

STATE BUSINESS RELATIONS AND ECONOMIC DEVELOPMENT IN AFRICA AND INDIA

KUNAL SEN

IDPM, UNIVERSITY OF MANCHESTER AND JOINT
RESEARCH DIRECTOR, EFFECTIVE STATES AND
INCLUSIVE DEVELOPMENT (ESID) RESEARCH
CENTRE

ROUTLEDGE-ERIA STUDIES IN DEVELOPMENT ECONOMICS

State–Business Relations and
Economic Development in
Africa and India

Edited by
Kunal Sen

ROUTLEDGE


WHAT WE TRY TO DO IN THE BOOK

- We addressed three core research questions that have been previously less studied in the literature.
- Firstly, what characterises effective state-business relations and how have they evolved over time in Indian states?
- Secondly, what are the implications of effective state-business relations for economic performance?
- Finally, how do effective state-business relations emerge? What political factors explain their provenance, and why do collusive state-business relations that are not growth enhancing persist over time?
- Both quantitative and qualitative methods, and contributions by political scientists and economists
- Based on original empirical research undertaken in India and Africa, as part of work done in the IPPG research consortium (www.ippg.org.uk)

State Business Relations (SBRs)

- Political scientists like Evans and political economists like Amsden have argued that ‘collaborative’ relations between the state and the business sector can be growth-enhancing.
- Evidence mostly relying on case-studies from East Asia.
- Lack of quantitative evidence on the impact of these collaborative relationships on growth.
- Very little evidence for Africa and South Asia

What do we understand by effective State Business Relations (SBRs)

- “a set of highly institutionalised, responsive and public interactions between the state and the business elite”

Effective vs Ineffective SBRs

Effective SBRs are more likely to be characterised by collaborative and synergistic relations between the state and the business elite

Ineffective SBRs will be more likely to be characterised by collusive and rent-seeking relations between the state and the business elite

What characterises effective SBRs?

- *Transparency* in information
- *Reciprocity* in actions
- *Credibility* in statements
- *Trust*
- *Absence of collusive behaviour* between business and states

How do SBRs affect economic growth?

Effective SBRs can help prevent both government failures and market failures.

How do they prevent market failures?

- They help **solve information related market and co-ordination failures** (e.g, business associations monitoring their members and ensuring compliance).
- Peak and sectoral business associations that are active, independent of the state and representative of the private sector in the region, can resolve many of the **collective action** problems that are inherent in developing countries.

SBRs and Government Failure

- Effective SBRs lead to **credible commitment** on the part of the government to certain policies can minimise uncertainties on future policy actions in the minds of investors.
- Creates an institutional environment where the private sector demands **high quality public goods** from the state such as infrastructure, effective public administration and secure property rights.
- **Check and balance function** on government tax and expenditures, and policies.

Why and how do SBRs matter for economic growth?

- To understand their effects on growth, we need to measure the effectiveness of SBRs.
- We need a measure that is time-varying and across countries/regions within countries to capture the effects of SBRs both over time and across space (panel data).
- We need a measure which is based on the **observable** features of effective SBRs, mostly relying on secondary data.
- **Properties of our measures:** i) in most part, objective, and not subjective; ii) formal dimensions captured more than informal dimensions; iii) combination of de jure and de facto.

