

The Iconization of Chandrababu:

Sharing Sovereignty in India's Federal Market Economy

Economic and Political Weekly, Vol XXXVI, No 18, May 5-11, 2001

Lloyd I. Rudolph
Susanne Hoerber Rudolph
University of Chicago

In the 1990s India moved from a command economy to a federal market economy. Under these new conditions, the states command a larger share of economic sovereignty than they did under the centrally planned economy. Whether they do well or badly economically depends more than before on what they do for themselves. States can act in ways that transform their initial economic situation; agency can modify structure. The surging growth of several poor states such as Rajasthan and Madhya Pradesh and the lagging growth of some rich states such as Punjab and Haryana suggests that poverty is not a trap and wealth no guarantee of continued success.

A necessary condition of a shift from a command to a federal market economy has been the economic liberalization policy launched in 1991 by the Narasimha Rao Congress government. Its sufficient condition, we argue, is the displacement of public investment by private investment as the engine of economic growth. The states have become the principal arena for private investment. Their competition for private investment has generated races to the bottom and to the top. States seem to be learning that it is better for them to forgo short term benefits and to adopt the mutually advantageous benefits of cooperation over the longer term. While the union government in New Delhi continues to loom large in the calculations of the states, it is transforming itself from the interventionist, tutelary state of a centrally planned economy and the permit-license raj to the regulatory state of a federal market economy. Its new role is to enforce fiscal discipline and to insure transparency and accountability in market and federal processes.

The New Imagined Economy

State Chief Ministers as Entrepreneurs

Ben Anderson gave us nations as “imagined communities,” Satish Deshpande gave us “imagined economies” and Tim Mitchell gave us the “national economy ...as a representation.”¹ Economies like nations can be understood as constructions, products of symbols and rhetoric as well as of theorists’ and practitioners’ concepts and categories. This paper starts with the contrast between how India’s economy was imagined in Jawaharlal Nehru’s day and how it has come to be imagined in the post-liberalization era, a centralized planned economy in the 1960s and a federal market economy² in the 1990s. Commonly understood as sites for “truck, barter and exchange” and getting the prices right, economies are also sites for symbolic dramas. In the symbolic politics of imagined economies, actors appear on a public stage. They speak from scripts that go beyond the positivist world of the professional economist, beyond the interests and preferences of capital and labor, consumers and producers, buyers and sellers. The federal market economy is populated by persons, places and relationships that constitute a coherent symbolic world.

In the 1950s and 1960s, the heyday of India’s five year plans, Prime Minister Jawaharlal Nehru cut a heroic figure as chairman of the Planning Commission that he put at the center of India’s industrial modernization. The Indian state would occupy the commanding heights of the economy. Nehru imagined big dams as temples for a powerful Indian nation. As the new millennium opens, the heroic age of centralized planning has become a fading memory. In the 1990s drama of economic

liberalization state chief ministers play leading roles in India's emergent federal market economy. They are seen on front pages, covers of news magazines and television screens, making and breaking coalition governments, welcoming foreign statesmen and investors, dealing with natural disasters and domestic violence. By March 1995 a perceptive Raja Chelliah could observe that

The relative spheres of activities of the two levels of the government have been thrown into a flux. The scope for real decentralization of economic power has been greatly increased and new vistas have opened up for creative and innovative activities by the sub-national level governments.³

By the end of the nineteen-nineties, state chief ministers became the marquee players in India's federal market economy..

What has attracted media and policy attention in recent years, is the competition among the states for international attention and for domestic and foreign private investment. State chief ministers and their finance and industries secretaries to government went abroad, to the US, Western Europe, Japan, in search of private investors, including NRIs. As the new millennium opened India's state capitals were attracting world leaders. Bill Gates and Bill Clinton in Hyderabad; Yoshiro Mori and Lee Peng in Bangalore. Clinton's visit capped Andhra Chief Minister Chandrababu Naidu's relentless efforts to be known as India's most successful chief minister. From Dallas to Davos, he promoted his ambitious plans to transform Andhra Pradesh from a middle rank into a top rank state.⁴ As leader of the Telugu Desam, one of a growing number of politically successful state parties, his efforts to promote and use information technology caught the national imagination. Earlier, counter-intuitively, it had been Jyoti Basu, the long serving Communist Chief

Minister of Bengal, who took the lead in aggressively wooing job and revenue-generating capital.⁵

By mid-2000 it was S. M. Krishna, Karnataka's Congress chief minister, who appeared to be showing India its economic future. As **Outlook** put it, "Watch out, Naidu, S.M. Krishna is winning both panchayat polls and investors."⁶ In a world of federal competition in which some observers fear that a race to the bottom will make all the states worse off, Naidu and Krishna seem to be pursuing a race to the top that could make both better off..

