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*The opportunity and  
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SUMMER, 2013

## A passage to modernity

By Manish Agarwal

India's extensive infrastructure needs are well known. Decades of underinvestment have left the country with dire deficits in such critical areas as railways, roads, ports, airports, telecommunications and electricity generation. In the World Economic Forum's Global Competitiveness Report for 2011-2012, India ranked 89th out of 142 countries for its infrastructure. The report criticized its transport, ICT and energy infrastructure as "largely insufficient and ill-adapted to the needs of business," adding: "The Indian business community continues to cite infrastructure as the single biggest hindrance to doing business in the country."

**Indeed, the nation's infrastructure challenges** are a major drag on economic growth. During the halcyon years of India's boom, it was easier to overlook this threat. Lately, however, India's GDP growth has slipped to around 4.5%. The economy has been hobbled by high interest rates, inflation and a lack of reform. Meanwhile, the government is mired in a slow-moving system of coalition politics, and it's further

constrained by a hefty fiscal deficit and a deepening current account deficit. Given this environment of fading growth, political gridlock and the high cost of capital, it's not surprising that infrastructure spending has slowed in the past year or so.

Yet India's vast infrastructure needs are expanding all the time, and this presents enormous opportunities. The population has already surpassed 1.2 billion, and it continues to grow at a heady rate. Global trade is placing acute pressure on India's inefficient ports. Rapid industrialization is intensifying the strain on the nation's unreliable networks for electricity and water. The railway system — already infamously overcrowded — faces rising demand for freight capacity. And the government has fallen far short of its plans to build 20 km of roads each day — an urgent requirement in a nation where 65% of all freight is transported by road, and where traffic is so severe that the maximum highway speed for trucks and buses is only 30-40 km per hour.<sup>1</sup>

The need to upgrade India's infrastructure is especially acute in huge cities such as Mumbai, New Delhi, Kolkata and Bangalore. India's urban population of around 375 million is projected to reach 500 million by 2017.<sup>2</sup> By 2030, the country is expected to have 68 cities with over 1 million residents.<sup>3</sup> This torrid rate of urbanization means that massive investment will be required in everything from metro systems to clean water supplies, power generation to affordable housing.

**Recognizing these almost limitless requirements**, the government has called for \$1 trillion in infrastructure spending in the five years through 2017. The priorities include three airports, two ports, an elevated rail-corridor in Mumbai, and

<sup>1</sup> Report by India's Ministry of Road Transport & Highways, September 2011. <http://morth.nic.in/writereaddata/linkimages/Policy%20Issues-9224727324.pdf>

<sup>2</sup> Milken Institute Report on "Urbanizing India" <http://www.milkeninstitute.org/presentations/slides/428-230UrbanizingIndia.pdf>

<sup>3</sup> "India's urban awakening: Building inclusive cities, sustaining economic growth", McKinsey Global Institute, September 2010. <http://www.iutindia.org/ntpdc811/Annexure17.pdf>

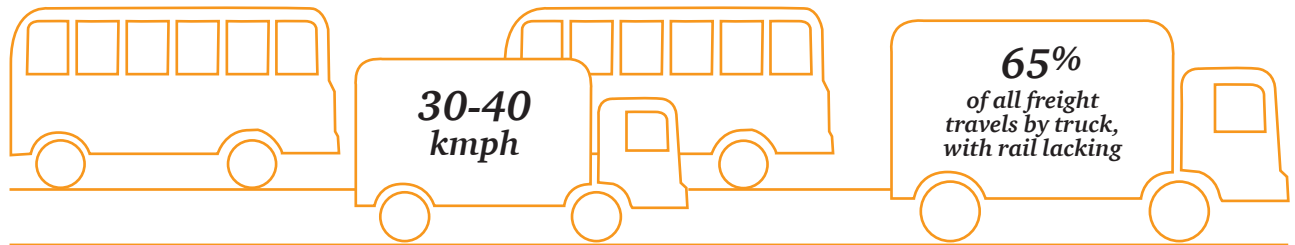
On cover and above: Train in Mumbai

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*Traffic is so severe that the maximum highway speed for trucks and buses is only*



almost 6,000 miles of new roads.<sup>4</sup> The Ministry of Road Transport outlined plans for \$120 billion worth of road-widening projects, with 65% of this money targeted to come from the private sector. There are also plans for \$60 billion to be invested in India's ports by 2020. The Indian Planning Commission has estimated that the country will need 180 additional airports in the next decade. And the government has set ambitious goals for wind, solar and nuclear energy, all of which will be needed to supplement power from coal and gas.

