Saurabh Dhiman et al. International Journal of Institutional & Industrial Research ISSN: 2456-1274, Vol. 3, Issue 1, Jan-April 2018, pp. 113-117

The challenge of Governmental policy coordination in India

Saurabh Dhiman, Shabad Dyal

Disaster Management Department of Geography, Panjab University Chandigarh

Abstract: **Policy coordination is one of the oldest challenges for governments, but has become even more important as the problems confronting governments change, and the ideas of "New Public Management" are diffused. This paper examines the causes for coordination problems and the mechanisms that may be available for improving coordination. It concludes by discussing the limits on coordination as a solution for the problems of governing..**

Keyboards: **Policy coordination; policy collaboration; policy integration; New Public Management; policy design policy practice**

1. Introduction

As the political and economic system of a nation changes over time, so do intergovernmental relations [IGR]. While the emphasis in the concept of federalism is on national-state relationships with occasional attention to interstate relations, IGR include not only national-state and interstate relations, but also national-local, state-local, national-state-local, and interlocal relations (Wright 1975). Thus, Professor Anderson defines IGR as "interactions occurring between governmental units of all types and levels" (Anderson 1960, 4).
Note that human interactions are at the core of IGR.1 Therefore, certain institutional mechanisms are required to facilitate interactions among political incumbents. These are called "coordination mechanisms". The aim of these mechanisms is to achieve 'policy coordination' by facilitating interactions among the executives of the two orders of government.
In India we have two such major intergovernmental forums called National Development Council (section I) and Inter-State Council (section II). In addition, Inter-State water tribunals are established from time to time to settle disputes related to water sharing (section III). In this context we review important recommendations of the Sarkaria Commission (section IV), the National Commission to Review the working of the Constitution (section V), and the Punchhi Commission (section VI).

2. Background

The story of India's economic development since Independence is a fascinating one. After a hundred years of stagnation before 1947, the Indian economy has grown at a steady clip ever since. The period between 1950 and 1965 was one of great optimism, as the basic institutional structure for development was put in place through the enunciation of new policies, setting up of new institutions, and enactment of the basic legal structure underlying economic activities. A certain degree of success was achieved during this period in rousing a somnolent economy, with economic planning, import substitution and self-reliance as the basic guiding principles. However, just as other Asian countries began to exhibit their export-oriented high-growth strategies, Indian policies became more rigid and inward-looking, and consequently, the 1965 to 1980 period exhibited relative economic stagnation. The 1980s were a period of hesitant transition from the hitherto dirigiste framework, but we had to wait till 1991 for a fullblown balance-of-payment crisis that then induced the beginning of comprehensive economic reforms, setting in motion the transformation of India towards a modern open economy.
There are many books and articles that chart this story, but none like this innovative compilation by Gautam Chikermane. It tells the story through 70 policies and enactments made over the 70 years since Independence, which can be described as forming the changing bedrock of Indian economic strategy over time. How does economic policy change come about? Economic theories undergo transformation, ideologies wax and wane, old leaders are replaced by new ones. At the same time, there is a great degree of continuity in institutions once they are set up. The expression of policy change is done through explicit policy announcements: legislative enactments are made and old ones repealed; new institutions are created, old ones shut down. These are the things this papers. Gautam has designed this paper as a reference work that any busy economic kibitzer can access. It will be of equal interest to current policymakers who may want to quickly see the origins of the policies they want to change; keen economics undergraduate or graduate students who want to trace the evolution of the Indian economy since Independence; professors who want to find the references that they have been searching for to buttress their lectures; researchers on the Indian economy who want minimize their Google search time; businesspeople who want to see the origins of the various laws that they operate under; and the lay reader who is just curious. Each of these 70 policies/enactments could demand a full-scale chapter, but Gautam has worked under a self-imposed restriction of 350 words for each, so that they are easily digestible. Such a collection could easily be just a boring

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reference work that you buy but keep on you shelf, never to be read again! But this is no dry compilation meant only for the policy aficionado. Gautam peppers each piece with his opinionated commentary so that it can even be read as a whole: a quick snapshot of the shifting sands of Indian economic ideology and policy practice.

