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Coalition Politics and Hindu Nationalism

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Introduction

The NDA Government continued the process of economic reform initiated by the INC Government in 1991, and sustained by the United Front Government during 1996–98. Faced with the need to deepen second-generation reforms, the NDA encountered a more complex set of challenges than its predecessors. The political implications of a broadened agenda – combined with shifts in the nature of party competition, federal relations and political mobilisation, not to mention the economy itself – have made managing the politics of economic reform particularly daunting during the NDA era.

In common with the other contributions to this volume, this chapter assesses the role of coalition politics, ideological constraints and external forces in shaping the NDA's performance in power. The chapter argues that the content, pace and sequencing of economic reform was to a considerable extent influenced by all three factors, though not necessarily in ways that might have been predicted at the time the NDA came into office. In the area of economic reform, the NDA faced the challenge of preventing the three constraints from merging together in ways that would make the task of liberalising the Indian economy even more daunting than it already was. Aspects of *Hindutva*, for instance, were constantly in danger of becoming wedded – through such RSS-linked front organisations as the SJM – to a form of economic nationalism that cast *external forces* (such as the World Bank, the International Monetary Fund (IMF) and multinational capital generally) as the nefarious drivers of the government's liberalisation programme. To the extent that the BJP's junior coalition partners were susceptible to the economic nationalism aspect of this logic, the three forces were often perilously close to solidifying into a formidable composite constraint. This was prevented both by skilful politics on the part of the coalition's managers, and also by certain structural factors. For instance, while the idea of economic nationalism was appealing to certain NDA elements (for crass political reasons as much as any ideological commitment to economic autarky), the *Hindutva* thrust given to these ideas by the likes of the SJM was anathema to them, indeed discrediting the otherwise sacrosanct idea of *swadeshi* in certain quarters.[1]

The relative influence of each of these three factors on the process by which the NDA pursued economic liberalisation varied across time, across policy domains and across reform tasks. Perhaps the most notable trend has been the continuity in the tactics used to manage the politics of reform. The NDA Government continued with the tendency towards Machiavellian politics displayed by its predecessors, including continued reliance on India's federal institutional structure to negotiate awkward political dilemmas.

Whether the momentum of reform slowed under the NDA, or whether (as the World Bank argued in 2003) 'the pace of reforms has slowed since the mid-1990s' (2003: i), depends very much on one's view of what constitutes 'reform', whether the earlier stages of reform are considered politically less demanding than later stages, and how much allowance is made for the broader economic environment within which reform takes place.

Indeed there are inherent analytical obstacles that confront any analyst seeking to characterise the NDA Government's performance on economic reform. The first is the difficulty of determining the appropriate standard against which to assess performance. Should we adopt process standards – indicating policy measures introduced – or outcome standards, indicating what the policies yielded? If we adopt process standards, as this chapter mainly does, should these be conceived of dichotomously – either a reform was or was not effected – or 'continuously', on the basis of gradual progress towards a policy shift? The case of labour policy illustrates this point. While legislative amendments to the much-criticised Industrial Disputes Act (IDA) of 1947 were not affected – to say nothing of its outright abolition, as some might like – steps in this direction were taken, such as clearance by the cabinet of certain IDA amendments.

Were we to adopt outcome measures, even more problems would arise. Certain policy changes take years to have an effect. But should initial indications of impact count? And if shorter-term indicators are used, is there not the potential problem that some of these impacts may rely upon perceptions influenced by *other*, non-economic aspects of policy? For instance, how much foreign direct investment (FDI) India receives may be affected as much by investor perceptions of communal stability and regional security as by India's relaxation of investment rules. Even a focus on the political implications of reform, which usually manifest themselves more quickly than do the economic effects, does not overcome the familiar difficulty of gauging their net *impacts*. This has two aspects: across and within constituencies. The overall balance across constituencies is difficult to assess because, while reform may have worked to the advantage of some social groups, it may well have hurt other interests. The ability of the 'winners' to substitute for the loss of support from the 'losers' is uncertain at best. Making assessments within constituencies presents problems as well. When a group is affected by more than one type of 'reform', there are few universally reliable, and comparatively applicable, measures for determining whether, in the case of an individual household or medium-sized firm (to say nothing of a diversified conglomerate), the losses from one species of reform – such as changes to the tax code – are fully offset by other aspects of liberalisation, such as increased foreign competition resulting from reduced tariff and non-tariff barriers to international trade.

In addition to the difficulty of deciding upon the most relevant agenda items for political analysis there is a second obstacle to assessing the NDA's performance. This is the problem of determining the validity of basic economic indicators associated with second-generation reforms. Huang and Khanna (2003), for instance, argue that we must challenge our most basic assumptions about what phenomena require explaining. For instance, China's lead over India in terms of FDI inflows, they argue, is quite possibly grossly overstated. This is because Chinese tax laws create incentives for economic actors to conceal earnings and to bring them back into circulation in the form of foreign investments, namely the phenomenon known as 'round-tripping'. While China's figures have been overstated – Huang and Khanna claim that estimates could be up to *twice* as high as actual inflows – India's numbers have been understated. It is possible, they argue, that India's foreign investment levels are double what the official statistics indicate. If they are right, then the two countries' respective foreign investment performances, in terms of inflows as a percentage of gross domestic product (GDP), are pretty close to converging, with investment into China equalling 2 per cent of total domestic output compared to a figure of 1.7 per cent for India.