**Given the scale of this infrastructure gap, it's small wonder** that India is one of the world's most attractive markets for companies in the infrastructure business. A recent report by Business Monitor International predicted that India's infrastructure sector will grow by 7.9% in the 2013 fiscal year — down from a previous estimate of 9.4%, but still a formidable rate of growth.<sup>5</sup> The opportunities are so extensive that money has poured in from overseas, including investments in 2011 from leading private equity firms such as Kohlberg Kravis Roberts and the Blackstone Group.

But India's difficult business environment has sapped the enthusiasm of many foreign investors. Among other things, they complain about unpredictable regulations; bureaucratic delays in approving projects; endless struggles to secure land rights; and the government's stalled attempts at reform. The country's reputation for corruption is also a major deterrent: in 2011, India ranked 95th out of 182 countries in Transparency

International's Corruption Perceptions Index, down from 87th in 2010. The telecom sector has been struggling with a scandal over licenses. And the government has rattled foreign investors by trying to claim over \$2 billion in taxes from Vodafone Group, attempting to change the law retroactively after India's highest court ruled in the firm's favor.<sup>6</sup>

Not surprisingly, some investors have retreated. According to Reuters, private equity investments in Indian infrastructure sank to \$183 million in the first quarter of 2012, down from \$459 million in the same period of 2011. There is also a rising tide of domestic disillusionment about the government's unwillingness to tackle the nation's economic challenges. In late 2011, while announcing Wipro's earnings, the technology firm's renowned chairman Azim Premji warned: "There is a complete absence of decision-making among leaders in the government."

**To shed further light on these issues, we interviewed** two of India's most prominent thinkers, whose penetrating insights we share in the pages that follow. Narayana Murthy, a legendary business leader who transformed Infosys into a global powerhouse in the software industry, talks of the "huge pressure" on everything from electricity to roads. To meet these challenges, he stresses the need for greater involvement by the private sector, and calls for entrepreneurs to be freed from "the tyranny of petty bureaucracy."

M.J. Akbar, one of India's most renowned journalists, weighs in with a candid discussion of some of the biggest threats to India's economic progress: political inertia, ominous water shortages, bureaucracy, and corruption — which, he says, "creates space for the incompetent to buy their way into the most important sectors of India's economy."

**Murthy and Akbar are both deeply concerned** about India's future. Yet they are also remarkably optimistic, given the country's extraordinary dynamism. As Akbar points out, India has already made astonishing progress, and he sees no reason why this should not continue. "There will be problems along the way," he concedes. "But even if we just equal over the next 20 years what has happened over the last 20 years, you are going to see a country which is very definitely at the top edge of the second world. Not the first world, but definitely the second."

For India, it seems, both the challenges and the opportunities are immense.

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<sup>4</sup> "India's PM Unveils Infrastructure Investment Plan", *Wall Street Journal* June 6, 2012. <http://online.wsj.com/article/SB1001424052702303665904577450692014546230.html>

<sup>5</sup> "India Infrastructure Report Q2 2013", *Business Monitor International*. <http://bmireports.blogspot.co.uk/2013/03/india-infrastructure-report-q2-2013.html>

<sup>6</sup> "Vodafone Gets Another \$2 Billion Tax Bill From India", *Wall Street Journal*, January 5, 2013. <http://online.wsj.com/article/SB10001424127887323374504578223001514954038.html>

## Confronting India's challenges with confidence and alacrity

In 1981, N.R. Narayana Murthy founded Infosys with six friends, each contributing \$250. Over the next three decades, he led the software consulting company as its CEO, Chairman and Chief Mentor, transforming it into a global colossus that now has over 145,000 employees. Today, Murthy is Chairman Emeritus of Infosys and serves on the boards of HSBC, the UN Foundation, the Ford Foundation, and the Wharton School. Renowned as a visionary entrepreneur and a champion of ethical leadership, he is also the author of *A Better India, A Better World*. In praising this book, Bill Gates hailed Murthy for demonstrating “that it is possible to create a world-class, values-driven company in India,” while India’s Prime Minister Manmohan Singh lauded Murthy as “an iconic figure... a role model for millions of Indians.” Here, Murthy discusses the challenges facing India — and how to overcome them with the help of government reform, private sector dynamism, and “huge foreign investment.”