The 70 narratives in the main text are only the tips of the many icebergs buried in the 683 endnotes that form the documentary basis for his 350-word policy descriptions. So, any interested reader can easily dive into the active digital links that almost all endnotes embody, and then take off into their own voyage of discovery that today's digital media enables. One thing leads to another, so the reader could also take this as a starting point to write their own interpretations of each of the policies and acts covered. As a former policymaker and a current teacher and researcher, I can attest to the days and months of painstaking research that this vast enterprise must have entailed.

Economic journalists, who have to be slaves to daily or weekly deadlines, are not known to have the patience to do detailed research and trace down long-forgotten documentary sources. That Gautam was not shy of taking up this massive enterprise is not surprising. If he can tackle the Mahabharata as a fiction writer and provide new subaltern insights, this work is clearly child's play. Moreover, it must be his classical Dhrupad training that provided him the discipline needed to do this painstaking work.

The Indian economy has miles to go. I hope that this snapshot of policies since Independence will enthuse us to continue making the changes that carry the country successfully into the 21st century.

3. Coordination between monetary and fiscal policies

The rate cut announced by the Reserve Bank of India on Jan. 15 surprised the market in a good way. Raghuram Rajan, the central bank's governor, cut the benchmark interest rate by 25 basis points more than two weeks ahead of the next scheduled policy meeting. The central bank had come under attack for holding off on cutting the rate for 20 months. Many economists believe the bank has now entered a cycle of moderate easing in order to play catch up with falling inflation, while keeping the Indian rupee stable.

In 2015, Modinomics will go full throttle in order to take Asia's third-largest economy beyond the current 6% growth trajectory. Rajan's move is a crucial linchpin of Prime Minister Narendra Modi's master plan, not just because lower rates are needed to encourage growth but because India needs monetary and fiscal policies to be in lockstep for a change.

In the 1980s, fiscal policy dominated because of large government deficits. To keep a lid on the cost of repayment, the government kept rates low and paid about 4% to captive buyers of government debt: state-owned banks and other public entities such as the Life Insurance Corp. of India and the Unit Trust of India. Interest rates were not determined by market forces.

The economic reforms of the early 1990s emphasized fiscal discipline and a move toward market-determined rates. RBI was given greater autonomy to play an active role in inflation control and exchange rate management. Greater coherence between monetary and fiscal policies was prompted by the 2003 Fiscal Responsibility and Budget Management Act, which put in place targets for the government that were strictly adhered to. Better management of public expenditure helped the central bank contain inflation at around 4%, which it also achieved by sterilizing (through buying dollars) the inflationary impact of a surge in capital inflows. India witnessed its highest ever gross domestic product growth rates in subsequent years, peaking at 11.4% in the first quarter of 2010.

But the subprime crisis saw India embarking on aggressive fiscal stimulus, which eventually led to inflation hovering around 10% from 2010 to 2012. This reduced the purchasing power of the rupee and caused it to depreciate sharply against the dollar. A disagreement between monetary and fiscal authorities emerged over how best to tackle inflation and growth. The government, despite the pressures of inflation, did not impose fiscal discipline and the fiscal responsibility rule targets were flouted. Meanwhile, the central bank came under tremendous pressure to put the brakes on rate rises after it put up the repo rate nearly 20 times between 2010 and2011. However, that failed to spur GDP growth because of policy paralysis, election uncertainties and supply bottlenecks. By 2013, inflation was still at double-digit levels and GDP growth was dismally low at around 5%.

Prime Minister Modi has promised to bring higher growth and stable inflation, and he has been lucky so far because of tumbling crude oil prices, which ease inflationary pressures and improve the balance of payments.

With inflation now standing at 4.4%, the finance ministry has criticized the RBI for being too conservative, especially when it refused to cut rates in December. Now, the central bank finally appears to be confident enough about the economy and the government's ability to improve its fiscal balance to start lowering rates.

