute Islamic state and secular nationalists seeking a neutral republic. President Sukarno introduced *Pancasila* as a strategic constitutional compromise. Major Muslim organizations made the historic choice to accept this framework, drawing direct parallels between *Pancasila* and the ancient *Medina Charter* to justify their participation in a multi-faith state.
- **The Suharto Regime to the Reformasi Transition (1967–1998)**
- Under the authoritarian "New Order" regime of President Suharto, the state strictly controlled political Islam to maintain stability and promote economic development. While this suppressed radical elements, it also limited genuine democratic expression. The collapse of the regime in 1998 led to the *Reformasi* (Reform) era. Led by visionary figures like Abdurrahman Wahid, the country underwent a transition that decoupled Islam from state authoritarianism, realigning it with democratic governance and universal human rights.
- **2002 to Present: Counter-Extremism and Contemporary Re-assertion**
- The fragile post-authoritarian democracy faced a severe challenge with the 2002 Bali bombings, followed by the rise of transnational ISIS networks in the 2010s. In response, major Islamic organizations like the Nahdlatul Ulama and Muhammadiyah partnered with the state to protect civic spaces from extremism. By 2022, this effort evolved into a confident re-assertion of pluralism, marked by landmark policies that reopened ancient Hindu and Buddhist UNESCO world heritage sites for active public worship.



COMPREHENSIVE ANALYSIS: INDONESIAN PLURALISM & INDIA-INDONESIA CULTURAL TIES
AXIA
IAS ACADEMY
HISTORICAL SYNTHESIS & CULTURAL FOOTPRINTS
INDIA
INDONESIA
MODI VISITED TEMPLE, ADRESSED PARLIAMENT
SHARED EPICS: LOCAL ADAPTATIONS OF RAMAYANA & MAHABHARATA
PRAMBANAN HINDU (BRAHMA/VISHNU/SHIVA)
BOROBUDUR BUDDHIST
MODI VISITED TEMPLE, ADRESSED PARLIAMENT
ANCIENT SITES: BOROBUDUR, PRAMBANAN TESTAMENT TO CLOSE TIES
GUJARATI TRADERS & SUFIS BROUGHT ISLAM MESSAGE
CULTURAL SYMBOLS: GARUDA, SARASVATI, GANESHA
WASHINGTON DC, SARASVATI, GANESHA
20000
THE CORE CONCEPTS: INSTITUTIONALIZING WASATIYYAH & PANCASILA
PANCASILA (THE FIVE PRINCIPLES): HUMANITARIANISM, DEMOCRACY, SOCIAL JUSTICE
UMMATAN WASATAN: "COMMUNITY OF MODERATION" (JUST BALANCE)
WASATIYYAH: ISLAMIC MODERATION IN EDUCATION,
WASATIYYAH GOVERNANIG COUNSELING
MEDINA CHARTER PROPHECETIC MODEL OF MULTI-FAITH NATION COEXISTENCE
INSANIYYA: HUMANITARIAN ISLAM & COMPASSION
IJTIIHAD: INDEPENDENT REASONING IN ADAPTING FAITH
INSANIYYA: HUMANITARIAN ISLAM & COMPASSION
MEDINA CHARTER CHARTER MODEL (PROPHET MUHAMMAD)
PANCASILA COMPATIBILITY (AZRA / NU LEADERS)
CHALLENGES & RESILIENCE: DEFENDING INCLUSIVE NATIONHOOD
GLOBAL RISE OF RIGHT-WING POPULISM
VS
INDONESIA'S ENDURING PLURALISM
DEMOCRATIC BACKSLIDING & BLASPHEMY LAWS
BALI BOMBINGS (2002) & ISIS RISE
&
NAHDLATUL ULAMA (NU) & MUHAMMADIYAH COUNTERING EXTREMISM
ABDURRAHMAN WAHID: CHAMPIONED HUMANITARIAN ISLAM
YAQUT CHOLIL QOUMAS: ALLOWED RITUALS AT HERITAGE SITES (2022)
MUSLIM LEADERS: POPOULARISING WASATIYYAH SINCE 1940S
WORLD'S MOST POPULOUS MUSLIM NATION
INCLUSIVE PLURALISTIC DEMOCRACY
APSC / UPSC SYLLABUS & PYQ SPECIAL FOCUS
GS1: CULTURAL EVOLUTION OF INDIAN FOOTPRINTS ABROAD
GS2: CONSTITUTIONAL MODELS, IR (ACT EAST POLICY), INDO-PACIFIC
GS3: SECURITY, COUNTER-RADICALIZATION (STATE-CSO COOPERATION)
GS4: ETHICS, COMPASSION, HUMANENESS (INSANIYYA), PLURALISM
SAMPLE PYQ TOPICS
SE ACHITECTURE SPREAD (UPSC GS1)
LOOK EAST VS ACT EAST (UPSC GS2)
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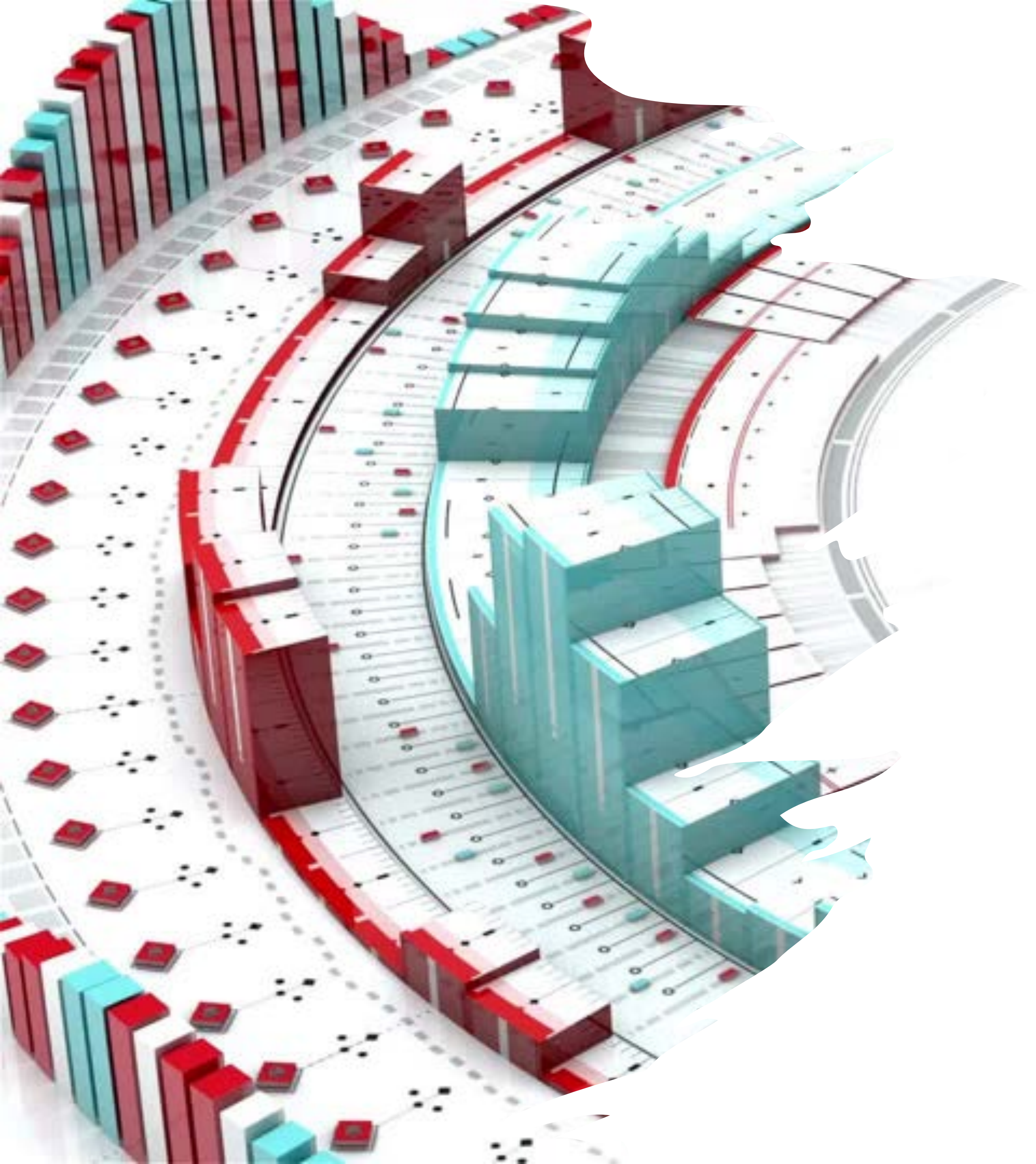

- **Logical and Philosophical Base**
- The viability of this unique governance model rests upon sophisticated philosophical adjustments that reconcile religious absolutes with the practical needs of a diverse democracy.
- **The Philosophical Premise of Synthesis:** The system operates on the conviction that civilizational progress is cumulative rather than replacement-driven. The adoption of a new religious identity does not require destroying ancestral monuments or cultural memories. Instead, ancient structures like Borobudur and Prambanan are treated as foundational national assets that inform modern citizenship.
- **The Theology of Realized Inclusion**
- The system derives its legitimacy by matching modern constitutional principles with historical Islamic precedents. By linking *Pancasila* to the *Medina Charter*, local thinkers created a valid theological path for inclusive citizenship. This logic states that a Muslim can be fully dedicated to a multi-faith democratic state without compromising their faith, as the Prophet Muhammad established a similar multi-faith political alliance in the seventh century.
- **Rejection of the "Clash of Civilizations"**
- The governance philosophy challenges the zero-sum logic of modern majoritarian populism. It replaces the idea of an inevitable clash between religious systems with a model of deliberate civilizational synthesis. By viewing Islam as a source of universal love (*Rahmatan li al-'Alamin*), the state turns religious practice into a tool for social cohesion rather than a political dividing line.

- **Multidimensional Analysis**
- **Social Dimension**
- The social fabric successfully handles deep ethnic and linguistic diversity by encouraging local cross-cultural interactions rather than enforcing assimilation. Grassroots civil society organizations act as social stabilizers, checking radical influences directly within communities. However, localized social frictions persist, driven by the occasional misuse of majoritarian sentiments and uneven economic development across the islands.
- **Political Dimension**
- Politically, the nation proves that democratic institutions can thrive within a deeply religious society. It shows that political Islam can choose consensus-driven moderation over radical governance. The main challenge remains defending these democratic gains against populist political parties that attempt to exploit religious identities during high-stakes election cycles.
- **Legal Dimension**
- The legal architecture reflects a continuous balancing act between constitutional guarantees of freedom and conservative local laws.
- The system balances broad constitutional protections with localized religious regulations and contested blasphemy laws. While national bodies work to resolve inter-faith property and worship disputes, the presence of punitive blasphemy laws shows that minority groups still face legal vulnerabilities.
- **Ethical Dimension**
- From an ethical perspective, the state promotes human dignity (*insaniyya*) over narrow sectarian interests. It emphasizes the moral duty of the majority to protect and honor the sacred spaces of minority traditions, as seen in the revitalization of ritual access to ancient temples. This ethical stance reframes pluralism as a shared moral responsibility rather than just a legal requirement.
- **International Dimension**
- In international relations, this syncretic identity serves as a powerful exercise in soft power diplomacy. It presents the nation as a balanced, democratic leader within ASEAN and the broader Muslim world. For India, this shared cultural history forms a natural bridge for its *Act East Policy*, transforming ancient cultural connections into modern strategic, maritime, and economic partnerships across the Indo-Pacific.
- **Economic Dimension**
- The historical foundation of this pluralistic model was built entirely on maritime trade routes. Today, this syncretic identity helps secure critical trade links throughout the Indo-Pacific. By maintaining domestic stability and a welcoming international image, the state attracts diverse foreign direct investment, proving that long-term economic growth is deeply connected to predictable, inclusive governance.

