

BOOK REVIEW

AN ECONOMIST IN THE REAL WORLD BY KAUSHIK BASU THE ART OF POLICY MAKING IN INDIA

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“An Economist in the Real World – The Art of Policy Making in India” Kaushik Basu 2016 Published by Penguin Viking Rs. 599/-

The Chief Economic Advisor to the Government of India is a very important senior level position. It has been held by men of eminence and intellect with the capacity to lead National discourse on Economic Policy Making through their writings and interviews. In December 2009, Kaushik Basu joined this elite group of distinguished men who had a bird’s eye view of economic policy-making in India and contributed immensely to addressing the challenges of the Indian economy for the period 2009-12.

I cannot remember any of the Chief Economic Advisors of recent past, Ashok Lahiri, Arvind Virmani and Raghuram Rajan, writing books on their years in office. 2009-12 was a very difficult period of macroeconomic policy making with slowing growth, high inflation, commodity price volatility, high interest rates, low investments, widening current account deficits and sluggish exports. I felt a certain level of curiosity when I saw the book in the stands and picked it up immediately. As I read through the preface, I noticed that Kaushik Basu felt that it is too early to publish his Delhi Diary for his two and half years in Government. He has set the book in a broader framework for policy makers to understand the longer-term policy formulations in Government.

As Kaushik Basu says it is a book on the Indian Economy and the art of policy making, blending economic theory with personal experience. It is clear that the man is an academic first and a reluctant policy maker later. The policy

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analysis on India's growth rates, inflation management etc are set in a global and local context in a longer term perspective indicating institutional positions and responses developing over a period of time. The book is lucid reading. I was quite impressed with the simplicity of writing and the manner in which narration covers India's complex economic story in a manner that totally engrosses the reader.

Kaushik Basu's analysis of the Indian Economy is divided into 10 chapters – India's growth Story: Stagnation, Crisis and Take off; Inflation: The Emperor of Economic Maladies; Fiscal and Other Macroeconomic Policies for an Emerging Economy; Globalization and the Challenge of Development; Food and Poverty; The Nuts and Bolts of the Economy; Law and Economics; The Social and Organizational Foundations of Economic Development and finally the Road Ahead.

August 9, 2009: Kaushik Basu's meeting with the Prime Minister indicates the importance attached in Government to the selection process of the Chief Economic Advisor. It is evident that the Prime Minister recognized Kaushik Basu as a man of high meritocracy and requested him to join the Government. Basu took up the offer and joined the post on December 8, 2009. It is interesting to note the advise Basu received from Amartya Sen, to make sure that no sentence conveyed some unwarranted message but also that no consecutive set of words within the sentence conveyed a wrongful message. The Sen Rule is very good advise to any policy maker and Kaushik Basu adopted it well.

The Chapter on India's Growth Story commences with the coffee house discussions in Delhi School of Economics. The emphasis of Indian policy makers in the initial years was openness in books, films and ideas but closed in economic policies. Sky-high tariffs blocked import of goods and foreign direct investment was blocked as India set up an economy strung up in rules, regulations and permits. The rising fiscal deficits and internal/ external borrowing could be sustained when the going was good, but in 1990-91 in the aftermath of the Gulf war, India was teetering on the verge of default on

international borrowings with a mere USD 5 billion in foreign exchange reserves. Kaushik Basu examines India's growth trajectory from 1950-51 to 2013-14 and says that the first growth surge was seen in 1975-76 because the Emergency created fears contributing to efficiency. The adoption of economic reforms under the International Monetary Fund's Stand-By arrangement, reduction in tariff rates for imports, easing up of foreign exchange controls represented a clear policy break from the economic policies that resulted in the Hindu Rate of Growth.

The momentum of the reforms of 1991-93 resulted in a growth surge from 2003 onward and more markedly after 2005. Fiscal consolidation, increase in investment and savings rates took growth rates to over 9 percent for 3 consecutive years from 2005 to 2008. The Indian Growth Story was noticed by several leading economists of the world and recognized as one of the most important of our age. The slowdown in the US economy following the financial crisis of 2008, caused global contagion adversely affecting India. There were other factors like policy inertia and monetary tightening by Reserve Bank of India as also a slowdown in the European Union economies due to a debt crisis. For India to return to 8.5 percent growth rate, the fundamentals remain sound – democracy, economic liberalism, high savings and investment rates.

In the Chapter on Inflation, Kaushik Basu says that starting from 2009, India had 5 consecutive years of inflation ranging from 7 to 11 percent per annum where commodity price spikes frustrated people, adversely impacting the poor. High inflation rates were seen in many countries like Russia, Germany, in the 1940s and Brazil from 1962 to 97 where lengthy periods of double digit inflation have impacted growth rates, setting growth rate back significantly. Tighter monetary and fiscal policies brought down inflationary spurts. In India the wage hikes of bureaucrats and industrial workers are directly indexed to the consumer price inflation Index. There was also a distinct difference between the food and non-food inflation with stubbornly high food prices caused by hoarding. The financial inclusion program with lacs of people putting money out from under their pillows and putting them into bank accounts contributed to inflation. The RBI and the Government used a

number of instruments to manage inflation including the repo, reverse repo and cash reserve ratio. In a global context, in 2011-12, there was stagnation in the industrialized countries including United States, European Union and Japan while there was inflation in almost all the Emerging Market Economies including India, Argentina, Brazil, Vietnam and China. The world witnessed a “Salad Bowl of Stagflation”. This is likely to last for some time and an imperative need for coordination of macro-economic management policies across Nations.

