Parsimony and politics are not natural bedfellows

India After The Global Crisis

By Shankar Acharya

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It is sometimes difficult to review books written by friends or those who you know well. There are instances where amity compels politeness and gentle phrases of muted non-meaning praise when the truth is quite different.

A reviewer doesn't face any such constraint with Shankar Acharya's works. Because Acharya has two outstanding characteristics as a commentator on matters economic. First, his logic and use of facts are impeccably sound, as they always have been either in drawing room debates or in essays and articles. Second, and no less important, Acharya writes excellent English — an attribute that is fast disappearing among many, particularly the new experts of the dismal science.

Let me therefore start with the kudos. This book, a compilation of Acharya's articles that have appeared in the *Business Standard* (*BS*), contains many gems. There are eight sections, all titled in a rather prosaic manner: Global Crisis Aftermath; Economic Growth; Reform and Economic Policies; Employment and Human Development; Budget and Fiscal Policies; External Sector Policies; and General, which has three articles that Acharya couldn't quite slot into the other seven.

I don't want to examine each section. Instead, allow me to touch upon a few choice articles.

The first is "Retreat of the Master", (pp 50-54), which is reprinted from *BS*, 24 June 2010. The Master is John Maynard Keynes, whose tenets were splendidly resurrected throughout the developed world in 2008 and 2009 — when all but certified lunatics believed that massive and sustained fiscal stimuli was the only way to prevent the global crisis from becoming another Great Depression. Keynes' best biographer, Robert Skidelsky, marked the occasion with a new book called *The Return of The Master*. Acharya's key observation is that Keynesian reflation through pump priming came to an end after two years, occasionally three, when major western economies realised that the deficit and public debt had gone out of control.

Then came the Greek sovereign debt crisis, the shaky state of Portugal and question marks about Italy — and we were back to raising taxes and severely cutting government expenditure, as the International Monetary Fund (IMF), the European Central Bank (ECB) and German chancellor Angela Merkel would readily prescribe. The only exception to this dramatic *volte face* was the USA. Acharya writes, "The astonishingly swift change in the prevailing macro-policy paradigm was both remarkable and unsettling. It also raised doubts about the foundations of macroeconomics."

Perhaps not. There is little doubt that the events of 2008 required massive government intervention *a la* Keynes. For major nation-states to think otherwise would have been suicidal for economics and politics. However, opening the expenditure tap has its problems. Bureaucracy loves it; as do most politicians. After all, more money for hundreds of programmes, many resurrected from the dark side of the moon, is great for power and prestige. Parsimony and politics are not the most natural bedfellows. Soon enough, saner heads across Europe and even the USA realised that such bounty via the treasury's printing press could not last. The debt burdens were too high for future generations of income earners and tax payers. This, and the strains of the Euro Zone exacerbated by Greece as well as Portugal, forced the reversal.

To me, the interesting question to ask – which Acharya tangentially touches upon but does not elaborate on – is the body language of increasing government expenditure. All of us who have grown up with admiring the logic and elegance of Keynes realise that most economies which embrace the route of determined deficit financing to stave off a possible depression don't know when to get off, and how. The backtracking, when it occurs, is often too late in the day and, therefore, politically painful. Consider India. After several years of restraint under ex-finance minister P Chidambaram, Pranab Mukherjee systematically jacked up the fiscal deficit to a point where the consolidated number is around 9 per cent of GDP. This was initially in response to the global crisis. Thereafter, it took a life of its own — pandering to all possible political needs of the coalition government, real or imaginary. In the last budget, Mukherjee promised to bring down the deficit to GDP ratio by 2 percentage points. Now that he has moved to the splendid mansion atop Raisina Hill, it remains to be seen whether his successors will have the political gumption to reduce expenditure, when state-sponsored improvidence has become the leitmotif of governance.

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The second article of Acharya's that I would like to touch upon is his "New Threats to Growth" (pp 78-83), reprinted from *BS*, 13 January 2011. The essay is about India, and Acharya raises exactly the issues that any right-thinking economist ought to highlight. These are (i) return of the twin deficits, fiscal and current account, (ii) inflation, and (iii) rapid slowdown in private investment.

As mentioned earlier, thanks to UPA-2's determined profligacy and lack of any economic governance worth the name, the combined fiscal deficit has risen to 9 per cent of GDP. In addition, the current account deficit is around 4.5 per cent of GDP. Moreover, inflation remains stubbornly high. When Acharya wrote this piece, double-digit inflation was being driven by both energy and food prices. Today, crude oil prices have come down from over $140 per barrel to around $80; but the prospects of poor monsoons will certainly increase food inflation. In any event, it seems unlikely that wholesale price inflation will rule below 7 per cent for any reasonable period of time.

This high and persistent inflationary overhang makes the Reserve Bank of India (RBI) very skittish and loath to reduce interest rates. Which, in turn, puts a dampner on much needed private sector investment — a vitally necessary instrument for cranking up growth and employment.

When Acharya wrote this article in early 2011, there seemed to be no clear solution in sight. Eighteen months later, the situation has worsened with India's GDP growth slumping to 6.5 per cent in 2011-12 versus 8.4 per cent in the previous year — and the government dithering and stumbling at every step.

The article that I like the most in this collection is "Ten Myths of Indian Economic Policy" (pp 110-14), reprinted from *BS*, 14 January 2010. Here are my four choices out of the ten:

Higher minimum support prices for foodgrain are good for farmers. Not quite. These are great for wealthy farmers. Certainly not so for millions of small peasants and landless sharecroppers who have to buy a large portion of the cereal needs from the market.

Our labour laws protect labour. Absolutely not. These protect a really tiny minority of unionised and government-employed workers, at the expense of the vast majority of the workforce. With the laws making it extremely difficult to be flexible with the labour force, we actually encourage less hiring than we should — and thus build greater pressure on unemployment.

Subsidies on food, fuel and electricity mainly help the poor. This is palpably incorrect. The great majority of India's truly poor have no access to subsidised foodgrain. Nor, too, to subsidised kerosene. And least of all to subsidised electricity — which has actually bankrupted almost all state electricity boards and has created hours and hours of darkness in our towns and villages.

The trader/middle-man is the root cause of many of our economic problems. While it may be argued that our trading systems with myriad intermediaries remain anchored to the late 19th century, the idea that any economy can function without trade between producers and the final consumers is utterly absurd. Those who believe in this, especially agencies within the central and state governments, have actually distorted trade links by trying to create so-called dis-intermediated systems, only to the detriment of all.

As I wrote at the beginning, this collection of Acharya's articles is a delight to read. If I had to be critical, there would perhaps be one comment worth making. Acharya is unfailingly polite in his critique of government policies and actions. Perhaps it is because he is unfailingly polite *per se*. It is equally possible that he is constrained to sharply criticise Manmohan Singh, who he worked for in the 1990s, and whom he holds in high personal regard.

Be that as it may, Acharya's continuously understated and polite style runs the risk of occasionally taking away from the innate strength of his critiques. My request is that in his future articles and essays, Acharya becomes more forthright and sharper in his critical discourse. It will add heft to his huge portmanteau of reason. ■