- **Linkages with NCERTs**
- **Class 11 Political Science: Political Theory (Chapter on Secularism)**
- **Core Concept:** The Western model of secularism involves a strict separation of church and state, whereas the Indian model features "principled distance," where the state interacts with all religions equally.
- **Analytical Link:** The Indonesian approach offers a third comparative model: active state facilitation of religious harmony using a shared philosophical framework (*Pancasila*), without adopting a completely secular stance or establishing a state religion.
- **Class 12 Political Science: Contemporary World Politics (Chapter on Regional Organisations - ASEAN)**
- **Core Concept:** Assessing the socio-political stability, economic growth, and internal dynamics of Southeast Asian nations under the "ASEAN Way" of consensus and non-interference.
- **Analytical Link:** This case study highlights how domestic pluralism and moderate governance help anchor a key ASEAN member, directly supporting regional stability and resisting external geopolitical pressures.
- **Class 7 & 11 History: Our Pasts & Themes in World History (Chapters on Cultural Transitions and Maritime Trade Networks)**
- **Core Concept:** The expansion of Chola maritime expeditions, the spread of Indian art and architecture to Southeast Asia, and the role of Indian Ocean trade routes in spreading Sufi traditions.
- **Analytical Link:** Provides the historical context needed to understand why modern Muslim nations in Southeast Asia retain deep connections to classical Hindu-Buddhist iconography and architecture.

- **Linkages with UPSC CSE Syllabus**
- **GS Paper 1: Indian Culture and Society**
- **Syllabus Topics:** Salient aspects of Art Forms, Literature, and Architecture from ancient to modern times; Salient features of Indian Society, Diversity of India; Secularism, Communalism, Regionalism.
- **Application:** Writing analytical answers on the historical spread of Indian art and architecture beyond its geographical borders, and comparing global models of diversity management and pluralism with the Indian experience.
- **GS Paper 2: Governance, Constitution, and International Relations**
- **Syllabus Topics:** Comparison of the Indian constitutional scheme with that of other countries; Bilateral, regional, and global groupings and agreements involving India and/or affecting India's interests; Effect of policies and politics of developed and developing countries on India's interests.
- **Application:** Evaluating India-Indonesia bilateral relations within the *Act East Policy*, analyzing security dynamics in the Indo-Pacific, and examining constitutional designs that balance majoritarian demographics with robust minority protections.
- **GS Paper 4: Ethics and Human Interface**
- **Syllabus Topics:** Human Values - lessons from the lives and teachings of great leaders, reformers, and administrators; Tolerance and compassion towards the weaker sections.
- **Application:** Using concepts like *Insaniyya* (universal humaneness) and *Wasatiyyah* (moderation) as cross-cultural ethical examples in essays and case studies focused on tolerance, conflict resolution, and harmony.

- **Way Forward**
- To sustain and replicate these models of pluralism amid global polarization, clear institutional, legal, and diplomatic strategies must be pursued.
- **Comprehensive Legal Reform of Blasphemy Provisions**
- To protect foundational pluralistic values, democratic states must reform or narrow the scope of vague blasphemy laws. This prevents such statutes from being used by majoritarian groups to target religious minorities or restrict open civic discussion.
- **Institutional Strengthening of Grassroots Inter-Faith Fora**
- The model of state-facilitated, local inter-faith arbitration councils—like the *Forum Kerukunan Umat Beragama*—should be strengthened and institutionalized globally. Moving dispute resolution out of polarized political arenas and into community-led, consensus-driven spaces helps defuse tensions before they escalate into violence.
- **Deeper Integration of Civil Society into Counter-Extremism**
- Governments should avoid relying solely on hard security measures to fight radicalization. Partnering directly with traditionalist, moderate religious civil organizations helps protect educational institutions and local communities, using theological moderation to counter extremist narratives from within.
- **Elevating Shared Cultural Footprints into Strategic Partnerships**
- In the Indo-Pacific, nations like India and Indonesia should actively use their shared cultural heritage to strengthen modern ties. Transforming ancient syncretic connections into collaborative maritime security, tourism corridors, and digital trade networks helps build a more stable, rules-based regional order.

UPSC CSE Prelims Questions

1. With reference to the cultural history of India, consider the following statements: (2020)

1.Commercial and cultural contacts between the Malabar coast and Southeast Asia date back to pre-Christian eras.

2.The architectural style of the grand monuments in early Southeast Asian kingdoms was entirely independent of Indian influence.

Which of the statements given above is/are correct? A) 1 only B) 2 only C) Both 1 and 2 D) Neither 1 nor 2

Answer: D (Statement 1 is incorrect as intensive regular commercial contacts with Southeast Asia primarily gathered momentum from the early centuries of the Christian era, though early exchanges existed; Statement 2 is completely incorrect as Southeast Asian architecture shows deep structural and artistic linkages with Indian Silpasastras).

2. Which of the following kingdoms were associated with the life of the Buddha? (2014 / 2015)

1.Avanti

2.Gandhara

3.Kosala

4.Magadha Select the correct answer using the code given below: A) 1, 2 and 3 B) 2 and 4 C) 3 and 4 only D) 1, 3 and 4 *Answer: C*

With reference to the spread of Indian culture to Southeast Asia, the famous Borobudur temple is located in which modern-day nation? (Cloned Contextual) A) Cambodia B) Thailand C) Indonesia D) Vietnam

Answer: C

UPSC CSE Mains Questions

GS Paper 1

•"The rock-cut architecture represents one of the most important sources of our knowledge of early Indian art and history." Discuss the statement with special reference to its spread and influence on Southeast Asian temple architecture. **(2021, 15 Marks)**

•Assess the impact of Indian cultural footprints—including language, religion, and epic literature—in Southeast Asia from the ancient period to the medieval era. **(2018, 10 Marks)**

•How do you explain the fact that despite being a land of immense religious and ethnic diversity, the idea of an inclusive nationhood has survived in India? Contrast briefly with global experiences. **(2016, 15 Marks)**

GS Paper 2

•Evaluate the economic, strategic, and cultural dimensions of India's 'Look East Policy' turned into 'Act East Policy', with special focus on bilateral relations with maritime neighbors like Indonesia. **(2022, 15 Marks)**

•Indian constitutional secularism is a unique model that maintains a 'principled distance' from all religions, unlike the absolute separation seen in Western models. Analyze this statement in comparison with multi-religious democratic nations in the developing world. **(2019, 15 Marks)**

GS Paper 4

•"Tolerance and compassion are the foundational values facing modern multi-ethnic societies today." In this context, explain how values derived from religious moderation can assist modern public administrators in resolving deep-seated communal conflicts. **(2023, 10 Marks)**

The many portents of growing inequality

India is witnessing a constant rise in the number of millionaires and high net-worth individuals (HNIs). In the last financial year, 5,032 people entered this exclusive club. This took the strength of India's millionaire club to more than 871,000. As an Indian, this may feel like a shimmering statistic, but many aspects of the same report will leave you sad and dejected.

Income inequality is rising in India, leading to exasperation among the middle class.

For the uninitiated, HNIs are those who have property or any financial instrument worth $1 million, or ₹8.5 crore at current conversion rates, which they can quickly convert to cash if the need arises, after meeting all their financial obligations. Last year, this club witnessed an increase of 6% — comparatively lower than the 2021-2023 period (when the share market and real estate enjoyed a bull run) that saw the HNI club swell by upto 9%. These are the fortunate few who control 65-75% of India's wealth and business.

However, we aren't the only victims of income inequality. This tendency or trend is growing across the globe, whether in developed countries such as the US and Japan or middle-income countries such as China along with the entire group of developing nations. A report by Capgemini Research Institute and UBS Global Wealth suggests the world has witnessed an increase in average wealth, yet the common person's financial condition has deteriorated. On the one hand, we have new money magnates such as trillionaire Elon Musk who are brushing the old-money royalty aside. On the other, their societies are seeing growing hardships among people at the bottom of the economic pyramid.

This is why the world is hurtling towards rising criminal activity and disaffection, borne out of a growing tribe of depressed people. The trend is posing a challenge not only to families, societies or administrative structures but even the integrity of nations. Let me begin with a few examples from our neighbourhood.

Recall the street demonstrations in Sri Lanka, Bangladesh, and Nepal. The disaffection among the Sri Lankan populace was so great that the demonstrators breached the heavy security cordon to enter and vandalise the Presidential palace. Public anger brought about a change of political leadership in these three countries. It's a different matter that the "change" itself is experiencing a trial by fire today. Not only in South Asia but African nations such as Kenya, Latin American countries, and even our former colonial masters, the UK, have tasted the bitter pill of violent demonstrations.

During the violent demonstrations in our neighbourhood, I was closely watching the youth of these countries. Almost everywhere, reels showing politicians, the rich and the well-heeled went viral, with demonstrators lamenting the obscenely opulent lives of the former while they were struggling to put two square meals on the table.

In India, the situation mercifully isn't that bad but it isn't normal or easy either. Reports of educated young men and women attracted to cybercrime, lured by the "quick buck" and "reel worthy luxury lifestyle", startle a conscientious person.

Consumerism has induced dangerous levels of fear of missing out (FOMO) among the youth. Income inequality adds fuel to the fire.

Now, let's look at the other aspect. It is often said that if India has to progress economically, it needs to align its productivity and economic policies with global needs. That we have the world's largest number of graduates and engineers sounds great, but when we assess their ability at the altar of productivity, we realise they are not up to the mark. According to a study, only 56.35% of Indian graduates are employable. This means more than 43% are condemned to struggle in the current scenario. Among the employable graduates, most are engineers. Again, within this pool, the highest demand is for computer science graduates — though the latter too are facing stiff challenges in these times of Artificial Intelligence. Are they prepared to deal with it? It is clear that even after knowing coding and theory, only 46% will be effectively employed. Even they will have to work hard to develop critical thinking and soft skills.

The sad fact is we don't have much time left to fill the gap. Enthusiasts who call India a young country may find their vigour dampening when they discover that we have 66% of the population in the working age bracket (15-59 years). The writing is on the wall. We have little time left to harness the demographic dividend. We will have to bridge our contradictions by the 2035-2040 timeframe. If we fail, then India runs the risk of becoming old before becoming rich.

It's not a coincidence that most countries are facing the same malady. If they don't increase the productivity of their workforce, they will lag behind in the age of automation and AI. It will increase the threat of neo-colonialism. We can already see green shoots of the trend.

Agencies such as the United Nations that are supposed to protect human rights and democracy are powerless in front of developed countries. This is the reason Russia's invasion of Ukraine is entering its fifth year and Israel kept killing people in Gaza for months. Later, it attacked Iran along with the US. It is true that Ukraine is holding out against Russia with the help of Europe and the US. Iran too is making the US' life miserable with the help of Russia and China. But the wars have endangered the current global order.

It also raises a question: What happens if the tragedy of national and social inequality is not addressed? Will it lead to mass starvation, a third world war, nuclear disaster, or something else?

