

SHRINK THE STATE

An unwarranted expansion of state power does not augur well for BRICS economies, says DEEPAK LAL

ALL the BRICS – Brazil, Russia, India, China and South Africa – seen as “shining” are currently in actual or incipient trouble. I had discussed China’s case in my previous column (“China’s hubris”, June 18). Brazil’s so-called social democratic “Brasilia consensus” is now being aped by many other Latin American countries not seduced by Hugo Chávez. Its basis is the macroeconomic stability introduced by Henrique Cardoso, combined with Lula’s adoption of the Mexican Progresista programme of conditional cash payments to the poor, financed by the commodity price boom. The resultant rise in consumer credit, shortage of domestic savings – with investment increasingly financed by foreign investment leading to a growing current account deficit and currency appreciation – and an expansion of the vast and inefficient public sector have led to overheating and a rise in inflation. A hard landing, particularly if the commodity cycle turns, is likely.

In Russia, growth has been fuelled by the commodity boom. But most of the gains have been appropriated by various public and private “mafias” generated by Vladimir Putin’s authoritarian capitalism. Inflation is rampant and many highly educated and talented young people who find that their prospects are blocked by nepotism are emigrating to the West. Recognising this, Russia’s President Dmitry Medvedev has sought to privatise the state monopolies – particularly in the resource sector – created under Putinism, but is unlikely to succeed since his mentor is breathing down his neck. Without weaning the country off its resource-based mono-economy, as Mr Medvedev realises, Russia will not be able to maintain growth, a prospect further clouded by the Russian demographic collapse.

In both cases, as in China, the current woes can be attributed to a halt in and, in some cases, a reversal of the processes of implementing the classical liberal policy package called the “Washington consensus”, after its partial implementation in the eighties and nineties led to rising growth rates and reduced poverty. But it also provided the means to expand the scale and scope of their government’s inherent dirigiste impulses. The pendulum that had been swinging worldwide from the mid-eighties away from dirigisme to economic liberalism



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– emblematic of which was the fall of the Soviet Union and its empire – has been swinging back, not least in India.

The Congress party-led United Progressive Alliance’s (UPA’s) victory in 2009, which was expected to herald a new dawn for the “dream team” of economic reformers, has turned to winter. With a government beleaguered by various scams, and in which power is wielded by Congress party president and her acolytes but responsibility is laid at the door of the increasingly helpless reformist prime minister, the well-known second-generation reforms are stalled. Moreover, the governance is increasingly being taken over by an economically illiterate judiciary – witness the recent astounding statements about black money and economic liberalisation by the Supreme Court.

The political processes resulting in a similar halt in economic liberalisation in these hitherto fast-growing economies, and which now cloud their future economic prospects, should not surprise readers of this column and of my works on the predatory state and on how past dirigisme breeds crises leading to reform, which, in turn, leads to the next cycle, as happened in Europe during much of the modern period (*The Political Economy of Poverty, Equity and Growth* by Deepak Lal, H Myint). But there are differences in the future paths that these four economies, governed by different polities and re-

source endowments, are likely to take.

In both Russia and China, the authoritarian regimes have bestowed untold riches on the predators controlling the state. In Russia, the siloviki have garnered the rents from the commodity boom through their control of natural resource-based state monopolies. In China the top functionaries of the Communist Party of China and their descendants – or the “princelings” – have their fingers in most of the lucrative pies of crony capitalism. In both countries, discontent is growing on this score, compounded in China by land expropriation by officials, which has led to many riots. But there is more hope of Russia, with its quasi-democratic system, being able to fend off this discontent through political means, a prospect not currently open to China. Both face the same problem that brought down some of the authoritarian regimes in the Arab Spring, and which haunts others: a growing educated and young population that desires economic opportunities and personal freedom. The former is more important for Russia, the latter for China. Both could lead to political crises, particularly if the economy slumps.

In both Brazil and India, the democratic system provides a safety valve for popular discontent. It also leads to populism, particularly in creating entitlement economies. In Brazil, given the dominant Christian cosmology empha-

sising egalitarianism, there is a political need to distribute some of the natural rents to the larger polity. The danger is that the entitlements thus created could become unsustainable with a fall in commodity prices leading to a crisis.

In India’s case, two kinds of populism need to be distinguished. The first, embraced by the UPA, is redistributive with an extension of state largesse. It views the majority of citizens as being dependent children who need the state to provide for them. The other is to empower the people who are fully capable, autonomous beings held back by various impediments created by dirigisme, and the state’s failure to provide the basic public goods of law and order and merit goods. This form of populism is being adopted by Nitish Kumar, Narendra Modi and perhaps Mamata Banerjee. Indian polity doesn’t need redistribution with growth, as those infected by Western cosmologies seem to believe, but greater opportunities to serve people’s own ends. India is an aspiring, not an egalitarian, society. It is tragic that the Bharatiya Janata Party, which could espouse the “good” populism”, is engaged in mindless *tamashas*.

The current problems of governance and a halt in growth prospects are owing to an unwarranted expansion of the state, after the economic liberalisation generated by the past crisis of dirigisme had reversed economic stagnation or decline. To avoid the next crisis, it is time to shrink the state.