Regardless of whether a process or outcome standard is considered most appropriate, what constitutes an acceptable threshold for successful reform remains unclear. Should the NDA be judged against its manifesto commitments? Or would the known preferences of key decision makers within the BJP be a more appropriate standard? Or given that manifestos are, in practice, aspirational statements rather than realistic commitments, should the NDA's reform performance be judged against *ex ante* expectations (voiced by journalists, economists and others) about how far its reform programme was likely to go? Or should its performance be assessed against the standard set by international development institutions: the reform milestones in bilateral and multilateral aid programmes? How about comparing the NDA against its predecessors in the post-1991 era, the Narasimha Rao government or the United Front? But the tasks, and the times, were different then.

In the end, there is no obvious method for arriving at a completely satisfactory standard. Judgements must be made on a case-by-case basis. Either way, advancing the process of economic reform into a new generation will present the new government with a huge range of political problems, not least the sheer enormity of this ever-expanding agenda, which includes the deepening of existing structural reforms as well as the need to address issues of equity, to place public finance on a more sustainable footing, to stand up for India's interests in multilateral trade negotiations, to upgrade the country's decaying infrastructure, and to combat the corruption that drains both public resources and entrepreneurial energy. Moreover, each of these issues and the tradeoffs involved in prioritising among them involves acute political dilemmas.

Before proceeding further, one final caveat is in order. The NDA Government's ability to advance the reform agenda would have been severely handicapped had not other enabling factors been present. For instance, one macro-level condition that permitted the generally liberal course of reform to persist was the positive performance of the Indian economy. Inadequate progress on certain indicators, such as the consolidated (central plus states) fiscal deficit as a proportion of GDP, has been eclipsed in public discussions by the high annual GDP growth figures (particularly in a world marked by meagre economic growth in most countries during the period under investigation). Likewise, headline-grabbing statements such as the size of India's foreign-exchange reserves (which stand in such great contrast to the 1991 situation), or the fact that during at least one quarter during 2003–04 India balanced its current account for the first time in a quarter-century, have also become salient in economic debates. All of this has taken place in a low-inflation context; this was critical, as India's polity is notoriously averse to even mild inflation (at least by the standards of other developing countries).

Conceptualising the second generation

There is no universally accepted definition of what constitutes a second-generation reform agenda. Second-generation reforms are often conceived of as delving deeper into sectoral specificities. Thomas Friedman, in his evocative style, calls this the shift from 'wholesale' to 'retail' reform (2004).[2] Others would contest such a generalisation, claiming that some basic reforms – such as rules for fiscal prudence – were usually not enacted in the first wave of reform. This is certainly true of India, and indeed of most other countries with the capacity to resist the more extreme austerity programs that characterised World Bank and IMF structural adjustment recipes of the 1980s and early 1990s.

The reason why there is no unanimity on what constitutes second-generation reform is not simply that each analyst has his or her own policy preoccupations; just as important is the widespread questioning of the standard economic prescription of privatisation, deregulation, trade liberalisation, unrestricted transnational capital flows and so forth. Doubts about the wisdom of this reform package have existed ever since the rise to prominence of neoliberal economists within the international financial institutions during the mid-to-late 1970s.[3] These began to boil over in a

more concerted (and intellectually coherent) *counter*-counter-revolution during the latter part of the 1990s – first in the wake of the East Asian economic crisis, and then in the anti-globalisation protests in Seattle, Prague, Genoa, Gothenburg and elsewhere. By the turn of the millennium, orthodoxy had become heterodoxy. What John Williamson had once called 'The Washington Consensus' had fractured.

In a recent book, *After the Washington Consensus*, Kuczynski and Williamson (2003) delineated the contours of what they were promoting as a new post-consensus reform agenda. They make three main points relevant to understanding reform's second generation, and therefore to the NDA's performance during its term in office. First, any practical approach to constructing a second-generation reform agenda must include the unfinished business from the first generation. Second, second-generation reform must be centred on institution building, without which markets will not function and the reformist momentum will not be sustained. Finally, issues of equity must be addressed, for reasons of political sustainability if nothing else, and these must inform part of the way in which reform is sold to sceptical publics.

World Bank President James Wolfensohn is in almost complete agreement with Williamson. Wolfensohn (1999) sees the 'first and second generations [as] *not* being sequential'. Indeed, he maintains 'that the first and second generation actually coalesce in terms of timing' (1999). Wolfensohn also argues that

> [t]he second generation issues focus around the questions of the structure of the right institutions, of the improvement of the administrative, legal, and regulatory functions of the state, addressing the incentives and actions that are required to have private sector development and to develop the institutional capacity for reforms.
>
> (1999)

Finally, Wolfensohn wants equity and fairness not only to be part of the agenda, but also to be seen to be part of it, so that they are central to the political discourse and not just the economic strategy. As he put it, 'Second generation reforms must also address the very important question of how you build consensus in a society' (1999). The idea that second-generation reforms must address a broader social constituency and also require attention to filling in the detail of earlier broad-brush reforms is consistent with the view taken by officials in other developing countries. Guillermo Ortiz, who heads the Mexican central bank, admitted in early 2004 that the early phases of economic liberalisation in Mexico were confined largely to the domain of elite politics, but saw the 'urgency' of spreading discussions of reform into mass politics.[4] Ortiz argued that it was necessary for 'Mexico to finish the structural reforms at the micro level', and that '[w]e did the first stages of structural reform from the top down' (cited in Friedman 2004). That was the relatively straightforward part. 'The next stage is much more difficult,' he maintained, because the government will 'have to create the wider consensus to push the reforms in a democratic context' (ibid). This has clear echoes of Wolfensohn's view.