IT'S NOT A COINCIDENCE THAT MOST COUNTRIES ARE FACING THE SAME MALADY. IF WORKFORCE PRODUCTIVITY DOESN'T RISE, THEY WILL LAG BEHIND IN THE AGE OF AI

Shashi Shekhar is editor-in-chief, Hindustan. The views expressed are personal

- **Key Terms and Explanations**
- **High Net-Worth Individuals (HNIs):** These are individuals who hold liquid, investable financial instruments or property worth $1 million (approximately ₹9.5 crore) or more, entirely free of their immediate financial liabilities and personal consumption assets. Unlike illiquid wealth tied up in primary residences, this capital is highly mobile and capable of influencing capital markets, venture ecosystems, and luxury real estate overnight.
- **Income Inequality & The K-Shaped Recovery:** An economic phenomenon where different segments of an economy recover or grow at drastically different rates post-crisis. While the top tier (asset owners, tech entrepreneurs, corporate leaders) experiences exponential wealth expansion, the bottom and middle tiers face stagnant wages, inflation, and underemployment.
- **Demographic Dividend:** The accelerated economic growth potential that materializes when a nation's working-age population (typically ages 15 to 59 or 64) outnumbers its non-working, dependent population. This is a finite historical window; if this workforce is underutilized or unemployable, the dividend transforms into a severe demographic liability.
- **Employability Gap:** The profound mismatch between the formal qualifications granted by the higher education ecosystem and the actual practical, technical, and cognitive competencies demanded by the contemporary corporate market. A high graduate count does not automatically equate to a productive workforce.
- **Relative Deprivation and Consumerism FOMO:** A psychological state where individuals evaluate their well-being not by absolute survival metrics, but in comparison to the ostentatious lifestyles displayed by the elite on digital platforms. Driven by consumerism, this "Fear of Missing Out" breeds intense social alienation and can push vulnerable youth toward illicit economic pathways.
- **Neo-Colonialism in the Digital Age:** The indirect exploitation of developing and middle-income nations by technologically dominant superpowers. Instead of physical conquest, this modern manifestation operates through the control of advanced automation, proprietary Artificial Intelligence architectures, data monopolies, and global financial systems.

- **Main Arguments and Substantive Parts**
- The structural challenges facing the modern state can be synthesized into four interconnected core arguments.
- **The Great Divergence: Asset Bull Runs vs. Middle-Class Stagnation**
- A clear paradox is visible in the domestic market: the rapid expansion of the elite wealth bracket vs. the economic compression of the middle class. While capital-market booms and real estate appreciation have rapidly elevated hundreds of thousands into the HNI category, this wealth remains heavily concentrated. The top tier controls an overwhelming majority of national business assets. Meanwhile, the broader populace faces structural inflation and low real-wage growth, creating a pervasive sense of economic exclusion.
- **The Demographic Deadline: The 2035–2040 Boundary**
- With nearly two-thirds of its citizens situated within the productive working-age bracket (15–59 years), the nation possesses a vital macroeconomic asset. However, this demographic window is strictly time-bound. Projections show that structural rebalancing must occur before the 2035–2040 window closes. Failure to build institutional capacity, absorb labor, and elevate productivity within this timeframe risks creating a society that grows old before it grows rich—collapsing under the weight of an aging population without the fiscal cushions of a high-income country.
- **The Structural Skill Deficit and the AI Disruption**
- Quantity does not guarantee quality in human capital. Despite producing millions of graduates annually, deep systemic flaws mean less than 60% are immediately employable. Even within the highly sought-after engineering and computer science fields, the rapid rise of Generative AI and automation is fundamentally shifting baseline requirements. Traditional coding literacy is no longer a guarantee of security; instead, the economy demands advanced critical thinking, cognitive agility, and complex problem-solving skills—areas where the educational infrastructure lags behind.
- **Global Instability and Institutional Decay**
- These internal domestic pressures operate within a highly volatile international environment. Global governance bodies like the United Nations are increasingly unable to enforce international law or restrain unilateral state actions. The resulting prolonged regional conflicts degrade global supply chains, fuel structural inflation, and threaten the stability of the global economic order. For developing nations, this institutional decay increases their vulnerability to technological and economic dependencies.

- **Historical Evolution of the Issue**
- **The Post-Independence Era (1947–1980s): Fabian Socialism and State Control**
- Following independence, the state adopted a command-and-control economic model heavily influenced by Fabian socialism. The primary focus was state-led heavy industrialization, wealth redistribution, and strict regulatory licensing (the "License Raj"). While this framework successfully prevented extreme private wealth concentration and preserved a basic social safety net, it resulted in low GDP growth rates and a severely constrained private sector.
- **The 1991 Watershed: Liberalization, Privatization, and Globalization (LPG)**
- Facing a balance of payments crisis in 1991, the nation dismantled the License Raj, opened its markets to foreign direct investment, and integrated with the global economy. This pivot unleashed market forces, triggered decades of high GDP growth, and fostered an environment ripe for private enterprise and wealth creation. However, the reforms naturally favored asset owners and capital-intensive sectors, laying the groundwork for the modern wealth gap.
- **The Tech and Service Boom (2000s–2010s): Skewed Growth Dynamics**
- Growth over the next two decades was driven primarily by the services sector—especially Information Technology (IT) and Business Process Management—rather than labor-intensive manufacturing. This service-led model created a prosperous urban middle class and a new wave of dollar-millionaires. However, it bypassed the vast majority of the agricultural workforce, leaving millions stranded in low-productivity, informal employment.
- **The Contemporary Era: Hyper-Financialization and Automation**
- Today, the economy is characterized by a K-shaped growth trajectory. Post-pandemic asset inflation, robust real estate markets, and venture capital flows have accelerated the growth of the HNI tier. Concurrently, the rapid rise of automation and AI has disrupted traditional entry-level white-collar jobs. This leaves a massive, highly connected youth population facing a shrinking pool of traditional jobs, creating modern social anxieties like digital consumerism FOMO.

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INDIA'S COMPLEX SOCIO-ECONOMIC LANDSCAPE: PROSPERITY & IMPERATIVES (UPSC CSE ANALYSIS)
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RISE OF THE ELITE & THE INEQUALITY FLAW
A DUAL LANDSCAPE
DEMOGRAPHIC DIVIDEND & THE PRODUCTIVITY CHALLENGE
CONSTANT HNI RISE
(High Net-Worth Individuals)
5,012 NEW MEMBERS ENTER CLUB (Last FY)
TOTAL MILLIONAIRE CLUB STRENGTH: >871,000
FORTUNATE FEW CONTROL 65-75% OF BUSINESS & WEALTH.
HNI CLUB GROWTH: 6% (down from 9%).
RISING INCOME INEQUALITY
MIDDLE-CLASS EXASPERATION
RISE OF THE ELITE & THE INEQUALITY FLAW
(A Sad Statistic)
POPULATION IN WORKING AGE (15-59): 66%
THE TICKING CLOCK & RISKS
Must harness dividend by 2035-2040.
Risk of becoming OLD BEFORE RICH.
GRADUATE EMPLOYABILITY
Largest number of grads/engineers.
STUDY: ONLY 56.35% EMPLOYABLE
>43% condemned to struggle.
RISING INCOME INEQUALITY
YOUTH ALIENATION & SOCIAL CONSEQUENCES
A DUAL LANDSCAPE
EDUCATIONAL MISMATCH & EMPLOYABILITY GAP
AI & AUTOMATION CHALLENGE
CS GRADS FACE STIFF CHALLENGES.
Only 46% effectively employed.
REQUIRES Critical Thinking, Soft Skills.
PROTEST
TECHNOLOGICAL NEO-COLONIALISM RISK
Lagging countries in productivity fall behind.
GLOBAL INSTABILITY & INSTITUTIONAL DECAY
GLOBAL & NEIGHBORHOOD UNREST
DEMONSTRATIONS IN
Neighbors leading to leader change.
• Viral reels showing politician opulence vs. public struggle.
• African, Latin American, UK demonstrations.
• Growing tribe of depressed people.
FOMO
(Fear Of Missing Out)
Induced by consumerism, dangerous levels of fear among youth.
CYBERCRIME LURE
Educated youth lured by "quick buck" and "reel-worthy" luxury lifestyle.
• Russia-Ukraine (5th Year)
• Israel-Gaza-Iran Conflicts
UN POWERLESSNESS
FUTURE RISKS:
• STARVATION
• WORLD WAR III
• NUCLEAR DISASTER
WAY FORWARD: A POLICY IMPERATIVE
• Align Economic Policy with Global Needs
• Bridge Education & Employability Gap
• Harness Demographic Dividend
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- **Logical and Philosophical Base**
- **The Growth vs. Development Dichotomy:** At the heart of this issue lies a fundamental conflict between two economic philosophies. One prioritizes aggregate capital accumulation (GDP expansion, stock market health, and HNI growth), assuming that wealth will naturally trickle down. The other focuses on human capabilities (health, education, and equal opportunity), arguing that true development is impossible when the wealth generated remains concentrated in a small minority.
- **The Rawlsian Lens on Distributive Justice:** Under John Rawls' *Theory of Justice*, specifically the "Difference Principle," socioeconomic inequalities are morally justifiable only if they work to the maximum benefit of the least-advantaged members of society. The current structural reality challenges this principle; wealth concentration at the top is accelerating while the bottom tiers face stagnant job markets, violating the ethical baseline of a balanced social contract.
- **The Strain on the Hobbesian Social Contract:** The foundational legitimacy of the state rests on an unwritten pact: citizens respect the rule of law in exchange for security, economic opportunity, and structural stability. When large numbers of educated youth invest time and resources into education but find themselves structurally excluded from meaningful employment, this social contract begins to fracture. The result is growing alienation, public unrest, and an increase in opportunistic cybercrime.
- **Technological Determinism vs. Human Agency:** There is a flawed assumption that technological progress naturally improves human welfare. In reality, without deliberate state intervention and proactive skilling frameworks, unchecked technological adoption can reinforce existing inequalities. Instead of democratizing opportunities, it can lead to job displacement and digital neo-colonialism.

- **Multidimensional Analysis**
- **Social Dimension**
- **Erosion of Social Cohesion:** Widening wealth gaps weaken the shared trust holding communities together, sharpening divisions along class, regional, and urban-rural lines.
- **Relative Deprivation and Mental Stress:** Constant exposure to curated, affluent lifestyles on social media creates an environment of intense status anxiety and alienation among youth facing underemployment.
- **The Squeeze on the Middle Class:** The traditional middle class faces a dual challenge: rising costs for quality healthcare and education, combined with precarious, highly disrupted employment options.
- **Political Dimension**
- **The Rise of Populist Movements:** Sustained economic frustration creates fertile ground for populist rhetoric and volatile street-led protests, as seen in several neighboring South Asian countries.
- **Pressure on Democratic Instability:** When economic aspirations are consistently unmet, public frustration can lead to direct challenges to administrative authorities and state infrastructure.
- **Policy Capture by Capital Elite:** Concentrated economic power often translates into disproportionate influence over policy design, potentially skewing regulatory frameworks to favor capital over labor.
- **Legal Dimension**
- **Emergence of Novel Cyber-Criminology:** The intersection of youth underemployment and digital access has driven a rise in organized cyber fraud, financial scams, and illicit digital activities.
- **Strain on Judicial and Law Enforcement Machinery:** Legal and enforcement systems face a growing burden trying to police cross-border, technology-driven crimes with outdated investigative frameworks.
- **The Challenge of Regulating Digital Labor Markets:** The growth of the gig economy complicates traditional labor laws, leaving courts to balance business flexibility with basic worker protections.
- **Ethical Dimension**
- **Commodification of Human Worth:** Defining social value through material accumulation and digital visibility distorts foundational ethical values like empathy, community service, and honest labor.
- **Corporate Responsibility vs. Profit Maximization:** The widening gap highlights an ethical deficit in corporate strategies that prioritize short-term shareholder returns over sustainable wage growth and long-term domestic job creation.
- **Generational Inequity:** Today's youth face a structurally harder path to economic independence and housing security than the generations before them, despite holding higher formal qualifications.
- **International Dimension**
- **Decay of Multilateral Governance:** Global institutions like the UN Security Council are increasingly sidelined, unable to resolve protracted geopolitical conflicts or protect human rights in fractured regions.
- **The Threat of Digital Neo-Colonialism:** Developing nations risk falling into systemic dependency on a few technology-exporting superpowers that control foundational AI models and high-tech intellectual property.
- **Globalized Fractures and Supply Chain Shocks:** Local conflicts quickly escalate into global economic challenges, causing energy price volatility and food supply disruptions that hit low-income nations hardest.
- **Economic Dimension**
- **The Structural Trap of the K-Shaped Economy:** Strong growth metrics driven by premium consumption mask weak demand in mass-market consumer goods, indicating low purchasing power among the broader population.
- **The Challenge of Capital-Intensive Growth:** Massive investments in infrastructure and technology do not automatically generate proportional employment if those industries lean heavily on automation rather than labor.
- **Risk of Missing the Demographic Dividend:** If the working-age population is not rapidly upskilled, the window for high-velocity growth will close, leaving the state with an aging workforce and insufficient national savings.