*India's economy is growing rapidly, its population is expanding at an extraordinary rate, and there's massive migration from the countryside to overcrowded cities like Mumbai and New Delhi. How concerned are you about the stress all of this places on urban infrastructure such as roads, the water supply, and the electricity system?*

It's a big challenge, there's no doubt at all. The country is progressing very fast. We grew at 8.5% on average over the last few years. Last year, which ended on March 31, 2012, we grew around 7%. When the economy grows at this rate, it's only natural that there's huge pressure on infrastructure. Even though we've been building infrastructure, we're not able to keep pace with demand. That results in huge productivity losses and delays, mainly in urban areas.

*Where do you see the most acute strains on India's infrastructure?*

Transportation from place to place takes an enormous amount of time. You see it when you're commuting from home to office and office to home. Our



roads have not been developed as quickly as our logistical demands require. Also, the average speed of our freight trains today must be about 40 mph, which is no speed at all these days. We're not adding a lot more railway lines. We're not expanding roads or improving the quality of our roads. So the movement of goods takes a long time. Similarly, our port infrastructure is not as developed as we'd like. The average time for clearance at our ports is several

days, whereas it's several hours in many other countries. For India's economy to make sustained progress, we have to build better roads so that the transportation of goods becomes efficient; we have to build ports; we have to enhance our power capacity; and we also have to improve access to coal and other raw materials. These are all very important requirements.



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*How does the inadequacy of India's electricity system affect companies, many of which contend with frequent power outages?*

To give you an example, I know several manufacturing companies in states like Karnataka and Tamil Nadu that don't get power for several hours a day. Therefore, they've installed their own generators. But that power is about twice as expensive — or sometimes 2.5 times as expensive — as the power the state provides, since the state has economies of scale. When you have to pay 2.5 times the normal rate for power, you become less and less competitive in the marketplace; you're not able to sell your products, so your corporation becomes weaker, which means that it pays lower taxes and can't employ as many people.

*How economically disruptive is the logjam on India's roads?*

We're adding about four million vehicles every year and about 11 million two-wheelers, but the roads are not expanding. When I leave my home in south Bangalore at 7 a.m., it takes me only 20 minutes to drive to

Electronics City [the industrial park in Bangalore where Infosys is headquartered]. At 8 a.m. it takes me about 40 minutes. But if I leave at 8.30 a.m., it takes me an hour. And this is one of Bangalore's better roads. Before it was built, I would spend two and a half hours waiting in traffic to come to the office or get home, and this is still the norm in many other parts of the city and in other Indian cities. These traffic conditions reduce your productivity and waste your time, and you're not in a very good mood when you get to the office or come home if you've just spent two and a half hours in traffic.

*In Aravind Adiga's recent novel Last Man in Tower, an exasperated resident of Mumbai complains: "Look at the trains in this city. Look at the roads. The law courts. Nothing works, nothing moves; it takes ten years to build a bridge." Why do such things function so inefficiently in India's cities? Is there a cultural reason why Indians accept these frustrations?*

Yes. Somehow, the staple diet of Indians is apathy. We see a problem around us and don't do much about it. The government doesn't act with a sense

of alacrity; there's so much legislation still pending with the parliament. What many countries take six months to complete, we most often take several years to do. Our nature, our natural pastime, is apathy. My interpretation is that it's because we were under foreign rule for 1,000 years — for the whole of the last millennium, except for the years since we got independence from the British in 1947. We weren't in control of our destiny, so we weren't responsible for designing a better strategy for our society. It's natural for a nation like that to take a little time to bring back a sense of urgency, to bring back a sense of self-created destiny and alacrity.

*Is that what entrepreneurs like you have injected into Indian society?*

I think so, yes. I have a fetish for quick action because of the apathy I see around me. My children make fun of me: they say, "We shouldn't discuss anything with dad because he'll go ahead and do it immediately!" But there are many people in the country, particularly in the private sector, who have now realized the importance of speed.

*After revisiting India in 2011, Thomas Friedman, the author of The World is Flat, warned: "As much as I'm impressed by the innovative prowess of India's young technologists, without a government to enable them with the roads, ports, bandwidth, electricity, airports and smart regulations they need to thrive, they will never realize their full potential." Is he right?*

Absolutely, he's right. I do think that India has done well to get to the current orbit. But for us to move to the next orbit, we need good leadership. For us to bring prosperity to the vast majority of Indians and to enjoy inclusive growth, we will have to enhance our governance system, enhance our transparency and accountability, combat corruption, and enhance our infrastructure.