The defining event that shifted attention to the states as arenas of economic decision-making occurred in 1993 when the Government of Maharashtra [GOM], India's most industrialized state and home of India's pre-eminent global city, Mumbai, began negotiations with the Texas energy giant, Enron, to build a \$3.5 billion, 2000 megawatt power plant. The negotiations revealed the down as well as the up side of autonomy. States can seize the opportunity provided by the center's diminished influence and resources to shape, for better or worse, their own fates. On December 8, 1993 the GOM and the Maharashtra State Electricity Board [MSEB].⁷ signed a Power Purchase Agreement [PPA] with Dabhol Power Company, Enron's India subsidiary, for the supply of about 2000MW of power. Described as "one of the largest contracts [civilian or military] in world history, and the single largest contract in [India's] history," it involved total energy investment of \$3.5 billion over the life of the 20 year contract and, as estimated in 1996 on the basis of then prevailing indexed fuel costs, \$34 billion over the same period to be paid by the MSEB to Dabhol/Enron..

What matters about this event for our story is that the Government of India [GOI] played at best a supporting role. In September 1994, it provided a sovereign counter-guarantee, a decision it came to regret. The GOI's agents, e.g. a cabinet committee, the Finance Minister and the Central

Electricity Authority [CEA] opposed the project. So did the World Bank. The GOI was cajoled, bullied and, for all practical purposes, pushed aside by the GOM. whose actions some have called shady, fool-hardy or illegal. More recent reflections indict the project and its failure to use competitive bidding instead of non-transparently negotiated “memos of understanding,” as “a perpetuation of old command-and-control habits” and an invitation to corruption rather than an instance of liberalization.⁸ The actions were also potentially disastrous for the GOM and possibly for New Delhi, whose sovereign guarantee could make it financially liable if the GOM/MSEB finds it can’t pay its bills for the high cost electric power it is committed to purchase over the 20 years of the contract.⁹

As we write in 2001, eight years later, the financial and political ups and downs of the Enron deal continue to rivet the country’s attention on state level economic decision-making, although the initial optimism about attracting FDI has faded. Sharing economic sovereignty and economic decentralization carry hazards as well as opportunities.

Our use of the term “federal market economy” is meant to draw attention to the fact that the new imagined economy evokes not only the decentralization of the market but also new patterns of shared sovereignty between the states and the center for economic and financial decision making. This increased sharing shifts India’s federal system well beyond the economic provisions of its formal constitution. Over the last decade it has become clear that if economic liberalization is to prevail, it is the state governments and their chief ministers that can and must break the bottlenecks holding back economic growth. Can they and their governments negotiate a path that avoids surrender to populist pressures and yet effectively responds to the inequalities generated by market

solutions?¹⁰

If state chief ministers have become marquee players in the drama of the federal market economy, business leaders, economic regulators and a new breed of policy intellectuals can be found in conspicuous supportive roles. They overshadow the actors who in Nehru's time shared the limelight focussed on the centrally planned economy, the able but now almost invisible deputy chairman of the Planning Commission in New Delhi's Yojana Bhavan, K.C.Pant; the more visible Union Finance Minister, Yashwant Sinha, and other economic ministers and secretaries to government. As profit has come to be seen as a measure of productivity rather than as a symbol of greed and of anti-social gain,¹¹ the media increasingly depict India's business men [there are still few women] as persons to respect and emulate. Kumaramangalam Birla, Ratan Tata, Dhirubhai Ambani¹², the young heirs of old business houses and the energetic builders of new; the IT entrepreneurs such as Wipro's Azim Premji and Infosys' S. Narayana Murti, are persons with whom state Chief Ministers do business, the entrepreneurs and managers who are said to make things happen and make the economy grow. As India moves from a centrally planned, state-dominated economy to a decentralized federal market economy, the economic views, philosophies of life and ways of living of India's successful business men have come to attract some of the respect and admiration earlier enjoyed by the sentinels guarding the economy's commanding heights.