- **Linkages with NCERTs**
- **Class XI NCERT – *Indian Economic Development***
  - *Relevant Chapters:* Chapter 4 (Poverty), Chapter 6 (Rural Development), Chapter 7 (Employment: Growth, Informalisation and Other Issues).
  - *Core Connection:* These sections explain the historical shift from structural unemployment to informal employment, helping clarify why high GDP growth rates can coexist with low quality job creation.
- **Class XII NCERT – *Introductory Macroeconomics***
  - *Relevant Chapters:* Chapter 2 (National Income Accounting).
  - *Core Connection:* This chapter discusses why Gross Domestic Product (GDP) is an imperfect metric for national welfare, showing that aggregate output numbers can easily obscure severe internal income inequality.
- **Class XII NCERT – *Contemporary World Politics***
  - *Relevant Chapters:* Chapter 6 (International Organisations), Chapter 7 (Security in the Contemporary World), Chapter 9 (Globalization).
  - *Core Connection:* These text segments provide the foundational context for understanding why multilateral institutions struggle to manage modern conflicts, and highlight the uneven economic consequences of global integration.
- **Class XI NCERT – *Introducing Sociology***
  - *Relevant Chapters:* Chapter 4 (Culture and Socialisation), Chapter 5 (Doing Sociology: Research Methods).
  - *Core Connection:* Offers tools to analyze concepts like relative deprivation, class stratification, and how digital media reshapes social expectations and status anxiety among youth.

- **Linkages with UPSC CSE Syllabus**
- **General Studies Paper 1 (GS1): Indian Society**
- **Salient Features of Indian Society & Diversity:** Structural transformations within the traditional class hierarchy, and the growth of the HNI tier alongside urban slums.
- **Effects of Globalization on Indian Society:** The spread of global consumerism, social media FOMO, and their impact on traditional social support systems.
- **Poverty and Developmental Issues:** Spatial and socio-economic inequality, and the unique challenges faced by the urban middle class.
- **General Studies Paper 2 (GS2): Governance, Constitution, Polity, Social Justice, and IR**
- **Welfare Schemes for Vulnerable Sections:** The design and efficacy of social security programs aimed at mitigating wealth gaps.
- **Issues Relating to Development & Management of Social Sector:** Addressing quality deficits in higher education and fixing systemic human resource mismatches.
- **Important International Institutions:** The structural limitations of the UN system and other multilateral bodies in managing complex, multi-polar conflicts.
- **General Studies Paper 3 (GS3): Technology, Economic Development, Environment, Security**
- **Indian Economy and Issues Relating to Planning, Mobilization of Resources, Growth, Development, and Employment:** Analyzing the structural causes of jobless growth, capital concentration, and K-shaped economic trajectories.
- **Inclusive Growth and Issues Arising From It:** Policy interventions needed to bridge income gaps and expand shared prosperity.
- **Basics of Cyber Security:** The rise of youth-driven cybercrime syndicates fueled by underemployment and digital access.
- **General Studies Paper 4 (GS4): Ethics, Integrity, and Aptitude**
- **Status and Ethical Problems in Public and Private Institutions:** The ethical responsibilities of wealth creators toward structural equity and fair wages.
- **Human Values & Role of Family, Society, and Educational Institutions:** Reforming education to foster critical thinking, ethics, and civic responsibility over pure material accumulation.
- **Corporate Governance:** Evaluating corporate practices regarding equitable compensation models and sustainable wealth distribution.

- **Way Forward**
- **Rebuilding Human Capital for an AI-Driven Economy**
- **Dynamic Curriculum Overhauls:** Higher education must shift from rote theory to active cognitive development. Curricula should be updated in real-time partnership with industry leaders, emphasizing advanced problem-solving, ethical reasoning, and AI-resilient soft skills.
- **Institutionalizing Lifelong Learning Frameworks:** The state should introduce accessible, nationwide micro-credentialing platforms, allowing early-career professionals to continuously upskill as automation changes the workplace.
- **Igniting a Labor-Intensive Manufacturing Renaissance**
- **Targeted Support for MSMEs:** Scale up the Production Linked Incentive (PLI) schemes specifically for labor-absorbing sectors like textiles, leathergoods, agro-processing, and green energy infrastructure.
- **Decentralized Industrial Corridors:** Establish specialized production clusters in Tier-2 and Tier-3 cities to ease the pressure on overcrowded metropolitan areas, absorb surplus rural labor, and encourage balanced regional growth.
- **Implementing Progressive Fiscal Reforms and Strengthening Social Safety Nets**
- **Taxation and Incentive Realignment:** Refine the tax code to incentivize direct corporate investment in long-term domestic job creation, research, and workforce development, while exploring nuanced mechanisms to ensure fair capital distribution.
- **Universal Quality Infrastructure:** Expand state investments in foundational social assets—such as high-quality public healthcare, digital connectivity, and competitive primary education—ensuring equal opportunity regardless of family income.
- **Modernizing Digital Regulation and Cyber Security Defenses**
- **Strengthening Cyber Jurisprudence:** Upgrade law enforcement with advanced AI analytical tools to detect, disrupt, and prosecute cybercrime networks, while creating viable, legal digital employment alternatives for tech-competent youth.
- **Establishing Safeguards for the Gig Economy:** Introduce clear, comprehensive regulatory frameworks that provide fair compensation, health security, and pension access for gig-economy and informal workers.
- **Advocating for Strategic Multilateralism and Technological Sovereignty**
- **Championing Global South Alliances:** Use platforms like the G20, BRICS, and Voice of Global South summits to advocate for democratic reforms in international bodies, ensuring developing economies have a voice in global governance.
- **Building Open-Source Technological Independence:** Invest heavily in sovereign AI models, digital public infrastructure, and domestic semiconductor research to protect the nation's digital sovereignty and insulate it from technological neo-colonialism.

Civil Services Exam (UPSC) - Prelims Focus Questions

1. **Economic growth in India is often described as "jobless growth". Which of the following indicators directly reflects a situation where GDP grows but employment opportunities remain stagnant?**

A) A concurrent drop in the Capital-Output Ratio. B) A persistent divergence between the growth rate of Gross Value Added (GVA) and the Employment Elasticity of Growth. C) An immediate reduction in the velocity of money circulation. D) A systematic stabilization of the consumer price index.

2. With reference to the concept of the "Demographic Dividend" in India, consider the following statements:

1.It is driven primarily by a sharp drop in the dependency ratio, expanding the share of the population in the 15–59 age bracket.

2.The closure of this demographic window is uniform across all Indian states, driven by identical total fertility rates (TFR).

Which of the statements given above is/are correct?

A) 1 only B) 2 only C) Both 1 and 2 D) Neither 1 nor 2

3. The Gini Coefficient is a standard metric used globally in economic analysis. What does a Gini Coefficient approaching a value of '1' signify?

A) Complete equity in income distribution across the entire population. B) Maximum concentration of a nation's total income within a single individual or household. C) Balanced growth across primary, secondary, and tertiary sectors. D) Complete insulation of the domestic economy from global trade shocks.

Civil Services Exam (UPSC) - Mains Analytical Questions

- **GS Paper 3 (2023):** "Is inclusive growth possible under market-driven economic frameworks? Highlight the major structural impediments in achieving equitable distribution of wealth in India."
- **GS Paper 3 (2021):** "Explain the concept of the K-shaped economic recovery. How has the post-pandemic economic trajectory impacted the Indian middle class and informal labor sectors?"
- **GS Paper 2 (2020):** "The platform economy and gig work have transformed the nature of employment, yet they challenge traditional labor protections. Examine the social justice implications for the modern workforce."
- **GS Paper 4 (2022):** "Obscene disparities in wealth accumulation raise serious ethical dilemmas regarding the social responsibility of private capital. Evaluate this statement using foundational principles of distributive justice."
- **GS Paper 2 (2023):** "The structural paralysis of the United Nations Security Council in the face of prolonged global conflicts reflects a deeper crisis in multilateralism. Discuss India’s potential role in navigating this institutional vacuum."

Public finances now compensate the majority for economic insecurity, regardless of growth

India's Prosperity Problem

Rathin Roy

Bit of a squeeze

'To be rich is glorious' is a slogan apocryphally attributed to Deng Xiaoping. Equally, to be poor is dehumanising. Individuals in extreme poverty are constantly on the verge of extinction, requiring handouts from government, or charity, to survive. They have no hope that their progeny will escape their fate, unless there's intervention.

Extreme and chronic poverty, unattended, is a terminal disease. For this reason, the most important global Millennium Development Goal (MDG) promised the elimination of extreme poverty by 2020. Happily, this goal has been substantially met in India. India's extreme poverty has plummeted from roughly 421 mn people in 1990 to under 75 mn in 2025.

The next goal is an increase in universal prosperity, meaning most people being able to afford basic necessities by earning enough to buy these *without needing subsidy*. These include food, clothing, decent housing, healthcare and education. Whether the last two are publicly or privately supplied is not the question here. That decision is about efficiency and universal affordability. Both should be affordably provided to the population without need to subsidise anyone.

If most people in an economy can afford these five things, then the economy is 'developed', it has attained a threshold level of prosperity. This requires a high level of per-capita income, but also relatively fewer people earning less than the per-capita income and, therefore, requiring subsidy. Hence, how much the majority (not just the rich) earns matters for a prosperous society.

Economic growth does not automatically ensure prosperity, though a larger per-capita GDP is a necessary condition. Economic growth produces prosperity if it results in a larger number of people becoming prosperous, due to their income shares rising as a consequence of growth. This is called inclusive growth.

The greater the number of people whose income share rises by at least as much as the growth rate, the more inclusive is an economy. An inclusive economy delivers a prosperous society. There are billionaires in prosperous societies. But if the number of billionaires rises even as the majority of people see their incomes stagnate, then growth is not delivering prosperity.

I am speaking of incomes rising when growth rises *before* redistributional transfers. If people stay poor and their incomes rise only because government transfers money from the rich to the poor, that is not inclusive growth. I term this 'compensatory income' — handouts given to compensate people for failure of the economic system to allow them to earn more. If a large number of people depend on such handouts, then growth is not delivering prosperity.

