L – 1/13 (GF), Hauz Khas Enclave
New Delhi 110016
(+91 11) 46113750 41654982
contact@karkiassociates.com
www.karkiassociates.com

KarkiAssociates
STRATEGY • ORGANISATION • GOVERNANCE

Market or Business Friendly[1]

The Axes of Inefficiency and Corruption

- Dr. Rajnish Karki[2]

The election of mid-2014 was a watershed for India's political economy. It marked the shift and coming of age of a new polity, that reflects and builds upon the process of economic reforms since the early-1990s. A government that believes in markets and globalisation as a matter of conviction and is open and unequivocal about it, or that's right of centre in economic thinking, was ensconced in the seat of political power in India. This is a far cry from the left of centre 'planned – self-sufficiency' oriented governments earlier, especially till the late 1980s. The election having resulted in an absolute majority, after nearly quarter of a century, underscores the decisive shift in India's politico-economic beliefs and aspirations, as a nation and at large.

The expectations of sharp and swift improvement in the economic well-being, naturally ran high, especially in the business community. Indian stock market indices rose over 30% during the first year, in sharp contrast to most of their overseas peers and without much change in the corporate earnings, underscoring the heightened expectations from the political economic shift. However, after two years, there is a widespread feeling of disquiet and being short on expectations. That's in the backdrop of macroeconomic parameters having improved to about their best levels in decades, and there being no slackening or change in the convictions of ruling party and no denying the sincere and hard at work intent of leadership.

Some disquiet can be attributed to the emotions and hype built into a major election outcome and to the lag between initiatives and impact. This will get moderated and even out over time. Much of being short on expectations, though, relate to a couple of fundamental reasons. One, misplaced understanding of the role of government in a market economy in the country, so that a right of centre government will be business friendly is taken as a corollary. Two, lack of understanding of the process of change in governance along the axes of corruption and inefficiency, let's say high on both counts to becoming better and moving across diagonally.

The government – business relationship in India is a case of distortion and of convoluted evolution. Government decided to be the lead creator and driver of

[1] Published: https://indiastrategyforum.wordpress.com, 27 April 2016
[2] Dr. Rajnish Karki specialises in strategy and organisation, more details at www.karkiassociates.com/profile.html

economic enterprises early on, soon after independence. The private businessmen and enterprises were to be there but on the periphery. And they consequently evolved skills in gaming the system and their orientations and approaches became deep seated over the decades. The reforms of early 1990s changed rules of the game. But in the government linked sectors the old ways continued and they re-asserted and became pervasive again in the last decade.

The 2014 election saw a reaction to the enhanced discretion and regulation, for instance the environment, and to the incessant scams and paralysis of governance. The new government was expected to be business friendly, which broadly translated to the expectations of higher corporate growth, profitability and stock prices and of favourable deals and easing of financial and other problems by many. This was misplaced, actually dangerous, at the conceptual and operative levels and for the government as well as the corporate sector.

The role of a government in the market-globalised economic framework, are essentially three-folds, to enhance and sustain growth, promote competition, and build regulation and institutions where market forces tend to fail or are inadequate. And the government ought to be market friendly. This is broadly aligned with being 'business friendly' on growth, but is clearly separate and opposed on the latter two. On growth too, while the expansion and diversification of existing businesses is important, the greater focus of government needs to be on the formation of new enterprises and on the micro and small ones.

The gains of market economy accrue to nation and people at large when there is greater competition, in the form of better products and lower prices. We have seen it happen across sectors, such as consumer electronics and automotive, since economic reforms of early-1990s. The greater competition meant heightened pressure on the existing businesses to improve functioning, and it did affect profitability on the whole and in the short run and some truly inefficient enterprises faced of existential threats. There were howls of protests and lobbying in mid-1990s, but bulk of the Indian companies responded well and learnt to compete and thrive. We are seeing a repeat from some quarters, especially from companies that became reckless in expansion and debt during previous decade and from those who are currently facing troughs of global and industrial cycles. It's their problem, not of the government.

Markets do not work well, when business comes in contact with government. The government could be a customer or a provider of essential, irreplaceable resource, i.e. land, mining, drilling rights, spectrum, or a regulator. The businesses are expected to pursue their interests at all times and to try play with the rules and interfaces some of the times. While the interfaces as customer are in need of micro and incremental improvements and as provider are have been largely sorted, the regulatory part is the weak link in India's market economy. There is notable progress, though in some areas, in the quality of regulation and enforcement, for instance the stock markets, telecom.

Our regulatory and institutional framework and its governance, is high along the axes of both corruption and inefficiency. Instead of continuing on the path of becoming robust and better, the institutional environment actually deteriorated in the past decade. The incoming government needed to reverse the tide and move diagonally across the axes towards being non-corrupt and efficient. The leadership has broadly stuck to the task and made determined moves on several fronts. At the least there is little evidence to the contrary, and the abatement in breaking out of periodic scams during the last two years, does point to the reversal in trendline.

The business doesn't like inefficiency in governance but it's stance on corruption could be ambivalent. There is a sizeable proportion of Indian enterprises and groups who have grown by gaming the system for decades and the consequent attitudes, approaches and capabilities are intrinsic to their identity. Change of trendline in governance will disadvantage and discomfit such groups and the disappointments and protests will tend to follow. But the right and proactive stance for them is to change their ways of doing business, some of which certainly will be painful. Similarly, the set of companies who managed exclusive access to coal licenses earlier and at below-normal prices would be at a loss from the improved governance.

In a market economy, the effective governance cannot but be low on corruption as well as inefficiency. And the government ought to push diagonally along the axes determinedly and consistently. This is akin to any change dynamic, where a move creates constituencies of winners, losers and those in zone of indifference. The current government has the mandate and needs to show the requisite wisdom and skill in managing the change dynamics – and move as fast and as far along the decidedly correct and clear path. The economy and the people at large are better off when the market is growing, competitive and well-regulated on the watch of a non-corrupt and efficient government.