Also over-shadowing the images of an increasingly obsolescent Nehruvian interventionist state are the administrators and policy intellectuals of India's emergent "regulatory state,"¹³ persons such as RBI [Reserve Bank of India] chairman Bimla Jalan, SEBI [Securities and Exchange Board of India] chair D. R. Mehta, former NCAER [National Council of Economic Research] Director

General, Rakesh Mohan [now economic adviser to government], and CII's [Confederation of Indian Industries] Director General, Tarun Das.

The Federal Market Economy: Causes and Reasons

Economic liberalization, the dismantling of the "permit-license raj" and an increasing reliance on markets, proved to be an enabling factor for the emergence of the federal market economy. The dismantling of controls provided a window of opportunity for enterprising state governments. But economic liberalization tells only part of the story of the emergence of a federal market economy. It was a necessary but not a sufficient condition. Equally important was the marked decline in public investment and, as a consequence, of the center's financial leverage. Capital expenditure of both center and states

1. Benedict Anderson, **Imagined Communities: Reflections on the Origin and Spread of Nationalism**, London: Verso, 1983. "Communities are to be distinguished, not by their falsity/genuineness, but by the style in which they are imagined, 15.

The phrase, "imagined economies" is taken from Tim Mitchell's paper, "At the Edge of the Economy," presented at the South Asia and Middle East [SAME] workshop, University of Chicago, February 2, 1995. The argument about the recent invention of the idea of the economy is also made in Mitchell's "Fixing the Economy," **Cultural Studies**, 12,1, 1982, 82-101.

Satish Deshpande, "Imagined Economies; Styles of Nation-Building in Twentieth Century India," **Journal of Arts and Ideas**, 25-26, December 1993, 5-35. "If nations are indeed 'imagined communities' as Benedict Anderson has so persuasively suggested, then I would argue that one of the dominant modes in which the Indian nation has been imagined is a community of producers, as an *economy*....." 5-6.

2. We distinguish Barry Weingast's deductive use of a model, MPF ["market preserving federalism"], to assess and judge Indian federalism from our use of a Weberian style ideal type, a federal market economy, that enables us to organize our inductive analysis

of ideas and practices in India. Sunita Parikh and Barry Weingast conclude that "the Indian case far better illustrates what occurs in the absence of market-preserving federalism....India's federalism retains the hierarchy of federalism but eliminates the main mechanisms that sustain strong markets. States are not free to set their own economic policies. Nor can they capture the gains from policies that foster economic growth."

Sunita Parikh and Barry R. Weingast, "Response" to Jonathan Rodden and Susan Rose-Ackerman, "Does Federalism Preserve Markets?" and "Commentaries," Ronald I. McKinnon and Daniel Rubinfeld, in **Virginia Law Review**, 83, 7, October, 1997, 1611.

As will become clear from our analysis below, we come to quite different conclusions.

See also Barry R. Weingast, "The Economic Role of Political Institutions: Market-Preserving Federalism and Economic Growth," **Journal of Law, Economics, and Organization**, 11, Spring 1995.

3. Raja J. Chelliah, **Toward Sustainable Growth: Essays in Fiscal and Financial Sector Reforms in India**, New Delhi: Oxford, 1996, 19

4. In the annual ranking of states compiled by **Business Today**, which ranks 26 states according to the perceptions of CEOs about states as investment destinations, Andhra went up from 22nd in 1995 to 3rd in 1999. "State of the States," **Business Standard**, December 29, 1999. In so far as perceptions as much as "objective conditions" shape investment behavior, this is a consequential measure.

5. See Aseema Sinha's case studies of Bengal, Gujarat and Tamil Nadu in "From State to Market - via the State Governments: Horizontal Competition after 1991 in India," paper presented at the Association of Asian Studies Annual Meeting, Boston, March 11-14, 1999.

6. **Outlook**, June 25, 2000, 16-18.

7. Our account of the Enron episode is largely based on the carefully researched, highly critical book by Abhay Mehta, **Power Play; A Study of the Enron Project**, New Delhi: Orient Longman, 1999.