If a large number of people depend on 'compensatory income' (read: handouts), then growth is not delivering prosperity

The development transformation of Japan, China, South Korea and, more recently, Chile reflects a process that fosters inclusive growth. These countries grew by exporting manufacturing goods using cheap labour. But, over time, wages rose significantly across the economy allowing the vast majority of people to grow more prosperous.

It created billionaires. But at the same time, public investments fostered world-class health and education systems, and liveable cities and rural habitats, further enhancing mass prosperity. In contrast, countries like Brazil, Turkey, Argentina, Thailand and the Philippines could not foster inclusive growth. They also created billionaires but not prosperity. They are stuck in a middle-income trap, where GDP has grown to respectable levels, but the majority remains dependent on public transfers and handouts to secure basic requirements of a prosperous existence.

A developed economy requires a high level of per-capita income, and relatively fewer people requiring subsidy. How much the majority, not just the rich, earns matters for a prosperous society

What of India? From 1980 until about 2010, the country saw a period of reasonably high growth and modest increase in inclusive prosperity, even as the pace of poverty reduction accelerated. Remarkably, India did this without increasing manufacturing exports significantly (though exports of services did play a role). Instead, the economy, especially in southern and western India, prospered through increases in domestic consumption and investment underpinned by continuously rising real wages, including in agriculture. The top 10% of the population saw a huge increase in prosperity, some of which trickled down to the next 40-60%.

But post-2011, India was unable to further expand prosperity to the next tranche of 150 mn-odd people. Their income stagnated. Regional inequality accentuated, with the majority population in the north and east earning per-capita incomes 1/4th that of peninsular India. This led to a huge shift in public spending, away from health, education and basic services, to transfers to the poor to keep poverty at bay, and to subsidise almost everything they could not afford with their earnings — food for 800 mn people, gas cylinders, affordable housing, free bus rides for women.

Public finances are now used to not build things, provide livelihoods, or provide quality health, education or public transport, but to compensate the majority for prosperity failure. And this continues whether growth is high or low.

The disease of prosperity failure has now spread to the educated, especially Gen Z. Their wages have fallen precipitously. Unlike 30 yrs ago, white-collar entry level jobs now earn less than required to pay income-tax because the young, without legacy assets from ancestors, face deprivation. In these circumstances, they can hardly be expected to pay I-T. This despite India being the fastest-growing economy in the world.

To repeat, to be poor is dehumanising. But to be part of the 'not poor-but-not prosperous' Indian majority, dependent on family or government subsidies in the face of high economic growth, is profoundly depressing.

The writer is former member, EAC-PM

- **Key Terms and Explanations**
- **Extreme Poverty:** This represents the absolute baseline of human survival. It refers to a condition where individuals lack the means to secure basic life-sustaining needs like minimum caloric intake, clothing, and shelter. They exist on the brink of survival, entirely reliant on state interventions or charity. *Example:* An unhoused, landless laborer struggling to meet the World Bank's $2.15/day threshold.
- **Universal Prosperity:** Moving beyond mere survival, this is the state where the vast majority of a population can independently afford essential services—food, decent housing, quality healthcare, and education—through their own earned income, without requiring government subsidies.
- **Inclusive Growth:** This is the holy grail of developmental economics. Growth is only "inclusive" when the income share of the majority (the middle and lower economic tiers) rises at a rate equal to or faster than the overall GDP growth. If a country's economy grows by 7%, but the wages of the working class remain stagnant, the growth is exclusive, not inclusive.
- **Compensatory Income:** A critical concept to grasp. These are state-sponsored handouts or welfare transfers designed to compensate citizens because the economic structure has failed to provide them with a living wage. *Example:* Providing free food grains to 800 million citizens because their actual wages are too low to absorb market food prices.
- **The Middle-Income Trap:** A situation where a developing nation experiences rapid growth—usually by leveraging cheap labor and basic exports—reaches a middle-income level, and then stagnates. Wages rise enough to make basic exports uncompetitive, but the workforce lacks the high-level skills needed to transition to advanced, high-value industries.
- **Trickle-Down Economics:** An often-critiqued economic theory suggesting that wealth generated at the top (by billionaires and massive corporations) will naturally cascade down to the poorer sections through job creation and market expansion.

- **Main Arguments and Substantive Parts**
- The discourse around modern economic development requires a fundamental shift in how we measure success—moving away from just tracking poverty eradication to actively measuring the growth of independent prosperity.
- **The Illusion of Macro-Growth:** A rising GDP and the proliferation of billionaires are necessary but insufficient indicators of a healthy economy. If an economy is producing massive aggregate wealth, but the majority of the population sees stagnant real wages, the resulting societal structure is highly fragile. Growth without wage expansion is fundamentally broken.
- **The Danger of the "Transfer Economy":** When the masses cannot earn enough to live decently, the state is forced into a corner. Instead of utilizing taxpayer money for capital expenditure—like building world-class universities, high-speed rail, or advanced hospitals—governments must divert these funds toward revenue expenditure (free food, free transport, housing subsidies) just to keep the population afloat. This creates a perpetual cycle of dependency rather than empowerment.
- **Regional and Generational Fault Lines:** Economic stagnation is rarely uniform. There is a stark divergence between different geographies (e.g., the booming peninsular regions versus the struggling northern and eastern belts). Furthermore, this failure of prosperity is deeply impacting the youth (Gen Z). Despite being the "fastest-growing economy," white-collar entry-level wages have in many cases plummeted in real terms, leaving educated youth facing downward mobility and financial despair.
- **The Asian Miracle vs. The Latin American Trap:** Successful transitions to prosperity (like Japan or South Korea) involved utilizing cheap labor for manufacturing, which steadily pushed up real wages across the board, backed by massive investments in public health and education. Conversely, economies that failed to broad-base their wage growth ended up stuck, producing high inequalities and a permanent underclass dependent on government doles.

- **Historical Evolution of the Issue**
- The trajectory of India’s economic development offers a textbook case study on the shifting paradigms of poverty and wealth creation.
- **The Pre-1991 Era (The Struggle for Basics):** In the decades following independence, the primary focus was on basic survival. Characterized by the "Hindu rate of growth," heavy state control, and an inward-looking economy, poverty was chronic and widespread. The state was a provider, but resources were acutely scarce.
- **The 1991–2010 Boom (The Rise of Real Wages):** Economic liberalization unlocked unprecedented energy. Driven heavily by the services sector, IT, and a domestic consumption boom, this era saw robust growth. More importantly, real wages—even in the agricultural sector—saw continuous upward movement. Millions were pulled out of poverty, and the first genuine wave of broad-based middle-class prosperity emerged, particularly in western and southern India.
- **Post-2011 to Present (Jobless Growth and Subsidy Reliance):** The momentum of wage growth began to stall. While absolute, extreme poverty continued its downward trend (plummeting to under 75 million), the *quality* of jobs deteriorated. The economy failed to absorb the surplus agricultural labor into high-paying manufacturing. Consequently, to manage the distress of stagnant wages, the state pivoted aggressively toward Direct Benefit Transfers (DBTs) and massive welfare schemes, essentially institutionalizing "compensatory income" to maintain social stability.

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KEY TERMS & DEFINITIONS

DEFINING THE SOCIO-ECONOMIC LANDSCAPE

EXTREME POVERTY
Survival on charity; constant peril; progeny's future grim.

UNIVERSAL PROSPERITY
Afford necessities (Food, Shelter, Health, Education) with earned income without subsidy.

INCLUSIVE GROWTH
Income share rises for all; majority benefits equally with overall growth.

COMPENSATORY INCOME
Handouts given due to failure of economic system to provide living wages.

THE CHALLENGE & TIMELINE

THE DANGER OF STAGNATION

THE MIDDLE-INCOME TRAP

INDIA'S DEVELOPMENT TRAJECTORY

ERA OF STRUGGLE: High poverty, low growth.

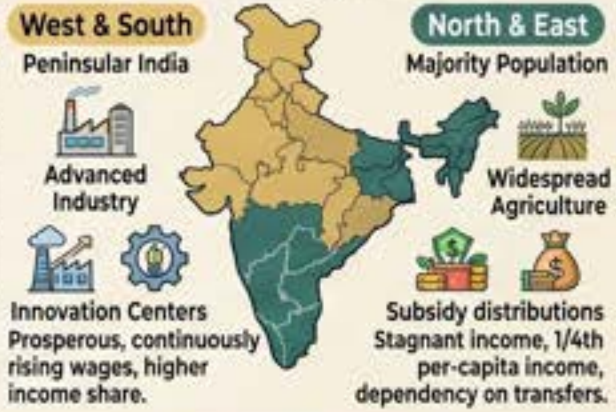
ERA OF BOOM: Services-led growth, rising real wages, broad prosperity.

ERA OF Jobless Growth, Regional Inequality, Subsidy Dependency.

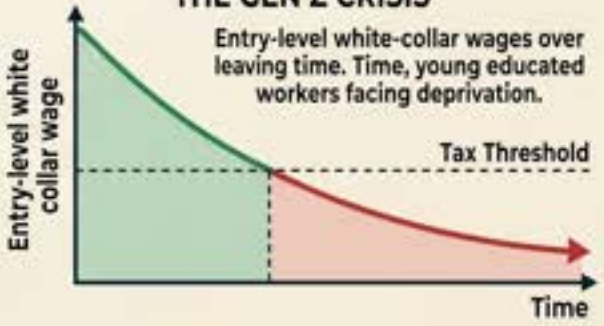
REGIONAL & GENERATIONAL DIVISIONS

DIVERGING FUTURES

REGIONAL INEQUALITY MAP



THE GEN Z CRISIS



THE WAY FORWARD

ACHIEVING UNIVERSAL PROSPERITY: A REFORM STRATEGY

PIVOT TO CAPABILITY
Shift from Entitlement to Capacity-Building (Health, Education).

REVITALIZE LABOR-INTENSIVE MANUFACTURING
East Asian model, broad-based wage rise, sustainable growth.

INSTITUTE LIVING WAGE
Ensure decent standard of life beyond basic minimum wages (ILO).

SKILL GEN Z
Integrate modern skills, vocational training for new economy.

Constitutional Articles 38, 39(c), 43

Amartya Sen's Capability Approach (conceptual)

- **Logical and Philosophical Base**
- **Amartya Sen’s Capability Approach:** True development is not merely the absence of poverty or the provision of free rations; it is the expansion of human capabilities. Sen argues that society must empower individuals with the tools (quality education, health, skills) to achieve the kind of life they have reason to value. Handouts keep people alive, but they do not build capabilities.
- **The Dignity of Labor (Kantian Ethics):** Work should allow an individual to live a life of dignity. If a person works a full-time job but still relies on state charity to feed their family, their labor is being structurally devalued. A system that institutionalizes the working poor is ethically compromised.
- **The Constitutional Mandate:** The Directive Principles of State Policy (DPSP) are the philosophical bedrock here. **Article 38** mandates the state to minimize inequalities in income. **Article 39(c)** warns against the concentration of wealth. Most importantly, **Article 43** directs the state to secure a "living wage" and a decent standard of life for all workers. The reliance on compensatory handouts is a tacit admission that the living wage mandate is failing.
- **The Social Contract Theory:** Citizens pay taxes and adhere to laws with the expectation that the state will foster an environment where their hard work leads to upward mobility. When the youth find that education and hard work lead to wages below the income-tax threshold, the social contract begins to fracture, leading to disillusionment and social unrest.