This chapter thus begins from the premise that first- and second-generation reforms are not, primarily, headings under which it is possible to list specific economic sectors (agriculture, finance), techniques of economic governance (privatisation, fiscal adjustment), or actor-related processes (labour, civil service reform). Rather, each of these familiar agenda items, as well as others not listed, is an ongoing process, consisting of more than one stage of reform. Therefore, in assessing the NDA's management of the politics of second-generation reform, this chapter does not treat any individual reform as inherently either a first- or second-generation issue. Instead, the relevant criterion is whether the NDA Government successfully advanced individual reform issues in ways likely to make them politically sustainable over the long term.

Political tactics for managing the politics of economic reform

The influence of political calculations on not just the broad parameters of economic reform, but specific measures as well, dates to the very beginning of India's economic reforms of the 1990s. In his first budget speech in 1991, which justified and gave some concrete shape to the newly launched policy of economic liberalisation, former Finance Minister Manmohan Singh (currently Prime Minister) announced a range of subsidy cuts. In the face of mass demonstrations, those relating to agricultural inputs (particularly on fertilisers) were 'rolled back', allegedly on orders from Prime Minister Narasimha Rao. By the time that the NDA Government took power, such humiliating policy 'rollbacks' had become a regular feature of the budget speech drama. Having been initiated into this curious rite following his first budget speech in 1998, Yashwant Sinha – Finance Minister during most of the NDA Government – reportedly made it his practice to draft a 'rollback announcement' even before presenting his budget to parliament. This is a stark reminder of the pervasiveness of politics in the reform process, and an indication of how responses to such pressures get institutionalised, binding future reformers.

In a study which focussed on the period from 1991–98, I argued that the reorientation of India's development strategy could be seen as a process of 'reform by stealth', an approach made possible by a combination of three factors: the political-management skills of India's politicians, the fluid institutional environment within which they operated and the political incentives thrown up by the initial policy measures they employed to address the 1991 economic crisis (Jenkins 1999).

These factors have been just as relevant during the subsequent period of BJP-led coalitions, from 1998–2004. The NDA adopted similar means to its predecessors in power. Echoing a characterisation often applied to Narasimha Rao, one of Prime Minister Vajpayee's long-time political colleagues called him 'a master of ambiguity', who 'sends different – sometimes wholly incompatible – messages to different communities'.[5] It is thus perhaps not surprising that the process of pursuing reform quietly – avoiding conflicts until propitious moments, dividing opponents, and using illiberal methods to achieve liberal ends – persisted under the NDA. Some of the means employed have remained the same since the days of Narasimha Rao; others have recently emerged.

Arun Shourie, Minister for Disinvestment, Communications and Information Technology in the NDA Government, showed his implicit appreciation of Narasimha Rao's philosophy of the politics of reform: in a world in which change is always taking place, there are advantages to harnessing the forces already in motion. When asked by an interviewer to elaborate on his characterisation of the central political dilemma facing a reformer – the need to effect 'a complete U-turn without [it] seeming to be a U-turn' – Narasimha Rao stated that accomplishing this feat becomes less difficult to comprehend '[i]f you understand that where you are standing is itself in motion'. According to the former Prime Minister, once you realise that 'you are not static' then '[t]he turning becomes easier' (Gupta 2004). Grasping for himself this dynamic of perpetual motion, Shourie described his belief that second-generation reforms are 'propelled by the opportunities that have opened up' as a result of earlier reforms (2004). His view was that, eventually, a process of self-propulsion emerges: 'one reform creates pressure that other reforms be put through. Import–export licensing is abolished. Trade increases. Traders and manufacturers demand that ports be improved so that turnaround time comes down to Singapore levels, that the DGFT (Directorate General of Foreign Trade) accepts electronic filing of forms' (Shourie 2004). Ultimately the reformer's job becomes one of guiding rather than pushing.

In the area of telecommunications reform, one of Shourie's ministerial responsibilities, the NDA demonstrated its understanding of how to use strategic delay to its political advantage in advancing the process of liberalisation. Instead of pushing ahead aggressively on certain extremely controversial reform measures, the NDA Government let events already 'in motion' overtake the status quo. Ministry officials responded to technological convergence and price distortions that had arisen in the domestic market – themselves the result of how licenses for cellular and other services were issued – by claiming helplessness in the face of forces beyond their control. Reliance Industries Limited, India's largest private-sector firm, was reportedly permitted, as a result of its alleged inside access to high-ranking politicians in the governing coalition, to poach on markets that were not within the terms of its original license. Eventually, this made a mockery of the existing system, in effect forcing reform to take place by dint of necessity rather than through a planned effort that would have required the expenditure of the NDA Government's scarce political capital. Reflecting on this process, none other than the Disinvestment Minister himself remarked that 'by exceeding the limits which restrictions sought to impose upon them', companies such as Reliance had 'helped create the case for scrapping ... regulations' (*The Economist* 2003b). Even critics of the NDA's performance on economic reform had to agree. Referring specifically (though indirectly) to this very case, one critic regarded this as part of a larger pattern, in which

> [r]eforms in India ... are driven by either crises or vested interests. The 1991 reforms were driven by a foreign exchange crisis; others such as the telecom reforms of 1999 (when firms migrated from high fixed license fee commitments to a lower revenue-sharing license fee regime) were driven by the needs of the private sector telecom players – indeed, even the latest move towards a unified license is being driven by the needs of one part of the industry.
>
> (*Business Standard* 2003)

The BJP, when in opposition, nuanced its anti-reformism by claiming that it opposed external sector liberalisation until internal reforms were firmly in place. It also claimed that its approach to the external sector would be guided by pragmatism, and close attention to India's national interest, rather than a dogmatic acceptance of free trade. This was symbolised by the famous statement about wanting to import 'computer chips' not 'potato chips'. The BJP's 1996 manifesto, prior to first taking office, was also careful not to dismiss globalisation entirely, instead referring to the need to adopt a 'calibrated' approach to global economic integration. These fine distinctions were, of course, an attempt to have it both ways, something to which most parties aspire. But as the BJP-led NDA adapted to the realities of power, it found this balance difficult to sustain, and before long the government was adopting means similar to those used by its predecessors.