*The government has called for \$1 trillion in infrastructure spending. How can this enormous investment be funded, particularly at a time when India's finances are already stretched?*

Developing nations like India need to seek huge foreign investment and huge debt from abroad to build our infrastructure, then make ourselves more

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productive and competitive on a global scale, sell more, then pay back these loans. There's no other model in the world. It's happening in some areas already: India's IT industry is very competitive, and some auto companies are very competitive. But it has to happen in many other industries.

*Some infrastructure sectors in India have been privatized or partly privatized. How successful is this proving to be?*

The airports and some ports have been privatized, and they're working pretty well. Power production is open to the private sector, but power distribution is still in the government's hands in most states, so it's not working as well. There are huge losses in transmission, and there's a lot of theft of electricity. Several state governments give free power to farmers, and that's causing some strain. And the state governments aren't able to pay power manufacturers on time. So, it's a mixed bag. Unfortunately, we've looked at this situation piecemeal, not holistically. The solution is to

look at the entire supply chain and bring in the participation of the private sector.

*Does the success of technology companies like Infosys suggest that private enterprise is the most effective driver of economic progress in India, not the government?*

The software industry is a good example of how the private sector can add tremendous value to the economy if the government takes a back seat and acts as a catalyst. In our area, the government did a good job of promoting the Indian software industry abroad. The moral of the story is that the government should become a catalyst, listening to the people in the trenches who are producing goods and services, then creating laws and rules that will make them more competitive.

*What should the government do to foster more entrepreneurship?*

First, we have to enhance our higher education system by creating greater interaction with well-known universities in developed countries like the U.S., the U.K., Australia, France,

Germany, and Japan. Second, we need regulations that attract the best venture capital firms to India in even greater numbers. Third, we have to create a business environment for entrepreneurs where there's very little friction created by bureaucrats. Today, it takes several days to even register a firm. And smaller entrepreneurs suffer under the tyranny of petty bureaucracy in terms of factory inspectors, tax inspectors and so on. We need to shield them from this bureaucratic tyranny at the state and central level.

*What advice would you give to foreigners who are, nonetheless, looking to invest in India?*

One of the drawbacks of our system is that the rules and regulations are not very transparent. They're not very explicitly written in simple English that can be understood by you and me in the same way. Therefore, there's an opportunity for misinterpretation by the bureaucracy — and, when there's an opportunity for misinterpretation, there's a possibility for rent-seeking. That's something that foreign

investors don't like because they're used to open, clear rules. So, I'd advise them to use well-known Indian lawyers and make sure these lawyers look very carefully at whatever contracts they're writing, and also look at all the previous case studies.

*Some foreigners are also scared off by the perception that corruption is still too pervasive in India. How hard is it to avoid corruption?*

In fairness, at Infosys, we have not paid a single cent in bribes in the last 30 odd years

of our existence. Therefore, I do believe it's possible to do business with the government without any bribery as long as you're willing to accept a certain delay in the processing of applications and approvals. And if you demonstrate that you're not going to give any bribes the first time, the second time they won't ask you. So, my advice to any foreign investor is to be firm in being honest and in not succumbing to any such bribery situations the first time; the second time, you won't have to worry about it.

*What's the best way for countries like India to tackle chronic corruption?*

Simplification of laws, transparency of procedures, and the willingness of business people to accept delays in the beginning. For any nation, these instruments will go a long way towards combating corruption.

*India has made spectacular progress over the last 20 years. When you look at the next 20 years, what makes you fearful and what makes you hopeful?*

I've seen a new sense of confidence and hope amongst Indians in the last 12 years as

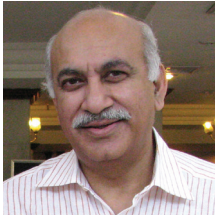
they've watched our country moving forward, our GDP growth rates increasing, our software companies succeeding, our banks becoming smarter and smarter. Even though we have problems, there's confidence today that we'll be able to solve these problems — if not tomorrow, then at least the day after. That's the biggest transformation I've seen in the psyche of India. This confidence is extremely important for a nation on the go.

Infosys Electronics City, Bangalore.