- **Multidimensional Analysis**
- **Economic:** Stagnant wages suppress domestic aggregate demand. If the bottom 80% of the population has no disposable income, they cannot buy consumer goods, which in turn discourages private corporate investment. Furthermore, funding massive welfare schemes widens the fiscal deficit, leaving little room for infrastructure spending.
- **Social:** The stagnation of the middle tier creates a deeply polarized society. The psychological toll on the youth—often termed the "demographic disaster" rather than dividend—manifests in delayed marriages, rising mental health crises, and a sense of hopelessness. It also exacerbates rural-urban migration distress.
- **Political:** The situation fuels "competitive populism" or the freebie culture. Political parties, unable to fix the structural job market, resort to promising increasingly extravagant subsidies (free electricity, direct cash transfers) to secure vote banks, heavily compromising state exchequers.
- **Ethical:** There is a profound moral hazard in celebrating high national GDP figures while normalizing the fact that the majority cannot survive without subsidized food. It raises questions about corporate governance—why are corporate profits soaring while entry-level wages are strictly suppressed?
- **International:** India’s global ambition to be a superpower is fundamentally constrained by its domestic socio-economic fragility. A nation cannot project hard power internationally if a vast majority of its citizens are economically vulnerable and dependent on state subsidies.

- **Linkages with NCERTs**
- **Class 9 Economics - Chapter 3 (Poverty as a Challenge):** Introduces the concept of the poverty line, vulnerability, and social exclusion, framing the baseline from which the transition to prosperity must begin.
- **Class 10 Economics - Chapter 1 (Development):** Crucially teaches that "averages hide disparities." This chapter explains why per-capita income (GDP divided by population) is a flawed metric if the wealth is concentrated in the hands of a few billionaires.
- **Class 11 Indian Economic Development - Chapter 4 (Poverty) & Chapter 7 (Employment):** These chapters discuss the nature of the workforce, jobless growth, and the historical evolution of poverty alleviation programs in India.
- **Class 12 Macroeconomics - Chapter 5 (Government Budget and the Economy):** Essential for understanding the difference between revenue expenditure (subsidies, handouts) and capital expenditure (asset creation), and how heavy welfare spending impacts the fiscal deficit.

- **Linkages with UPSC CSE Syllabus**
- **General Studies Paper 1:**
  - *Poverty and Developmental issues:* The shift from poverty elimination to broad-based prosperity.
  - *Regionalism:* The stark economic divergence between the affluent South/West and the struggling North/East India.
- **General Studies Paper 2:**
  - *Welfare schemes for vulnerable sections:* The efficacy and long-term sustainability of freebies and DBTs.
  - *Issues relating to poverty and hunger:* The transition from basic food security to nutritional and economic security.
  - *Social Sector/Services:* The critical need to shift spending from consumption subsidies to health and education capacity building.
- **General Studies Paper 3:**
  - *Indian Economy and issues relating to planning, mobilization of resources, growth, development, and employment.*
  - *Inclusive growth and issues arising from it.* (This is the most direct linkage).
  - *Government Budgeting:* Balancing fiscal prudence with welfare obligations.
- **General Studies Paper 4 (Ethics):**
  - *Corporate Governance:* Ethical distribution of wealth within corporations.
  - *Empathy and tolerance for weaker sections:* Understanding the psychological impact of systemic poverty on human dignity.
- **Essay Paper:** Highly relevant for topics concerning jobless growth, the myth of the demographic dividend, capitalism and inequality, and the future of India's youth.

- **Way Forward**
- **Pivot from Entitlement to Empowerment:** There must be a phased transition from consumption subsidies to capability investments. The funds currently used for "compensatory income" should be gradually redirected towards building state-of-the-art public healthcare and aggressively upgrading the public education system to global standards.
- **Revitalize Labor-Intensive Manufacturing:** India must urgently fix its manufacturing sector to absorb the masses exiting agriculture. Emulating the East Asian model—focusing on export-oriented, labor-intensive sectors like textiles, electronics assembly, and footwear—is crucial for driving up real wages.
- **Address Regional Imbalances via Decentralization:** To bridge the North-South divide, special economic zones and heavily incentivized infrastructure corridors must be developed in the eastern and northern belts to trigger localized employment and halt forced economic migration.
- **Institute a Genuine Living Wage:** Labor reforms must move beyond minimum wages to enforcing a "living wage" (as proposed recently by the Indian government aligning with ILO standards) that accounts for healthcare, education, and housing, ensuring the working class doesn't fall back into subsidy dependence.
- **Skill Upgradation for Gen Z:** To tackle youth wage stagnation, the curriculum must heavily integrate vocational training, digital literacy, and AI-readiness from the high school level, ensuring the workforce matches modern industry demands.

- **Prelims (Concept-based questions from past years):**
- *UPSC 2020:* "With reference to the Indian economy, consider the following statements: 1. 'Growth rate of GDP has steadily increased in the last decade.' 2. 'Growth rate of per-capita income has steadily increased in the last decade.' Which of the statements given above is/are correct?" (Tests understanding of growth realities vs. statistical averages).
- *UPSC 2018:* "Which of the following is/are the indicator/indicators used by IFPRI to compute the Global Hunger Index?" (Relates to basic necessities and poverty).
- *UPSC 2017:* "Which of the following are the objectives of the 'National Nutrition Mission'?" (Links to capability building vs. food subsidies).
- *UPSC 2015:* "The concept of 'Inclusive Growth' in India encompasses which of the following? 1. Financial Inclusion 2. Strengthening of MSMEs 3. Poverty Alleviation 4. Skill Development."
- **Mains (Analytical questions demanding multidimensional answers):**
- *UPSC GS-3 (2022):* "Is inclusive growth possible under market economy? State the significance of financial inclusion in achieving economic growth in India."
- *UPSC GS-2 (2021):* "Can the vicious cycle of gender inequality, poverty and malnutrition be broken through microfinancing of women SHGs? Explain with examples."
- *UPSC GS-3 (2020):* "Explain the meaning of investment in an economy in terms of capital formation. Discuss the factors to be considered while designing a concession agreement between a public entity and a private entity." (Relevant to state expenditure capacity).
- *UPSC GS-3 (2017):* "What are the salient features of 'inclusive growth'? Has India been experiencing such a growth process? Analyze and suggest measures for inclusive growth."
- *UPSC Essay (2016):* "Innovation is the key determinant of economic growth and social welfare." / "If development is not engendered, it is endangered."

ILLUSTRATION: AJAYA KUMAR MOHANTY

The poor's savings: Next frontier?

The best candidates to think out of the box are NPCI and the Reserve Bank Innovation Hub

REPROSPECT

M S SRIRAM

On the checklist of innovations, a point without a checkmark is savings. Traditionally, both policymakers and markets have looked at the poor as borrowers, to be rescued from the moneylender. The policy discourse focused on institutional credit — priority-sector targets, refinancing, and specialised institutions like cooperatives and regional rural banks. Irrespective of the supply-side push, the credit market for poor women was cracked in the late 1990s with microcredit. We have argued that there are still white spaces in the missing middle, but that is a discussion for another day.

In the past two decades, we have seen interesting developments in remittances, which have benefited inclusive customers. This was because of technology rather than policy priority. The roll-out of core banking solutions, the interoperable switch-making ATMs (automated teller machines) working across banks, the spread of the internet and mobile telephony, the setting up of National Payments Corporation of India (NPCI) — all these created an ecosystem for payments and remittances. The poor were collateral beneficiaries of this architecture. The policy of not loading user charges helped in the speedy adoption of Unified Payments Interface (UPI). While this is still not ubiquitous in deep rural areas and with women, the impact it has on easier, simpler and seamless remittances can be seen.

We have no such story for savings. The myth is that the poor — being poor — cannot save. The very same poor borrow and repay instalments with interest. If we look at savings and loans as a cash-flow continuum, the difference between loans (frontloading an expenditure/investment) and savings (backloading it) is not significant. In the iconic book The Poor and their Money, Stuart Rutherford termed this "saving up and saving down".

Apart from the myth, we have other restrictions. For savings, the risk of default or malfeasance is borne by the vulnerable customer and, therefore, the regulator is cautious in allowing any latitude in experiments with savings products.

High costs of frequent small-ticket transactions cannot be passed on to the poor customer by way of lower interest. In the case of loans, the lender controls cash flows by specifying a repayment schedule. In structuring a flexible savings product, factoring in volatile cash flows of the poor is complex. Bankers do not like such products because they do not fit into their cash management. Therefore, legacy institutions do not innovate on savings.

The regularity with which the poor are scammed with savings as bait shows two things. There is an appetite for savings, and there is no dearth of imagination and innovation. But this happens under the radar. Ponzi schemes, chit funds and even lightly regulated residuary non-banking finance companies like Sahara which were shut down demonstrate that the poor have an appetite to save. Other innovations in this space skirt the regulations. At one time, experiments by the Kshetriya Grameen Financial Services in Odisha and Tamil Nadu offered money-market mutual funds to the poor. The logic was that those were liquid and flexible, and had a positive return and mimicked an accumulating savings account. While being relatively safe instruments, those were not without market risks and had no insurance cover, and therefore were not to be offered to the poor.

With the rollout of technology for small payments done, savings in the regulated space are waiting for innovation. But who will bell the cat?

Let us look at UPI. All innovation in the payments space happened outside the banking system — with players like Paytm, PhonePe, BharatPe and BHIM. The banking system provided the interface and co-opted these payment gateways. All digital-lending innovation is also happening outside the banking ecosystem with fintechs leading the franchise. The banks are backstopping by colending or lending to NBFCs operating as frontal lenders.

The issue with savings is different. Regulatory restrictions provide this privilege exclusively to banks. Bankers are expected to be boring, and provide stability. Therefore, the regulator expecting bankers to be innovative would be a tall ask.

The poor save not only in the form of stashing away cash and informal deposits, but also putting money in different asset classes — goats, backyard poultry, gold, silver, and utensils (to be pawned). It is possible for the financial system to mimic the liquidity (or illiquidity), return, flexibility and safety by offering financial products that address the requirements of the poor.

In the past, one could argue that designing such products and rolling them out were expensive. No longer so. With every family having a Pradhan Mantri Jan Dhan Yojana (PMJDY) account, with possible inflows from direct-benefit transfers, banks could build innovative products that justify the investment in both technology and the rollout of such accounts. PMJDY accounts could be the anchor accounts on which multiple savings products could be built.

Would this include women? That would be a greater challenge because smart phones are usually family-owned and women need an agency and privacy to manage their finances. For women, an accumulating savings product to purchase a dream smartphone may be the first target.

Is it fair to expect banks to innovate? No, unless the regulator thinks out of the box to license a few digital-only banks. Legacy banks have too much on their hands, and their technology focus may be on investing in artificial intelligence-enabled call centres to do customer service and investment in cyber security.

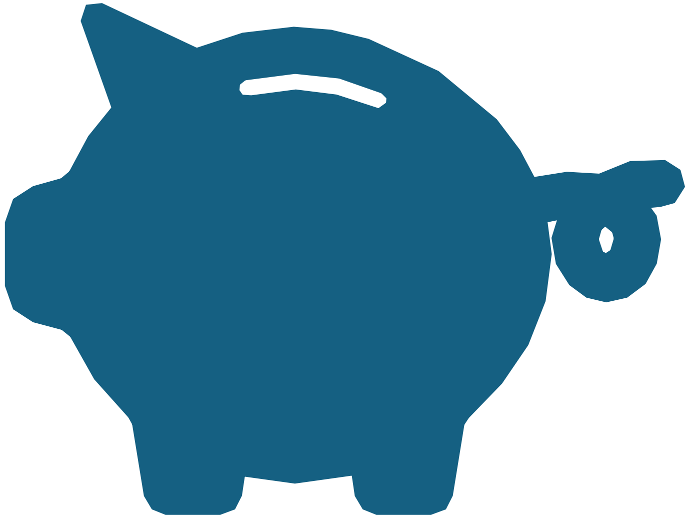
The best candidates to think out of the box are NPCI and the Reserve Bank Innovation Hub. Both have the ear of the regulator and leverage with the banking system. Are they willing to take up white-label savings products? As in the case of BHIM, will NPCI act as an interface with banks as a background engine?