The chapter on Fiscal and Macroeconomic Policies starts with the grandmother’s advise “don’t live beyond your means”, be responsible spenders and keep the gap between what you spend and what you earn as low as possible. The global financial crisis of 2008 saw a virtual policy revolution, with Nations using fiscal policy as a weapon to restore growth. The Keynesian approach of Governments overspending by running larger fiscal deficits to compensate for lack of spending by private firms/ ordinary individuals was effectively adopted in India restoring growth from 6.7 percent in 2008-09 to 9 percent in the succeeding 2 years.

Kaushik Basu argues for caution in issue of Government guarantees to large projects, which may not affect the fiscal arithmetic but amounts to undertaking future fiscal expenditure, and reiterates the advise of international standard bearers not to give guarantees to investors especially for private sector initiatives. Strategic government assurance is a powerful instrument to be used with care and Governments cannot rush into providing reckless guarantees.

On the issue of Exchange rate management, Kaushik Basu does not support the policy of export promotion through strategic central bank interventions, differing with the Chinese policy of fixed exchange rates and large foreign exchange reserves to boost exports. He supports India’s commitment to a floating exchange rate, curbing exchange rate volatility to keep the real economy stable and current account deficit within certain limits. The author refers to the conundrums in managing and predicting macro-parameters

saying that political leaders have to restrict themselves to making fatuously positive statements which should never be taken as forecasts as what they have to say about the economy affects the outcome. It is a conundrum faced by most of the Chief Economic Advisors too.

The Chapter on Globalization and the Challenge of Development is placed in October 2010, with President Obama asking Kaushik Basu to give some tips to the United States Treasury Secretary Tim Geithner. The author highlights the globalization challenges that exist in development, mentioning the impact the downgrading of sovereign credit rating of United States by Standard & Poors on the cost of hilsa fish in Chittaranjan Park fish market in Delhi. The downgrading of the US economy hurt China badly as it held a lot of foreign exchange reserves in dollars. Any substantial decline in the value of the dollar will be resisted by the 2 largest economies of the world. The developments in the euro zone have an important impact on the rest of the world. The quantitative easing by injecting liquidity into the economy by the United States has resulted in the salad bowl stagflation with inflation and growth in some countries and no inflation and no growth in others. When the US interest rates rose, money started to flow out to emerging market economies resulting in sharp depreciation in currencies. In the Indian context it led to an increase in exports. The author does make a pitch to address global inequalities particularly the challenge of addressing food deprivation and the poor.

The chapter on Food and Poverty indicates that even after 2 decades of steady growth 240 million Indians live below the poverty line. India has run a slew of anti-poverty programs since Independence, cheap food for needy, employment to the poor, cheap loans for people wanting to start business, interest subsidies for farmers etc. which did not have the intended results. The author questions India's food policy saying that the quantum of food stocks that the Indian government continued to hold during the period of high prices did not enable it to successfully even out the fluctuations in food production. The strategy for releasing food grains in India has scope for improvement. The food grain policy needs to be redesigned to fulfill the Right to Food conferred upon the citizens. The author's ideal food grain policy has two

components namely (a) the government should maintain the buffer with an aim to using it to hold down prices during times of food shortage and (b) the government must make sure that the poor and the vulnerable have access to food grains. The right to certain minimal amount of basic food is an achievable right.

The chapter on Nuts and Bolts of the Economy refers to the chapter on “Micro-Foundations for Inclusive Growth” in the 2009 Economic Survey of India highlighting the need for to focus on nuts and bolts matters in the rough and tumble world of macroeconomics. India has scope for improvement in formal enforcement of contracts. India is low on contract enforcement which is a pivot for growth and enterprise.

The chapter on Law and Economics focuses on India’s anti-bribery laws – The Prevention of Corruption Act, 1988, bribe taking and bribe giving are equally wrong. In the event of conviction, both the taker and giver are equally punishable. This is important in the context of harassment bribes in which large corporations are asked to pay a bribe for something which they have a legal entitlement. The issues of harassment bribery have been dealt with extensively and needs to be drastically cut down. The author opines that improvement in growth rates are possible if legal enforcement is strong, and cites the case of Bihar’s growth spurt from 2006-12.

The chapter on The Social and Organizational Foundations of Economic Development says it is important for developing countries to lay emphasis on the social and institutional drivers for economic growth. Economic policy can be run effectively if the social cultures are supportive., for example adherence to time, teacher absenteeism etc. India’s low rank in the Doing Business rankings is not surprising given the need for multiplicity of clearances which slows down the decision making process significantly. The administrative system needs to be reformed to give the Nation a burst of life and growth not seen in recent history.

The concluding chapter The Roadmap Ahead, the author says that India is at the crossroads. The prospects of a major take-off are real in way never seen before. India has invested in an open, secular, democratic society with a progressive foreign policy with a natural alignment of interests with the United States. India has nurtured higher education and research and creativity and this emphasis has enabled it greatly. India has the potential to become a global hub for education. There are large National gains from the investments made in higher education. The author concludes by saying that Nationalism of the day must make way for a global agenda that all peoples, irrespective of their narrow identities, can shape and cherish.

A thoroughly enjoyable read, strongly recommended.

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