Fiscal policy

India's composite budget deficit (which includes the combined deficits of the central and state governments, but does not include a number of off-budget liabilities) increased dramatically between 1997–98, the last year before the BJP came to power, and 2002–03. In 1997–98 it stood at roughly 7 per cent of GDP; by 2002–03 it was in excess of 10 per cent, and rising. Both higher expenditure, particularly in non-development areas (mainly government salaries and non-merit subsidies of various sorts), and lower revenue were to blame. There are limits to how quickly a government can reverse the course of trends inherited from its predecessors, particularly on government salaries; but the NDA never even appeared to try. On the contrary, it placed excessive faith in the ability of privatisation proceeds to plug its widening deficit.

One of the areas of expenditure that contributed massively to the fiscal imbalance was the power sector. Financial losses in this sector hit 1.4 per cent of GDP in 2001–02. Food and fertiliser subsidies amounted to a further 1.4 per cent of GDP in 2002–03. Adding in petroleum subsidies (0.3 per cent of GDP) brings these three items to almost a third of the total combined fiscal deficit.

Public expenditure is an area in which the NDA's performance was clearly constrained by both coalition politics and external forces. The Government of India's commitments to its international development partners – mainly international financial institutions, but also bilateral aid donors and regional development banks – should have resulted in an improvement in the country's fiscal situation. These commitments were embedded both within ostensibly binding conditionalities attached to lending instruments, and within the non-binding targets agreed as part of grant programmes. Another set of external actors, namely foreign investors, could also have been expected to act as a source of downward pressure on the budget deficit. Concerned with the impact of growing deficits on exchange rates, interest rates, consumer spending and other key indicators, both portfolio managers and multinational firms contemplating FDI should have helped to discipline the NDA Government's profligacy. An argument can of course be made that without these external pressures, India's fiscal condition would have been even worse, but this kind of counterfactual optimism is not very convincing.

The constraints imposed by coalition governance evidently exerted a much stronger influence than did the external forces. Needing to satisfy such a large range of coalition partners made the Finance Minister's job more difficult than it otherwise would have been. Though only a few of these partners were, on their own, a serious threat to governmental stability, almost all of the partners – especially those lacking control of key spending ministries in their own right – extracted expensive concessions from the coalition managers.

In the current phase of India's electoral politics, in which regional parties are significant contributors to the forging of parliamentary majorities, the category of 'coalition constraints' overlaps very substantially with what might be termed regional pressures. This, by implication, highlights the important role played by those non-BJP coalition partners that also ruled state governments. The large bloc of MPs from the TDP, which ruled Andhra Pradesh, was a crucial component of the NDA coalition's parliamentary majority. The TDP leader, and then-chief minister of Andhra Pradesh, N. Chandrababu Naidu, exerted pressure on the NDA that made it difficult, if not impossible, for the Government of India to exercise fiscal restraint. For instance, Naidu was among the main ringleaders of a movement among Chief Ministers to oppose the Eleventh Finance Commission's recommendation that decisions on the allocation of financial transfers from the central to the state governments be linked, in part, to the performance of state governments in reining in public spending. This led to a much-publicised political storm that not only undermined the proposals themselves, but also reinforced the message that the central government could be effectively challenged when it sought to take action to restore order to the public finances. This had substantial knock-on effects, as other coalition partners sought to extract fiscal concessions for constituencies located within their states. These concessions took the form of both changed tax rules that assisted certain sectoral interests and spending commitments that were intended to buy political support for regional parties, who could then claim that central government largesse would not have been forthcoming had not the regional party been part of, or actively supported, the NDA.

Perhaps the most blatant example of regional lobbying was Railways Minister Mamata Banerjee's insistence that the central government approve the proposals contained within her self-proclaimed 'Bengal package'. The willingness of the NDA leadership ultimately to comply with many, though not all, of these demands for regional patronage was only partly explained by Banerjee's support for the NDA. Another contributing factor was the BJP's lack of a significant electoral presence in West Bengal. Strengthening Ms. Banerjee's hand in the provincial politics of West Bengal would have encountered far more opposition from BJP leaders, as well as from other members of the NDA who viewed such concessions through zero-sum spectacles, had the BJP been a serious contender for power in West Bengal. Such complaints could be heard from BJP politicians in Andhra Pradesh: the BJP-led government in Delhi was providing additional resources and policy autonomy to a state government ruled by the TDP, a party that BJP leaders in Andhra Pradesh saw as their main political rival for the one prize that mattered to them – control of the state government.

Naidu and Chief Minister Prakash Singh Badal of Punjab, also ruled by an NDA coalition partner, the SAD, were key figures in resisting proposals to reduce the quantity of foodgrains and other commodities procured by the Food Corporation of India. This caused difficulties not just for the government's fiscal position, but for the prospect of agriculture reform more generally.