This space is crying to be occupied with tech-led innovation. Getting savings from microfinance customers will mute leverage-related stress if banks are able to capture the borrower's assets into their books, even as they continue to lend.

Is anybody listening?

The author is professor, Indian Institute of Management, Bangalore. He is thankful to Misha Sharma, Priya Ganesan and Dilip Asbe for conversations on this issue

- **Key Terms and Explanations**
- **Cash-Flow Continuum:** This is a conceptual approach that views loans and savings not as two separate financial products, but as two sides of the same financial coin. A loan allows an individual to "frontload" an expenditure—meaning they get a lump sum now and pay it back in small bits later. Savings, conversely, "backloads" the expenditure—meaning the individual stores small amounts over time to spend a lump sum later. For example, a street vendor buying a new cart can either take a micro-loan and pay weekly interest (frontloading) or save a portion of daily profits for six months to buy it outright (backloading).
- **Saving Up vs. Saving Down:** A structural behavioral concept in microfinance coined by development researcher Stuart Rutherford. "Saving up" refers to the traditional method of accumulating small, frequent trickles of money over time to build a large lump sum for future use. "Saving down" is the mirror image: obtaining a lump sum upfront through borrowing and then clearing that liability through small, disciplined future repayments.
- **White-Label Savings Products:** Financial applications or savings modules built by a centralized, expert technological utility entity but branded and deployed by individual banks. In practice, this would allow a small regional rural bank or cooperative to offer an ultra-modern, highly flexible digital micro-savings product to its rural customers without having to build the expensive technology infrastructure from scratch.
- **Reserve Bank Innovation Hub (RBIH):** A wholly-owned subsidiary of the Reserve Bank of India established to foster, facilitate, and anchor technological innovation across the Indian financial sector. It acts as a catalyst by bringing together fintech innovators, legacy banks, and regulators to test new models in a secure environment.
- **National Payments Corporation of India (NPCI):** An umbrella organization operating retail payments and settlement systems across India. Created as a public utility initiative, it is the powerhouse behind revolutionary platforms like the Unified Payments Interface (UPI), which democratized immediate digital payments nationwide.
- **Pradhan Mantri Jan Dhan Yojana (PMJDY):** India’s flagship National Mission for Financial Inclusion launched in 2014. It succeeded in opening hundreds of millions of basic, no-frills, zero-balance bank accounts for unbanked citizens, providing them with a formal digital identity, debit cards, and a baseline channel for direct benefit transfers.



- **Main Arguments and Substantive Parts**
- **The Credit and Payment Success vs. The Savings Deficit**
- The journey of financial inclusion in India has seen spectacular success in two major arenas: institutional credit and digital payments. Decades of policy pushes have established robust microcredit networks, Self-Help Groups (SHGs), and strict Priority Sector Lending (PSL) mandates to rescue the vulnerable from local moneylenders. Similarly, the deployment of core banking solutions and UPI transformed the remittance ecosystem, allowing seamless, cost-free digital fund transfers even in the remotest villages. However, formal micro-savings products have remained an unmapped, dry frontier, fundamentally left out of this technological renaissance.
- **Dismantling the Myth of the Incapacity to Save**
- A long-standing, institutional misconception dictates that the poor cannot save because their incomes are too low and entirely consumed by immediate survival. This assumption is visibly contradicted by financial realities. The poor consistently borrow from formal microfinance institutions or informal sources and successfully repay those loans in structured, interest-bearing weekly or monthly installments. If an individual has the financial discipline and regular cash flow required to repay a loan (saving down), they inherently possess the economic capacity to accumulate capital through savings (saving up), provided they are given the right instruments.
- **The Structural Inertia of Legacy Banking**
- Traditional commercial banking infrastructure is inherently structured around predictability and large-ticket transactions. For legacy banks, managing a high volume of tiny, volatile, daily deposits from the unorganized sector is an operational nightmare that complicates standard cash-flow management. Consequently, commercial banks prefer to focus their technological resources on highly profitable areas like artificial intelligence for urban customer service or cybersecurity, showing little to no commercial appetite for innovating flexible, low-ticket savings products tailored for low-income citizens.
- **The Regulatory Paradox of Asymmetric Risk**
- Regulators look at savings and credit through completely different lenses due to the placement of financial risk. In a credit transaction, the bank takes the risk of default; if a loan goes bad, the institution suffers, not the borrower. In a savings transaction, the risk of institutional failure or fraud is entirely borne by the vulnerable depositor. Because the poor are highly susceptible to losing their life savings, the central bank maintains an extremely cautious, ironclad regulatory stance on deposit-taking mechanisms, inadvertently stifling the flexibility needed for experimental micro-savings innovation.
- **The Flight of Capital to Informal and Risky Avenues**
- Because formal banking does not provide flexible options that match the fluid cash flows of the unorganized sector, the poor are forced to save through alternative, highly inefficient channels. They store wealth in illiquid or vulnerable physical assets like small livestock, gold, or kitchen utensils, which can easily be pawned but carry high transaction costs. Alternatively, their strong appetite for capital accumulation makes them prime targets for unregulated or poorly monitored financial entities, driving them toward predatory chit funds and catastrophic Ponzi schemes.

- **Historical Evolution of the Issue**
- **Pre-1969: Indigenous and Informal Dominance:** Following independence, the Indian rural economy was deeply entangled in informal financial credit structures. Banking was almost exclusively urban, elite, and transactional. The marginalized relied entirely on local moneylenders for emergencies, while savings were stashed away physically as cash or converted into non-liquid domestic assets.
- **1969–1980s: State-Led Credit Expansion:** The nationalisation of 14 major commercial banks in 1969 and the subsequent establishment of Regional Rural Banks (RRBs) in 1975 marked the beginning of "social banking." The primary policy objective was structural credit delivery to priority sectors like agriculture. While this expanded the banking footprint, it treated rural citizens purely as passive recipients of loans rather than proactive financial savers.
- **1990s–2000s: The Microcredit and SHG Boom:** The launch of the Self-Help Group-Bank Linkage Programme by NABARD in 1992 and the subsequent rise of Non-Banking Financial Companies (NBFC-MFIs) fundamentally cracked the credit market for low-income households, particularly women. This era proved the creditworthiness of the poor but cemented a policy bias that equated financial inclusion almost entirely with credit access.
- **2014–Present: The Digital Payment and Identity Revolution:** The arrival of the JAM (Jan Dhan-Aadhaar-Mobile) Trinity and the creation of NPCI brought structural transformations. PMJDY brought hundreds of millions of unbanked citizens into the regulated space, while UPI eliminated the transactional friction of small remittances. This created the massive digital highway and formal account base needed for advanced financial interventions.
- **The Contemporary Era: The Shift Toward Tech-Led Micro-Savings:** India now stands at a turning point where the digital payment architecture is fully mature, but the savings space remains unutilized. Policy focus is gradually shifting toward exploring how public fintech innovators like the Reserve Bank Innovation Hub can utilize this digital footprint to build secure, highly flexible micro-investment and savings frameworks for the bottom of the pyramid.

AXIA IAS ACADEMY

RISE ABOVE THE REST

MICRO-SAVINGS: THE NEXT FRONTIER IN FINANCIAL INCLUSION

THE PROBLEM: FORMAL SAVINGS DEFICIT & THE CREDIT-SAVINGS GAP

MYTH vs. REALITY

Myth: Poor Cannot Save

Reality: High Borrowing Capability

LEGACY BANKS & RIGIDITY

BANK

- High transaction costs
- Complex daily cash management for small-ticket items

REGULATORY PARADOX

CAUTION

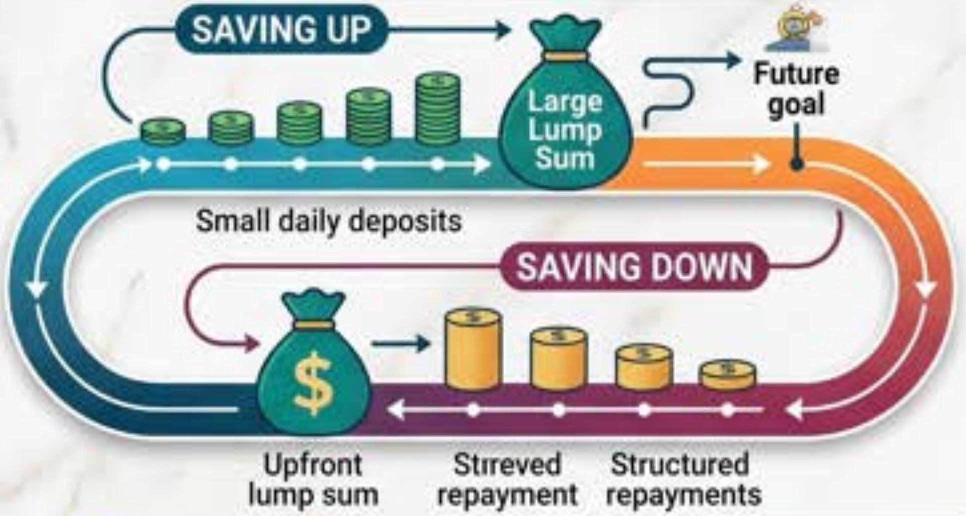
INNOVATION

- Predatory Chit funds
- Ponzi Schemes
- Un-liquid Livestock

INNOVATION

RISKY INFORML CHANNELS

CONCEPTUAL CORE: THE CASH-FLOW CONTINUUM



A NEW VIEW

White-Label Savings Products

Central products → Central utility → Local banks

Savings as a Commitment Device

WAY FORWARD & KEY UPSC CSE LINKAGES

1. **Centralized Tech Engine** (NPCI + RBIH Collaborative Utility)
2. **Flexible Daily Small Deposits** (Mobile App with pig icon)
3. **PMJDY Wealth Conversion** (Active Auto-sweep, micro-investments)
4. **Specialized Digital Banks with asset rules**

UPSC CSE LINKAGES

NCERT LINKAGES

- **Class 10** Money & Credit
- **Class 11** Rural Development

PYQ SPOTLIGHT & SYLLABUS

GS Syllabus

- GS3: Economy
- GS2: Governance
- GS3: Economy
- etc.. andre.