At the same time, the government seems on track to achieve the 4.1% fiscal deficit target this year. It has abandoned its medium-term target of reducing deficit to 3% of GDP and instead, it will aim to keep it at around 4%.

The elbow room so created will help the government invest more in India's notoriously poor infrastructure. At this juncture, the private sector is saddled with debt and the public-private partnership model is beset with problems in India, which means that infrastructure development will have to be largely shouldered by the state alone.

The government's policy budget, to be unveiled at the end of February, is likely to herald more rate cuts. Being the first full budget of the Modi regime, it is expected to conclusively demonstrate that the government can achieve its fiscal deficit target and buoy revenue next year. This will give Rajan more confidence to cut rates again some time between the budget and the RBI's next policy meeting in early April.

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For 2015, we can expect greater coordination between fiscal and monetary policies and hence, faster growth.

4. Fiscal-Monetary Co-ordination: Theory and International Experience

Fiscal-Monetary Co-ordination: Theory and International Experience', begins by setting out the macroeconomic orthodoxy which favoured a lead role for fiscal policy to address aggregate demand deficiency in economies during the Great Depression of the 1930s and to support the post-World War II reconstruction process. With monetary policy becoming ineffective at high unemployment levels, direct monetisation of fiscal deficits and keeping interest rates low were the prescribed channels whereby central banks had to acquiesce to fiscal dominance. With the failure of Keynesian policy prescriptions during the period of co-existence of high inflation and high unemployment in the 1970s amid oil price shocks and the breakdown of the multilateral fixed exchange rate system, monetary policy independence was sought to be achieved by adopting a monetary targeting approach. Nonetheless, monetary policy had to be co-ordinated with fiscal policy, particularly in cases where independently pre-set inter-temporal paths of fiscal deficits, uncertainties and objectives outnumbered the available independent instruments. Fiscal policy's potential for directly impacting price levels was brought forth by the 'Fiscal Theory of Price Level' developed in the 1990s, thereby identifying another channel of fiscal constraint on monetary policy's pursuit of price stability. Open economy extensions, particularly after the formation of European Monetary Union (EMU), and the need to address the financial stability objective, brought in more explicitly during the post-2008 global financial crisis, have also favoured the co-ordination of fiscal and monetary policies in recent years.

The experience of select advanced economies in the context of fiscal-monetary co-ordination shows that following the high inflation of the 1970s, the issue of central bank independence in the conduct of monetary policy gained importance during the next two decades. During the 1990s, many countries adopted inflation targeting, while fiscal policy increasingly became rule-based. These developments were reflected in commensurate changes in monetary policy operating procedures, while government borrowings reduced as fiscal rules came into play. The policy co-ordination mechanism between the central banks and the governments improved further during the 1990s amidst an emphasis on price stability in the UK and some other advanced countries3. By the early 1990s, many OECD countries had set up committees for consultation and co-ordination between fiscal authorities and central banks on public debt policy. At the same time, the operational responsibility for managing government debt was largely assigned to independent debt management offices with their own clear-cut objectives. This realignment of the operational framework often went together with the independence of central banks with explicit inflation mandates. Nonetheless, it is difficult to conclude whether the degree of fiscal dominance actually diminished significantly with central banks becoming more independent since the 1990s. As far as EMDEs are concerned, fiscal policy dominance was often the outcome of the importance assigned to socio-economic objectives that they had set for their respective economies. However, major economies like South Africa, India, Brazil and Russia eventually recognised that fiscal consolidation was essential to pursue and achieve the monetary policy objectives. An analytical assessment for the period up to the crisis shows that with the improving co-ordination mechanism between fiscal and monetary authorities, advanced as well as EMDEs have used both fiscal and monetary policies to deal with cyclical fluctuations.