The pressures from coalition politics – in its federal guise – also thwarted a number of other reforms related to public expenditure. Tax reforms, for instance, were important not only to the country's overall fiscal health, but also to removing obstacles the practical realisation of other second-generation reforms. A good example is the VAT. On 1 June 2003 India was to become the proud owner of a 'national value-added tax' (*The Economist* 2003a). But Finance Minister Jaswant Singh backed out just before the deadline. This had happened earlier as well. It was not just traders who were aggrieved but also state governments, many of whom feared a loss of revenue, despite commitments made by officials in the central government. If India is to achieve the level of manufacturing competitiveness its boosters foresee, then reform of the system of state-level sales tax (assigned to states by the Indian Constitution) is necessary in order to create a common market. But political pressures keep intervening. As the NDA Government was voted out of office in May 2004, it saddled its successor with the financial implications of its spending commitments, particularly the estimated Rs 40 billion per year needed to fulfil the inflation-indexing commitment made to central government employees. This will eventually affect state governments as well.

To its credit, the NDA did, to the surprise of many, pass the Fiscal Responsibility and Budget Management Act (FRBMA). The FRBMA established 2008 as the target year by which India's fiscal deficit would be eliminated. On the other hand, because of the optimism of its projections – which included an expectation for growth and tax revenues to continue on an upward curve for the foreseeable future – few observers considered it likely that this target would be met. The newly-elected United Progressive Alliance (UPA) Government, which assumed office under Prime Minister Manmohan Singh in late May 2004, almost immediately shifted the deadline back to 2009.

Trade policy

Trade policy in many ways encapsulates the problems that confront any attempt to provide a clear assessment of the NDA Government's performance on economic reform. On the one hand, it could be claimed that the NDA performed exceedingly well on this front. It reduced India's average applied tariff rate from more than 35 per cent in 1997–98 to approximately 29 per cent in 2002–03. Even with a general election looming, the NDA Government announced in February 2004 a reduction – from 25 to 20 per cent – in the peak duty for non-agricultural product imports, as well as the elimination of the Special Additional Duty. Moreover, the NDA undertook a major step in the overhaul of India's trading regime by phasing out quantitative restrictions on more than 1,400 product categories.

On the other hand, there are grounds for scepticism about such achievements, and not just in terms of whether as much was accomplished as originally promised. This is because policy changes that might, on one reckoning, be counted as government actions may well have been determined by India's multilateral commitments. By far the most important are the multilateral agreements administered by the WTO. These include both sector-specific agreements, such as the Agreement on Agriculture, and those dealing with broader issues that cut across a range of sectors, such as the Agreement on Subsidies and Countervailing Measures.

Governments often have a political incentive to claim that their hands are tied, their room for policy manoeuvre constrained by international treaty obligations. To complicate matters further, frequently the nature of India's commitments is disputable, making the element of volition involved hard to determine. One example is the case of edible oil imports. Soon after quantitative restrictions on imports of this and other product categories were phased out during 1999–2001, India experienced a surge of imports that drove down prices. While this was theoretically good news for consumers – assuming that markets were responsive enough to prevent traders from cornering all the savings – producer groups were less pleased. On the face of it, the import tariff level that the NDA Government had set for various edible oils, as a replacement for the quantitative restrictions (which limited the actual amounts that could be imported), was well below the bounded rates it had committed to at the WTO. Still, despite the pressure exerted by both edible oil producers and the oilseed farmers that supplied them, the NDA Government did not increase the tariff. Why it did not is one of the disputed issues referred to above, which make the assessment of trade policy so difficult.

In this case, because India's bounded rates clearly allowed tariff increases, any excuse for non-action by the government that invoked WTO obligations would not be tenable. As a result, other explanations began to circulate, most notably the belief that the NDA Government's failure to react to the import surge was part of a half-secret bilateral deal with United States trade officials. This deal allegedly emerged from negotiations on how to respond to the ruling by the appellate panel of the WTO's Dispute Settlement Body, which had ruled that India's continued use of quantitative restrictions on a range of products was a violation of its obligations under Article XI of the 'GATT 94', one of the agreements administered by the WTO (WTO 1999). Rather than retaliate against India with increased tariffs of its own, as WTO rules generally allow winning parties to a dispute to do, the US struck a deal. How true this was in the case of edible oils is less important than the perception that arose among participants in the public debate. This is an interesting example because the political incentive created was the opposite of the one cited earlier. The NDA Government did not want to claim that its hands were tied by an international agreement: the notion that Indian farmers could not be protected because of a deal with the US administration was not considered politically advantageous, to say the least.

Another explanation for why the NDA Government failed to raise tariff levels during this crisis stressed the Finance Ministry's sensitivity to pressure from the international financial institutions and market sentiment generally. The argument made by critics was that while, under the old system, changes in the level of imports permitted under quantitative restrictions could be imposed by the Ministry of Commerce acting alone, under the newly tariffised system a tariff increase required Finance Ministry approval, and given the close association between Finance Ministry officials (the main point of contact for Bank and Fund representatives) and the multilaterals, there was built-in resistance to taking action. Again, this kind of explanation can be contested; but by entering the political rumour mill it contributed to the perception that external forces were, indirectly, shaping the manner in which India's trade policy was being implemented, an aspect of 'policy making' that must be considered when arriving at an overall assessment of government performance in this area.

Assessing the NDA's performance on trade policy reform is also made difficult because of the uncertain boundaries of this policy domain. As a result of the Uruguay Round of trade negotiations, a range of new policy areas became part of an expanded multilateral trade agenda, the logic being that policies once considered purely domestic had implications for patterns of international trade. Thus, issues such as the level of subsidies provided to agricultural producers became subjected to international disciplines. In addition to its own policy decisions, therefore, the NDA Government's performance on trade policy must also be judged on its participation in international negotiations.