*When the economy grows at this rate, it's only natural that there's huge pressure on infrastructure. Even though we've been building infrastructure, we're not able to keep pace with demand. That results in huge productivity losses.*



## Learning along India's tumultuous path to progress



One of India's most renowned journalists, M.J. Akbar is the Editorial Director of the weekly newsmagazine *India Today*; he oversees the TV news channel *Headlines Today*; and he edits *The Sunday Guardian*, a weekly newspaper. In 1989, Akbar left journalism for several years, winning a seat in parliament and serving as a government adviser on education. He is the author of eight acclaimed books, including *Nehru: The Making of India*, a memoir entitled *Byline*, and *India: The Siege Within*. Here, Akbar explains the flaws and virtues of India's political system, and he discusses the urgent need to confront such issues as power shortages, pollution, and a lack of clean water.

*India has made extraordinary advances over the past 20 years, but it still lags behind China. One reason is that the Chinese government is far more effective at making things happen — whether it's urban planning, completing infrastructure projects, or confronting threats like climate change. Do you worry that India's cherished democratic system, for all its virtues, hinders its economic growth?*

There is no tradeoff as far as India is concerned. India is not going to trade its freedom for any other reward. It's as simple as that. India cannot live except as a free country. We cannot survive except as a free country. We are a federal people. We have a federal history. We didn't remove the British in order to bring domestic tyrants who will then have to be removed by some Indian Spring. Whatever the disadvantages of democracy will be, we will have to live with them. Nobody in India thinks of bread versus freedom as a debate. The key to India is that its future is being determined by democratic pressures. For example, India's poorest find

the whole idea of the trickle-down theory to be absurd. What is the trickle-down theory? Does it mean that those few who have swimming pools will get a waterfall and those who are dying of thirst at the bottom will get a trickle? In a democracy, you can't sustain that sort of thing. The core reality here is that if governments do not deliver in terms of growth, then they become vulnerable.

*When you look at what's holding India back, obviously one of the biggest issues is inadequate infrastructure. How big an impediment to India's economic progress is this infrastructure deficit, which you see everywhere from railways and ports to an insufficient supply of water and electricity?*

It's a huge impediment. How can you be honest and not understand that? But there are models within India that prove that things can be done, despite the impediments of democracy. Good governance can begin to make a difference, which we've seen in places like Bihar and Gujarat. What we should not expect from India is either

horizontal or vertical evenness. There will be curlicues and knots in the graph. There will be problems along the way. There will even be accidents. We see it on the Indian highways, which are littered with overturned trucks because Indian drivers lose control and don't respect rules. But even if we just equal over the next 20 years what has happened over the last 20 years, you are going to see a country which is very definitely at the top edge of the second world. Not the first world, but definitely the second.

*One long-term challenge is a lack of clean water, given the vast scale of urban development across India, the depletion of the nation's underground water supplies, and the growing problem of pollution. How concerned are you about this need to secure adequate water for India's rapidly-growing population?*

That's a huge problem. In fact, that's one of the great failures of Indian governance — this inability to have even a rational plan for water resources. It's extraordinary, but I don't think



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Mumbai train station.

anyone is even thinking about what huge catastrophes await us. To begin with, three of our major primary river sources are in Chinese hands: the Ganges, the Indus and the Brahmaputra. They all come from that part of the Himalayas which is controlled by China. The second problem is the mismanagement of water. It's a crime, the levels of water that are used by farmers in excess. What you need is a government that really begins to put its best minds to work on the issue of water resources.

There was only one minister in my memory who really understood the problem and wanted to do something about it. Then he was, alas, removed, possibly because he was not corrupt enough. The cost for water that will have to be paid by the urban consumer is going to become absolutely astonishing because the Indian government and political parties find it impossible to deny rural India. Water has to be privatized. It is becoming increasingly privatized because the public sources of water, the taps, are dry. People are now having to buy water in tanks.

*Is there a sense that environmental issues like this are becoming a more mainstream concern in India? Do you see, for example, a greater focus on building more resilient urban infrastructure to deal with the growing dangers of climate change?*

Indians love to argue. So there's always a big debate going on about the environment. It's one of the many issues that create turmoil. What I can't see is any resolution to the debate or any major policy emerging from the debate. At the moment, over the last two or three years, the government is so distracted by trying to save its skin and survive that it just doesn't pay any attention to the issue — at least, not as much attention as it requires. The issue is there. Everybody recognizes the issue. But then what should be done about it? That becomes a separate issue. But these things that I'm saying are rooted in time: in the future, we might have a government with rational priorities.