5. Policy Coordination Problems

In this last Topic in the series of lessons we pull things together and look at world monetary policy from a broader point of view. We have been concentrating almost entirely on a situation where the world consists of one big country and a large number of small ones. It was demonstrated that, apart from situations where a small country wants to change its actual and expected inflation rate, that country will find it in its interest to keep markets orderly and thereby follow the monetary policy of the big country. If the big country is following a stable monetary policy, the small country can gain little by acting independently.

In the industrialized world, however, we have more than one big country. The Euro Area represents a currency area, and therefore a country for our analytical purposes, almost as big as the United States. And at some point, China and India will certainly also enter the picture. How does world monetary policy work when there are two big countries (or currency areas) and many small ones?

If there are two big countries following different short-run monetary policies, the exchange rate of their currencies will have a tendency to vary substantially as a result of monetary factors in addition to the whole range of real factors likely to affect it. If one of the two countries cares about this exchange rate and maintains an orderly foreign exchange market by continually supplying a quantity of base money sufficient to eliminate overshooting, that country will end up following roughly the same monetary policy as the other big country which, we assume, does not care about exchange rate movements. If both countries are anxious to avoid overshooting nominal exchange rate movements, they could end up working somewhat at cross-purposes, thereby providing an opportunity for huge profits at their expense for private speculators. It would seem that the primary tool of policy coordination should be the telephone! The authorities of the two countries or currency areas will have to work together!

If the policies of the big countries are coordinated, small countries that manage to maintain an orderly market for their exchange rate with either big-country currency will also end up following a stable monetary policy roughly equivalent to

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the similar monetary policies of the two big currency areas. If the monetary authorities of the big countries cannot agree about how to deal with current business cycle fluctuations and operate using different short-run monetary policies, each small country has to chose which of the two exchange rates to maintain an orderly relationship of their domestic currency with, and therefore which of the two big countries' monetary policies to indirectly follow.

When big countries screw up big-time, as discussed in the previous Topic Past Mistakes Big and Small, other countries which maintain orderly markets will, as there demonstrated, tend to follow the same policies and the world economy will descend into crisis. Under those circumstances there will be enormous political pressures within countries to "do something". To proceed independently and maintain some appearance of order, countries can adopt fixed exchange rates at levels that provide favorably low real exchange rates to shift world demand onto their output. They can impose tariffs to channel domestic demand onto domestic output and attempt to control capital movements to prevent domestic savings from being channeled abroad into foreign investment. Indeed, competitive devaluations and "beggar-thy-neighbor" tariff policies were a major feature of the Great Depression of the 1930s. When the rest of the world becomes unstable, there is an understandable tendency to "circle the wagons" and try to go it alone! Obviously, the world is worse off as a result of those policies!

On this sad note we could have a final test. Any appropriate questions, however, would simply be a review of what has been studied in this and earlier Lessons. It would probably be better for you to spend the time reviewing that earlier material and going over the questions asked in earlier tests.

6. Conclusion

Coordination is a fundamental problem for public administration and policy. It has been recognized as an issue in government for centuries, but continues to vex individuals who attempt to make government work better. Despite numerous attempts to make public organizations work together more effectively, there is still no standardized method for approaching coordination issues, and much of the success or failure of attempts to coordinate appears to depend upon context. Hierarchical methods for coordination may work in some settings but not in others, and that is true for all the options available.

And just as the instruments for addressing coordination problems need to be matched to circumstances, so too does the need to coordinate differ across countries and across policy areas. Some policy domains may work well with minimal attempts to coordinate with others, but others may require substantial policy integration and coordination. Likewise, political systems may emphasize coordination and government more strongly than do others (see Hayward and Wright 2002).

The practical issues for producing coordination are troublesome, but the normative issues involved may be even more difficult. How much effort should be invested in attempting to create coordination, and in what circumstances? Can the resources be better used to deliver the services rather than coordinate them? Although much of the literature on policy coordination treats better coordinated programs this as an unalloyed virtue, in the real world of governing some balancing may be required. The appropriate balance will depend upon a number of factors, but political and professional judgments are required to make the correct decision on coordination.

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