There is no doubt that the NDA Government made its presence felt in world trade talks, and indeed in the routine operation of the WTO itself. Even discounting the claims made by the Ministry of Commerce – that India was instrumental in scuppering the Seattle ministerial meeting in 1999 – there is fairly unambiguous evidence that India's delegation to the Doha ministerial meeting in 2001 played a very important role. For instance, the Indian delegation helped secure a side agreement stating that public health emergencies needed to take a more prominent position in the implementation of the Trade-Related Aspects of Intellectual Property Rights Agreement (or TRIPs). India, as we have seen, was also a significant protagonist in several cases argued before various WTO Dispute Settlement Panels. India used this mechanism to press its claim that Indian textile producers suffered as a result of health and safety regulations in rich-country markets that unfairly discriminated against Indian products.

Perhaps India's most high-profile achievement under the NDA Government in the international trade arena was its role in helping to establish the so-called G-20, a loose group of about 20 developing countries whose mission was to act as a coordinated bloc on issues of mutual concern, particularly on agricultural subsidies and provisions for Special and Differential Treatment for poor countries. India, Brazil, South Africa, Nigeria and other large developing countries were able to forge this grouping in the run up to the Cancun ministerial meeting in late 2003, which was to assess progress on key issues introduced in the trade negotiating round begun at Doha in 2001. Publications of the Ministry of Commerce and Industry – the departmental reorganisation that created this joint ministry was itself the work of the NDA Government – routinely celebrated India's role in making the G-20 a workable entity, stressing that the government not only invested substantial diplomatic capital, but also used great ingenuity in tapping the intellectual resources of India's economics profession, both in India and among its diaspora (GoI 2004a: 20).

Labour policy

Labour reform – along with agricultural liberalisation – is often seen as among the most significant pieces of unfinished business from India's first generation of reforms. A complete overhaul of India's industrial-relations regime – including the conditions under which workers can be hired and fired, the rules governing union recognition, and the mechanisms for resolving employment disputes – is considered long overdue by the World Bank and other observers. India's restrictive labour regulations are widely regarded as unsuitable for its increasingly globalised economy.

Like its predecessors, the NDA continued to 'reform by stealth', facilitating backdoor policy changes rather than effecting them through overt decision making. This involved, among other things, relying on state-level leaders in India's federal system to negotiate awkward political dilemmas. Though the NDA avoided directly reforming the relevant labour legislation, during its time in power labour reform was nudged onto the terrain of mass politics through, for instance, the attempts by state governments (in Uttar Pradesh, Tamil Nadu, Rajasthan and Kerala) to take on state public employee unions in highly public confrontations. While this shift represented an important step in the direction of a second-generation reform agenda, on another key indicator – the building (or resuscitation) of institutions – there has been little progress. Indeed, a case can be made that the institutions necessary to manage the transition to a new labour-relations regime have been actively undermined, not least as a result of the Machiavellian politics mentioned earlier. The Indian Labour Conference, for instance, a tripartite body that could serve as a focal point for forging a workable compromise on many key labour issues, was marginalised.

Like its predecessors, the NDA Government was eager to promote Voluntary Retirement Schemes (VRS) to help firms to shed excess labour. While VRSs are not a substitute for the official 'exit policy' sought for so long by India's private sector, they contribute to solving the surplus-labour problems of many firms. The element of stealth derived not just from the fact that VRSs perform some of the functions that governments are too politically timid to effect by means of policy; other, more flagrant, sins of omission are involved. VRSs are often far from voluntary. Sometimes muscle power is used to intimidate workers, as governments (at the state and central level) turn a blind eye. In other cases, firms have been able to rely on the threat of keeping an employment dispute tied up in tribunals for so long that workers will never receive any payment if they refuse to sign up, voluntarily, for early retirement (Jenkins 1999).

Underhanded tactics could be found at the level of policy as well. In 2002, for instance, when declaring its intention to promote a series of Export Processing Zones (EPZs) and Special Economic Zones (SEZs) that would help India live up to its alleged 'trading superpower' potential, the government proposed to classify such zones as 'public utilities'. This would require employees of firms in these zones to provide 45 days' notice before going on strike, a substantial increase on the existing 30-day provision.

State governments have been far more active on the labour front than the central government. Whereas the central government mainly made announcements, the Madhya Pradesh state government actually watered down labour laws for firms in the Indore Export Processing Zone (EPZ) (*The Economic Times* 2003). Some state governments were reform trailblazers in certain policy areas, which helped others – including the central government – on the path of reform. In 2002, for instance, during cabinet debates on proposed amendments to India's Industrial Disputes Act (IDA) there was explicit discussion of precursor state-level legislation in Maharashtra. Maharashtra's legislation increased the number of employees a firm could have and still be exempt from the provisions of the relevant 'exit' regulations, which require approval by the state government to retrench workers or close down an enterprise. Discussion of the Maharashtra act was said to have played a role in selling to the cabinet proposals pushed by the Government of India's Finance Ministry. Insiders vouch for the fact that 'the example of Maharashtra's Industrial Act was cited by the pro-amendment ministers led by finance minister Yashwant Sinha' (*The Times of India* 2002). The Maharashtra government had, through example, provided a powerful argument to otherwise cautious coalition managers in New Delhi. Ultimately, the cabinet approved changes to the IDA, but these never reached the statute books.

Privatisation

In the budget for 2003–04, the NDA Government stated that it expected to realise Rs 132 billion in revenues from privatisation, a large sum in both absolute and relative terms. Had the target been met, it would have been equivalent to one half of 1 per cent of India's GDP. That this represented an extremely optimistic estimate was not an unfair assessment given that privatisation had yielded only Rs 30 billion in 2002–03.