Also useful is Sidharth Sinha, "Private Participation in Power: Dabhol Power Company - A Case Study," and Sidharth Sinha, "Appropriate Return to Equity in Private Power Projects: Dabhol Power Project Company - A Case Study," in G. Raghuram, Rekha Jain, Sidharth Sinha, Prem Pangotra, Sebastian Morris, eds., **Infrastructure Development and Financing; Towards a Public-Private**

Partnership, New Delhi: Macmillan, 1999, 122-160 and 161-69.

8. Amulya Reddy, "Lessons from Enron," *Hindu*, January 22, 2001

9. In early 2001, Enron did indeed invoke the Government of India's sovereign guarantee when MSEB appeared unable to meet its payments for November and December, 2000. According to State Power Minister Padmasinh Patil this was no freebee for the GOM, as GOI "will, in turn, recover it from funds allocated to the State Government." **Business Line**, February 7, 2001

10. We are not alone in attending to the federal dimension of economic reform and decision-making. Rob Jenkins breaks new conceptual and empirical ground in **Democratic Politics and Economic Reform in India**, Cambridge: Cambridge University Press, 1999. It goes beyond previous work on economic reform in India. His chapter 5, "Political institutions: federalism, informal networks, and the management of dissent" offers strong evidence for the existence of an emergent "federal market economy." pp.119-171.

See also Aseema Sinha, "From State to Market;" "India and the Theory of Market Preserving Federalism," paper presented at the APSA annual meeting, Washington, D.C., August 31 - September 4, 2000 and her forthcoming **Mapping Economic Reform: Federalism and the Politics of Economic Reform in India**, University of Wisconsin Press.

We have benefitted as well from John Echeverri-Gent's work on a "decentered polity." It theorizes and explains the economic decision-making and party system transformations of India's federal system and relates them to the shift in the 1990s from an interventionist to a regulatory state. See his "Politics in India's Decentered Polity," in Marshall Bouton and Philip Oldenburg, eds., **Asia Briefing 2002**, forthcoming. Echeverri-Gent's developed his conceptual distinction between an interventionist and a regulatory state in his work on SEBI's regulation of the Bombay Stock Exchange. He calls SEBI India's first independent regulatory agency in "Governance Structures and Market-Making: Regulating India's Equity Markets in a Globalizing World," paper presented at the University of California, Santa Cruz, November, 1998.

The Observer Research Foundation's **Economic Reforms; The Role of the States and the Future of Centre-State Relations**, New Delhi: Observer Research Foundation, 1996, is written from the perspective of an earlier paradigm in the study of federalism and center-states relations in India, e.g. Balveer Arora's essay,

India's Federalism and the Demands of Pluralism." Lawrence Saez examines many of the federal issues in "Federalism Without a Center: The Impact of Political Reform and Economic Liberalization on India's Federal System", PhD dissertation, Political Science Department, University of Chicago, 1999.

The Government of Rajasthan, provides an example of the entrepreneurial breaking of bottlenecks that can characterizes the use of, in Rob Jenkins' phrase, "stealth" in the sharing of sovereignty or decentering of the polity. Blocked by the provisions of the obsolete Telegraph Act, 1885 and the Wireless Telegraphy Act, 1933, from attracting investment to upgrade telecommunications in Rajasthan, including new developments in information technology, government contracted for project designs for laying a fibre optic cable or "spine" throughout Rajasthan and sought investors to implement it. The cable would not violate the two acts which barred private companies from transmitting voice messages on telephone ground lines. The acts did not bar transmitting data or digital information. Communication, Arvind Mayaram, Secretary to Government for Industries, December, 1999.

11. For a discussion of profit and the profit motive in pre-liberalization India see Lloyd I. Rudolph and Susanne Hoeber Rudolph, **In Pursuit of Lakshmi**, Chicago: University of Chicago Press, 1987, 26-27. See also Jeffrey D. Sachs, Ashutosh Varshney and Nirupam Bajpai, eds., **India in the Era of Economic Reforms**, New Delhi: Oxford University Press, 1999, 21-22.

12. See Hamish McDonald's serious biographical and analytical economic history, **The Polyester Prince: the Rise of Dhirubhai Ambani**, Sydney: Allen and Unwin, 1998. Through summer 2000 Ambani succeeded in preventing the sale of the book.

13. See Lloyd I. Rudolph and Susanne Hoeber Rudolph, "Redoing the Constitutional Design; From an Interventionist to a Regulatory State," in Atul Kohli, ed., **The Success of India's Democracy**, Cambridge: Cambridge University Press, 2001.