*For India to sustain the remarkable economic growth that it's racked up in recent years, it will need to generate a massive amount of electricity. Yet the inadequacies of the country's electricity system have created a serious economic bottleneck. Is anything being done to address this need for a more dependable supply of energy?*

The only thing the government has done is involve the private sector in electricity production and distribution — and then left the private sector to try and manage the social realities without the influence of the state. That doesn't sound very intelligent. Can you see such a situation working effectively? The point is that we are neither white nor black: we neither have free market freedoms nor state sector monopolies. These private sector companies are expected to deliver in terms of their corporate business plans, but they don't have the cushions available that state-owned monopolies enjoy. One of the great problems that industry faces is a completely opaque government, which then goes

on changing the rules after decisions have been made. The government has to know what it wants to do and then stick to that. The government must be a guarantor of law, if nothing else, and provide rules and regulations which have clarity. I think time will clarify these things. Experience will. The people's anger will. Let's see.

*Foreign visitors are often struck by the disarray they encounter in India — from the electricity blackouts to the chaos on overcrowded trains. Why is it that basic infrastructure like this remains so dysfunctional?*

In many of these cases, the government doesn't have the ability to subsidize large corporations of this nature because its own resources are obviously limited. But more than resources being limited, the problem is that the forces that bring modernization will not arrive because things are under government control, and the government lives by bureaucratic rules. Modernization needs entrepreneurship.

*How big a problem is inadequate infrastructure for India's poor — whether it's insufficient electricity, say, or a lack of clean water? Are they the ones who suffer most from these problems?*

The real problem is that the poor still don't think they're getting their share of economic growth. They need much greater compensation from employment to create economic uplift.

*One area where India has made tremendous progress is in telecommunications. How important has the liberalization of the telecom sector been, and how significant an impact have you seen from the growth of India's major telecom companies?*

Telecom is one of India's great success stories. Look at the empowerment of hundreds of millions of Indians. Today, the postcard is dead. The letter is dead. Communication is cheap, and that's had a huge positive effect in villages and at the low-

est economic levels. The quality of life for the poor has improved so dramatically because they can communicate with their loved ones. Otherwise, if you came from Bihar and lived in Bombay, you were cut off. How much could you convey in a letter without a mobile phone? So it's been a huge benefit.

*What needs to be done in terms of reform to encourage more entrepreneurship and to bring greater investment where it's most urgently required?*

We would have to do the same thing in other areas that we did to roads, which is to have clarity in the system of public-private partnerships. And then comes the most difficult part, which is to eliminate or, at least, curb chronic corruption.

*How big an obstacle is corruption to India's economic development?*

Quite substantial. Corruption doesn't simply create a transac-

tion that has to be factored into the business plan officially or unofficially. What corruption does is it creates space for the incompetent to buy their way into the most important sectors of India's economy.

*How can you prevent this type of insidious, pervasive corruption?*

It's difficult because democracy is a very hungry and thirsty beast, and the cost of elections is rising. So that's one of the real problems.

*In some ways, India seems to have moved backwards lately, with less progress in terms of reform and little decisive government action. Is that a concern?*

Yes, the momentum seems to have stalled a bit. That is because of the absence of governance, rather than misgovernance. But give us another 12 months and let's see.

*When you look at these almost intractable problems like corruption and a lack of political leadership, it must be easy to lose hope. What is it that nonetheless makes you optimistic about India's future? Is it encouraging, for instance, that so many regular Indians took to the streets over the last year to protest against corruption and to demand change?*

The fact that people are angry and can mobilize their anger and unseat governments is cause for enormous hope. We saw this with the recent election results in Uttar Pradesh [India's most populous province], where the establishment was wiped out and those who thought that rhetoric was sufficient for victory were told to forget it. Now, everybody knows that if an elected government doesn't deliver, then it will be in for its own disaster. We don't really need a sudden volcanic outburst because we have a system in which the guilty can be punished electorally. This is the dividend of democracy.

*Corruption doesn't simply create a transaction that has to be factored into the business plan officially or unofficially. What corruption does is it creates space for the incompetent to buy their way into the most important sectors of India's economy.*



Calcutta Stock Exchange.

## To discuss the issues

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