PYQ PYQ PYQ

- **Logical and Philosophical Base**
- **The Capability Approach to Financial Independence**
- The underlying logic of moving toward formal micro-savings is deeply rooted in the Capability Approach championed by economist Amartya Sen. True development is not merely about increasing consumption or providing debt; it is about expanding an individual's substantial freedom to lead the life they value. Credit, while useful, introduces debt liabilities and potential vulnerabilities. Savings, on the other hand, build internal resilience and individual agency. By providing a secure mechanism to save, the state shifts its citizens from a position of debt-dependence to one of self-funded financial security.
- **Behavioral Economics of the Unorganized Sector**
- The conventional economic view assumes that low-income individuals act short-sightedly, spending whatever they earn immediately. Behavioral economics refutes this, demonstrating that the poor are highly rational economic actors who navigate extreme volatility. They do not lack the psychological willingness to save; rather, they lack formal "commitment devices"—structural frameworks that match their daily, erratic earnings. When the financial system forces a daily-wage laborer into a rigid monthly or quarterly savings model designed for salaried classes, the system creates a structural mismatch that locks the poor out.
- **Asymmetric Regulatory Morality**
- There is an implicit philosophical tension between financial innovation and consumer protection. The regulator operates on a defensive ethical mandate: protecting the hard-earned deposits of citizens who lack the financial literacy to assess institutional health. This creates a regulatory asymmetry where credit innovations (where fintechs bear the risk) are given wide latitude, while deposit innovations are heavily restricted. Overcoming this requires a conceptual shift: recognizing that failing to provide a safe, flexible formal savings vehicle is itself a risk, as it actively drives the poor into the hands of predatory, unregulated entities.

- **Multidimensional Analysis**
- **Social Dimension**
- Formal micro-savings function as a powerful tool for gender empowerment and shifting household dynamics. In many low-income households, women are the primary financial managers but lack privacy and control over physical cash, which is frequently diverted by male members or spent on non-essential consumption. Providing poor women with private, secure digital savings accounts gives them the financial agency to accumulate funds for long-term household priorities, such as children's higher education, family healthcare, and improved nutrition. This breaks the cycle of generational poverty and builds social resilience against sudden life shocks.
- **Political Dimension**
- From a governance standpoint, transitioning the poor into formal savers reshapes the welfare state paradigm. Currently, state welfare heavily relies on Direct Benefit Transfers (DBT) to provide immediate relief. If these funds are deposited into accounts that offer no creative incentive to save, they are quickly withdrawn and consumed. By integrating smart, tech-driven savings architectures with existing PMJDY accounts, governments can design co-investment or asset-building welfare schemes. This shifts the state's political identity from a provider of temporary financial doles to a facilitator of long-term household wealth accumulation.
- **Legal & Regulatory Dimension**
- The legal arena presents a delicate balancing act for the Reserve Bank of India. Under current banking laws, deposit-taking is a tightly guarded privilege reserved for heavily capitalized commercial institutions. To foster innovation, the legal framework must evolve to accommodate new entities, such as digital-only banks or specialized micro-savings micro-utility services, without diluting depositor protection. Regulators face the complex task of designing ring-fenced regulatory sandboxes that allow tech platforms to handle frequent, small-ticket daily deposits while ensuring these funds are fully backstopped by licensed commercial banks and covered by deposit insurance schemes.
- **Ethical Dimension**
- The current financial architecture perpetuates an unethical reality known as the "poverty premium," where the poorest segments of society pay the highest relative costs to manage their money. When a low-income worker saves through informal chit funds or purchases gold in small, unrefined quantities, they lose a significant portion of their wealth to middle-men, fraud, or poor liquidation value. Providing the unorganized sector with free, secure, and yielding financial savings instruments is an ethical imperative of distributive justice, ensuring that the fruits of digital progress are shared equally rather than flowing only to urban, affluent classes.
- **International Dimension**
- India's deployment of Digital Public Infrastructure (DPI)—built on Aadhaar, UPI, and data-sharing networks—has become a core element of its international soft power and economic diplomacy. Expanding this architecture into the micro-savings domain positions India as a global leader in inclusive financial engineering. The successful creation of a public-utility tech engine for micro-savings provides a highly scalable, low-cost blueprint for the entire Global South, helping developing nations across Africa, Latin America, and South-Asia achieve United Nations Sustainable Development Goals (SDGs), particularly SDG 1 (No Poverty) and SDG 5 (Gender Equality).
- **Economic Dimension**
- At the macroeconomic level, mobilizing the micro-savings of the unorganized sector taps into a massive pool of idle domestic capital. Aggregating the small daily savings of hundreds of millions of citizens converts fragmented, informal cash into stable, long-term institutional deposits. This expands the domestic banking sector's loanable resource base without increasing reliance on volatile foreign capital. Furthermore, at the micro-level, access to flexible savings cushions families against seasonal unemployment or crop failures, reducing the incidence of over-indebtedness and default rates within the microfinance credit ecosystem.

- **Linkages with NCERTs**
- **Class 10 Economics: Chapter 3 – "Money and Credit"**
- **Nature of Linkage:** This foundational chapter introduces students to the dichotomy between formal and informal financial sectors, detailing how Self-Help Groups act as a bridge for the poor.
- **Analytical Expansion:** While the textbook focuses heavily on how these groups facilitate institutional credit to eliminate the grip of usurious moneylenders, the current issue expands this concept by examining the other side of the balance sheet: the critical need to formalize micro-savings using public digital infrastructure like UPI and PMJDY.
- **Class 11 Indian Economic Development: Chapter 6 – "Rural Development"**
- **Nature of Linkage:** This chapter offers a comprehensive critique of India's rural banking system, highlighting the achievements of social banking alongside its structural deficiencies, such as inadequate deposit mobilization and over-reliance on credit targets.
- **Analytical Expansion:** The discussion on technological micro-savings directly addresses the long-standing gaps identified in the textbook. It provides modern, tech-driven solutions—like utilizing the Reserve Bank Innovation Hub—to fix the structural inefficiencies of legacy rural banking systems.

- **Linkages with UPSC CSE Syllabus**
- **General Studies Paper 3: Indian Economy and Inclusive Growth**
- **Core Mapping:** Highly relevant to sections covering *Inclusive Growth and issues arising from it*, *Mobilization of Resources*, and *Banking Sector Reforms*.
- **Application:** Ideal for formulating arguments on how India can leverage its mature digital public payment infrastructure to build stable, low-cost domestic capital reserves while protecting the unorganized workforce from financial shocks.
- **General Studies Paper 2: Governance and Public Policy**
- **Core Mapping:** Connects to *Welfare schemes for vulnerable sections of the population by the Centre and States* and the *Development processes and the development industry*.
- **Application:** Provides an innovative analytical framework for assessing how the JAM Trinity can be upgraded from a tool for simple direct cash transfers into an ecosystem that encourages individual asset creation and long-term financial self-reliance.
- **General Studies Paper 4: Ethics and Human Dignity**
- **Core Mapping:** Relevant to *Human Values*, *Ethical issues in economic and developmental governance*, and *Distributive Justice*.
- **Application:** Empowers students to analyze the structural exclusion of the poor from secure wealth-accumulation vehicles as a systemic ethical failure, framing financial inclusion not just as an economic goal, but as a moral imperative to eradicate the poverty premium.
- **Essay Paper & Optional Subjects**
- **Core Mapping:** Directly applicable to recurring essay themes concerning technology as a social equalizer, women's financial autonomy, or sustainable rural development models. It also offers deep analytical value for candidates with optionals such as **Economics** (Development and Monetary Policy), **Sociology** (Rural Transformation and Gender Stratification), and **Public Administration** (Welfare Delivery Mechanisms).

- **Way Forward**
- **Building a Centralized Tech Engine for Micro-Savings**
- The state should not rely on profit-driven commercial banks to develop specialized micro-savings products for low-income segments. Instead, the National Payments Corporation of India (NPCI) and the Reserve Bank of India Innovation Hub (RBIH) should collaborate to build an open-source, public digital utility platform dedicated to micro-savings. Much like UPI revolutionized retail transactions, this platform could offer "white-label" micro-savings modules. Small cooperative banks, Regional Rural Banks (RRBs), and microfinance institutions could seamlessly integrate these modules into their existing operations without needing heavy technological capital expenditures.
- **Designing Products that Replicate Informal Flexibility**
- To successfully draw the unorganized workforce away from physical assets or risky chit funds, formal financial instruments must mimic the operational liquidity and flexibility of informal savings. Micro-savings accounts should allow for ultra-small, daily variable deposits (as low as 10 or 20 rupees) without charging transaction fees. Furthermore, these products must support instant, hassle-free micro-withdrawals through basic mobile networks or local business correspondents, eliminating the rigid documentation, minimum balance penalties, and bureaucratic delays typical of legacy commercial banking.
- **Converting PMJDY Accounts into Wealth Engines**
- The extensive network of hundreds of millions of Pradhan Mantri Jan Dhan Yojana (PMJDY) accounts needs to be transformed from simple, passive direct benefit receipt channels into active tools for capital growth. The financial system can introduce automated, micro-investment tools—such as intelligent auto-sweep systems. With the account holder's consent, these systems could automatically sweep tiny residual balances or a small fraction of incoming welfare transfers into safe, liquid, inflation-protected instruments like micro-mutual funds or government securities, helping rural households gradually accumulate wealth.
- **Introducing Calibrated Digital-Only Banking Licenses**
- The Reserve Bank of India should consider designing a specialized, niche regulatory framework for digital-only micro-savings banks. These entities would operate under custom regulations tailored for low-value, high-frequency transactions. To ensure absolute safety without stifling technological creativity, the regulator could implement strict asset-allocation rules. For example, these digital banks could be restricted to investing their accumulated micro-deposits solely in highly secure, low-risk government securities, while their depositors remain fully protected by the Deposit Insurance and Credit Guarantee Corporation (DICGC).
- **Deploying Behavioral Nudges and Local Interfaces**
- Financial literacy programs must move beyond traditional classroom lectures toward interactive, behavioral intervention strategies. Digital savings applications should use localized languages, intuitive iconographies, and gamified progress indicators tailored for semi-literate users. By using smart behavioral nudges—such as sending targeted text reminders that match daily market schedules or offering small, state-backed matching contributions when users reach personal savings goals (like buying a smartphone or funding a child's school fees)—the system can turn irregular cash savings habits into consistent, formal investment behaviors.

UPSC CSE Prelims Questions

•**Year 2015:** Which of the following is/are the objective/objectives of 'Pradhan Mantri Jan-Dhan Yojana'?

- (a) Providing housing loan to poor people at cheaper interest rates
- (b) Promoting financial inclusion in the country
- (c) Providing financial help to marginalized communities for starting businesses
- (d) Providing life insurance cover to poor people in rural areas
- *Answer Hint: (b)*

•**Year 2018:** With reference to the National Payments Corporation of India (NPCI), which of the following statements is/are correct?

- NPCI helps in promoting financial inclusion in the country.
- NPCI has launched RuPay, a card payment scheme.
- Select the correct answer using the code given below:
- (a) 1 only
- (b) 2 only
- (c) Both 1 and 2
- (d) Neither 1 nor 2
- *Answer Hint: (c)*

•**Year 2020:** With reference to the funds flow via digital channels, consider the Unified Payments Interface (UPI). Which of the following statements is most appropriate?

- (a) It allows instantaneous transfer of funds between two bank accounts on a mobile platform.
- (b) It completely replaces cash transactions in rural areas within a decade.
- (c) It requires mandatory internet banking credentials for every small merchant transfer.
- (d) It is handled exclusively by international payment consortiums to ensure safety.
- *Answer Hint: (a)*

UPSC CSE Mains Questions

•**GS Paper 3 (2022):** "Is financial inclusion the only effective path to alleviate poverty and achieve sustainable economic growth in rural India? Critically examine the role played by institutional credit ecosystems in this context."

•**GS Paper 3 (2016):** "Pradhan Mantri Jan Dhan Yojana (PMJDY) is necessary for bringing unbanked to the institutional finance fold. Do you agree that it will challenge the traditional informal financial intermediaries? Argue with evidence."

•**GS Paper 3 (2019):** "Discuss how the deployment of Digital Public Infrastructure (DPI) through the JAM Trinity has transformed the delivery of public welfare services and shaped inclusive economic growth in India."