Apart from ideological reasons, and the self-interested motivations of politicians who have long used public-sector enterprises as a source of patronage, an additional reason why privatisation aroused such strong resentment was the perception among both the political class and the public that the means by which privatisation (or disinvestment, to use the NDA's preferred euphemism) was being effected had in fact involved corruption. Critics frequently pointed to the privatisation of BALCO as an example of government callousness and legally dubious manoeuvring.[6] Of course, a case could be made that the alleged corruption that was involved in privatising this or any other company was a small one-off price to pay in exchange for ridding the NDA exchequer of the ongoing financial responsibility for these enterprises. Some critics would even go further, claiming that privatisation had improved the productivity in at least some firms. Nevertheless a potent political force was created by the equation in the public mind – and, crucially, among certain NDA coalition partners – of privatisation with corruption, favouritism to foreign firms, and an abandonment of India's ideological commitment to a strong state sector. This in effect combined the three political constraints on government performance with which this chapter's analysis has been concerned.

Interestingly, despite all the concern about public perceptions of privatisation, it was not public opinion, but rather the judiciary, that most seriously damaged the NDA Government's privatisation plans. Having decided to proceed with the partial disinvestment from two high-profile state-owned enterprises in the petroleum sector – over the objections of several ministers – the NDA Government ultimately could not take action. It was not the representative aspect of democracy that was able to halt the government. When the NDA Government sought to bypass parliament, the Supreme Court stepped in. It was a liberal institution of restraint,[7] with the capacity both to adjudicate between contending branches of government and to reinterpret constitutional provisions in light of changing times, which halted the NDA Government's most significant disinvestment. This highlighted the limits to the reform-by-stealth approach to managing the politics of economic reform.

Deregulation and re-regulation

The second generation of economic reform is, as noted earlier, centrally concerned with institution building. Among the most important institutions are those responsible for managing competition and creating an environment conducive to increased private investment, both domestic and foreign. More nuanced approaches to economic liberalisation than those that predominated in the 1980s have grasped the need to accompany vigorous deregulation with a judicious measure of *re*-regulation. The NDA Government's performance in this area has, again, been mixed.

One of the least impressive cases has been in creating the institutional framework for regulating the generation, transmission and distribution of electricity. This is a crucial infrastructure sector. Nevertheless, the intensive efforts undertaken to set the conditions for new investment and managed competition – in many cases with the assistance of bilateral and multilateral development agencies – failed. Even states like Orissa that were once touted as potential success stories have little to show for all the

effort. The creation of the Central Electricity Regulatory Commission (CERC) failed spectacularly to establish effective rules of the game, though there are high hopes among some observers – including those otherwise unsympathetic to the NDA – that the Electricity Act 2003, once fully in force, will have a salutary effect.

The telecommunications sector, by contrast, has witnessed a fairly healthy process of institutional development. To be sure, the Telecom Regulatory Authority of India (TRAI), the creation of which preceded the NDA, has lost important battles with Department of Telecommunications, with political decision makers (and the courts in some cases) siding against it – for instance, on questions relating to license fees and the process for setting tariffs. Slowly but steadily, however, the NDA oversaw the development of a telecommunications regulator with more organisational substance than was once believed possible.

Asking why India's telecom regulator managed to evolve into a substantial institution, while its counterpart in the power sector did not, Mukherji (2004) points to India's federal structure as an important institutional variable. Responsibility for the power sector is shared between the centre and the states, whereas telecommunications is a subject for the centre alone. As a result, India's telecom regulator could act – after a long period of maturation – as a more authoritative referee in disputes between government and private providers. Mired in provincial politics, state-level electricity regulators made decisions that rendered the CERC much less influential than it should have been.

Lal (2003) comes to a slightly different conclusion, stressing interest-group politics rather than institutional variables. He explicitly concedes some of the points made by Mukherji. (It should be noted, however, that Mukherji's explanatory framework stressed other factors as well, particularly the extent to which reform in the telecommunications sector was 'homegrown', whereas in the case of the power sector the World Bank and external consultants hired by aid agencies played a much greater role). Lal recognises that it 'has been argued that such "successful" reform is more likely in federally administered sectors like telecom, as they do not impinge directly on powerful voting interests like farmers' (2003). He stresses, however, that there is no clear correlation between central reforms being 'easy' and state reforms being 'difficult'. A more robust formulation, according to Lal, 'is that where the gulf between compensation and pain (in content, perception and time) for politically and financially powerful interest groups is narrow, reform proceeds in stealthy incremental doses. Where it is very wide (or appears to be so), as in power and income tax, it apparently grinds to a halt' (2003).

Echeverri-Gent's research on regulatory reform in the financial sector – particularly as it pertains to equity markets – suggests a similarly mixed picture. On the one hand, there was far less foreign institutional investment than either the NDA Government or many foreign analysts had anticipated. On the other hand, a number of reform measures that had long been promised by previous governments were finally implemented. India moved to a system of 'rolling settlement' periods for equity trading following Finance Minister Yashwant Sinha's announcement in 1999 that India would adopt global best practice. While it took two years – and a major financial scandal – before that pledge was fulfilled in July 2001, at least action was ultimately taken. As a result, according to Echeverri-Gent (2004), '[t]he deeply flawed account period settlement system that contributed to periodic breakdowns was replaced by a "T + 2" rolling settlement that is one of the most efficient systems in the world'. Something similar happened with derivatives trading. After repeated policy battles, in which reform advocates sought to abolish the 'carry forward' system that was used to finance speculative trading, and prompted many market crises, it was under the NDA that reform was successfully implemented, creating what Echeverri-Gent called 'a thriving derivatives market'. Again, it is difficult to determine whether the NDA was bolder than its predecessors, willing finally to take on the forces of resistance, or whether it was reaping the benefits of initial actions taken by earlier reformers (Echeverri-Gent 2004).

This raises the more general question: Which is politically more difficult: starting reform, which in some cases can be done with a stroke of the pen, or carrying through on the details, which is often what causes the real economic pain, and thus provokes the most serious political reactions? Narasimha Rao himself, not surprisingly, claimed that it was the initiation phase that was hardest. He compared the reforms introduced during his government with the further elaboration of the reform agenda during the subsequent governments, stating that liberalisation in 1991 'came from 0. Maybe negative. So taking something from 50 to 100 is making it double. But if you take it from 0 to 1, how many times is it? . . . Infinite' (Gupta 2004). He thus minimised the contribution of later governments by characterising their actions as making merely incremental changes, building on the foundations set by others (Gupta 2004). Nevertheless, precisely because many of the difficult decisions had been deferred by earlier governments, the NDA found itself with fewer reform options. A fair assessment would have to assign the NDA Government at least some of the credit for keeping the reform process on track.

Elections and reform: the closing stages of the NDA Government

By late 2003, with a general election less than six months away, and a round of important state elections in progress, NDA ministers started becoming more cautious, claiming that reform measures considered politically sensitive were significantly down the priority list. Union Commerce Minister Arun Jaitley, speaking at the India Economic Summit 2003, initially stated how positive labour reform would be for job creation, and then reassured any trade unionists that might be listening that nothing serious would be done in the short term. It was something for the next parliament. Asked when he thought action might be taken, Jaitley said 'I think in two to three years, work on labour reforms would pick up momentum' (*Hindu Business Line* 2003).

Near the end of 2003, the BJP wrested power from three out of four INC-controlled states in north India. It was a huge reversal: the BJP took 171 out of 230 state assembly seats in Madhya Pradesh, 120 out of 200 in Rajasthan and 50 out of 90 in predominantly tribal Chhattisgarh. Many in the BJP felt that the time was ripe for a further push on reform. 'We believe these polls dramatically improve the mandate to deepen economic reforms in India', a senior BJP official said soon after the verdict was announced. 'We want to bring it home to people that economic liberalisation is not some distant thing that happens in Delhi', and that it 'directly raises the standard of living of ordinary Indians, in the countryside as well as in the cities' (*Financial Times* 2004b). Jaitley, shedding his reticence of just a week earlier, asserted that the state elections results were 'a very strong vote for further economic reform' (*Financial Times* 2003).

By claiming so loudly that its victory in the 2003 state assembly elections was due to the success of economic reforms, the BJP could hardly be surprised when its defeat at the 2004 general election just months later was blamed on the political reaction to reforms as well. It is doubtful whether either interpretation was correct. For instance, nothing in the election survey data produced by the Delhi-based Centre for the Study of Developing Societies (CSDS) indicated that the NDA lost power because of a revolt against economic reform by India's voters. Neither, for that matter, were any of the three central factors discussed in this paper – ideological constraints, coalition pressures or external forces – responsible for the NDA Government's demise in 2004. The UPA Government, under Prime Minister Manmohan Singh, the key architect of the first generation of reform, will face many of the same political difficulties that its predecessor did in managing the transition to a second generation of reform built around new institutions and a greater focus on equity.

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Notes

1 I have analysed the implications of the existence of these competing versions of *swadeshi* in Jenkins (2003b: 584–610).
2 Ironically, Friedman introduced this term when discussing how the threat of economic competition from the likes of India (and China) would force Mexico into a new generation of reforms.
3 For an account of this rise, see Toye (1989).
4 For a useful discussion of the distinction between these two varieties of politics, see Varshney (1999).
5 This was the view of Balraj Madhok, a retired politician described as an 'old-style Hindu nationalist' who 'was Vajpayee's political mentor in the 1950s and 1960s' (*Financial Times* 2004a).
6 An interesting account of the issues arising in the BALCO case is found in Ahluwalia (2002).
7 For a good account of the balance between the liberal and representative aspects of democracy, see Zakaria (2003).

10 The NDA and Indian foreign policy

James Chiriyankandath and Andrew Wyatt

Introduction

Recent Indian foreign policy has been made in a profoundly altered context. We argue that the policies of the NDA Governments from 1998 to 2004 have to be understood as part of the larger re-orientation that has taken place since the end of the Cold War. Since 1991 India has lost its longstanding ally, the Soviet Union, and the Non-Aligned Movement has been rendered insignificant. During the same period, the US has come to dominate international politics. In assessing the foreign policy record of the NDA administrations, we will consider the impact of a number of variables that one would intuitively expect to determine policy outcomes. From a domestic point of view, these will include the impact of the BJP as the dominant party in the coalition, the effect of the coalitional character of the NDA (in particular the presence of a number of regional parties inside the coalition), prevailing ideas about India's place in the world and the institutional structure in which policy is made (in particular the dominance of the Prime Minister). From an external perspective, we will consider such variables as the policies of individual states towards India and its neighbours (with particular reference to the US and Pakistan), the role of international regimes and the changing international economy. While the focus is on developments after 1998, it is clear that some of these variables have had an impact on Indian foreign policy that predates the NDA.

In this chapter we argue that the foreign policy of the NDA has exhibited a strong degree of continuity with the conduct of its immediate predecessors. However, we do identify some significant divergences from what was India's overall trajectory in 1998. First, the BJP (rather than the NDA) took India over an important nuclear threshold in 1998. Second, Indian foreign policy more generally was more pragmatic and realist in orientation after 1998. This was true of both practice and the terms in which policy pronouncements were made. The chapter begins by considering the historical backdrop to the NDA's foreign policy making and the administrative, economic and political context within which foreign policy is made and how this has changed in the past decade and a half. It then