Measuring SBRs

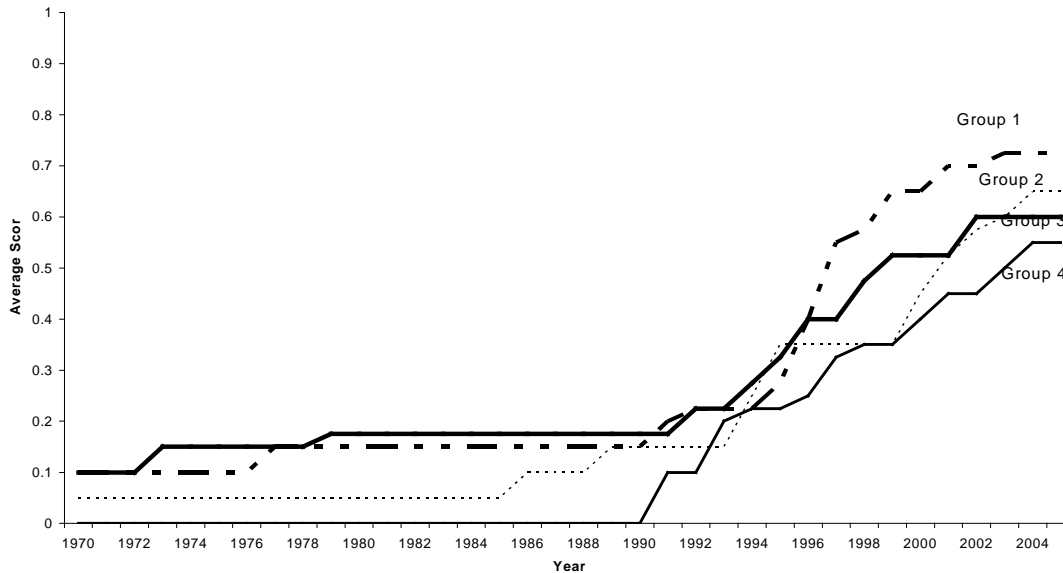
- How is the private sector is organised vis-à-vis the public sector? (e.g is there an umbrella business association, when was it formed?)
- How is the government is organised vis-à-vis the private sector? (is there an investment promotion agency, when was it formed?)
- How are SBRs practiced and institutionalised? (is there a joint economic council, when was it instituted?)
- What mechanisms are there for the avoidance of harmful collusive behaviour? (are there competition laws, when were they enacted?)

SBRs in Africa and India

- In Africa, we measured effective SBRs for 19 countries over 1970-2004.
- We used mostly de jure measures, mostly due to constraints of data collection.
- In India, we measured effective SBRs for 15 major states, over 1985-2008.
- We visited each state and could collect data that allowed us to bring in de facto dimensions of the measure.

SBRs in Africa

Chart 1 Higher SBR scores for groups of faster growing countries



Notes: Group 1 = Botswana, Mauritius, Uganda, Mozambique, Mali; Group 2 = Tanzania, Ghana, Eritrea (part), Senegal, Kenya; Group 3 = Benin, Ethiopia, South Africa, Nigeria, Rwanda; Group 4 = Malawi, Zimbabwe, Madagascar, Zambia, Cote d'Ivoire. Groups based on PPP GDP per capita growth rates over 1980–2004.

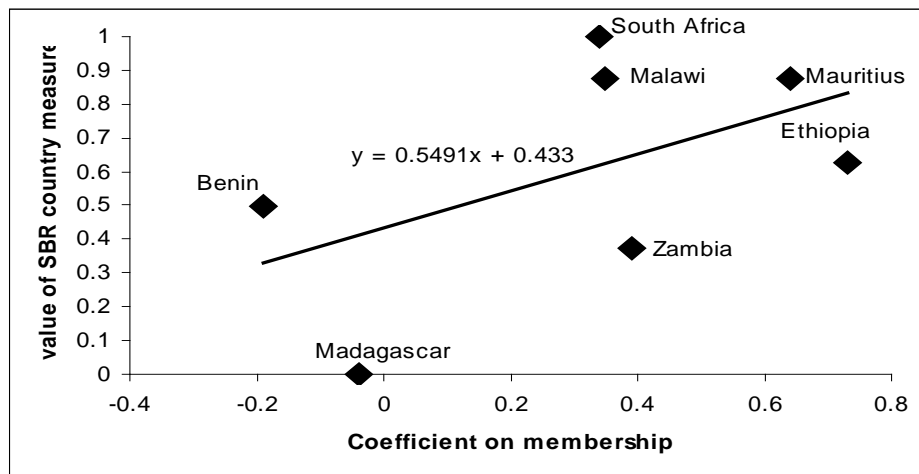
The Growth Effects of SBRs in Africa

- Dynamic panel data regressions of the determinants of economic growth in Africa show that effective SBRs have strong positive effect on economic growth in SSA (significant at 1 per cent level in most regressions).
- This effect remains robust to the inclusion of other measures of institutional quality (expropriation risk, corruption).
- Some evidence that SBRs are related to pro-poor growth as well.

The micro-effects of SBRs

- How do SBRs affect firm performance?

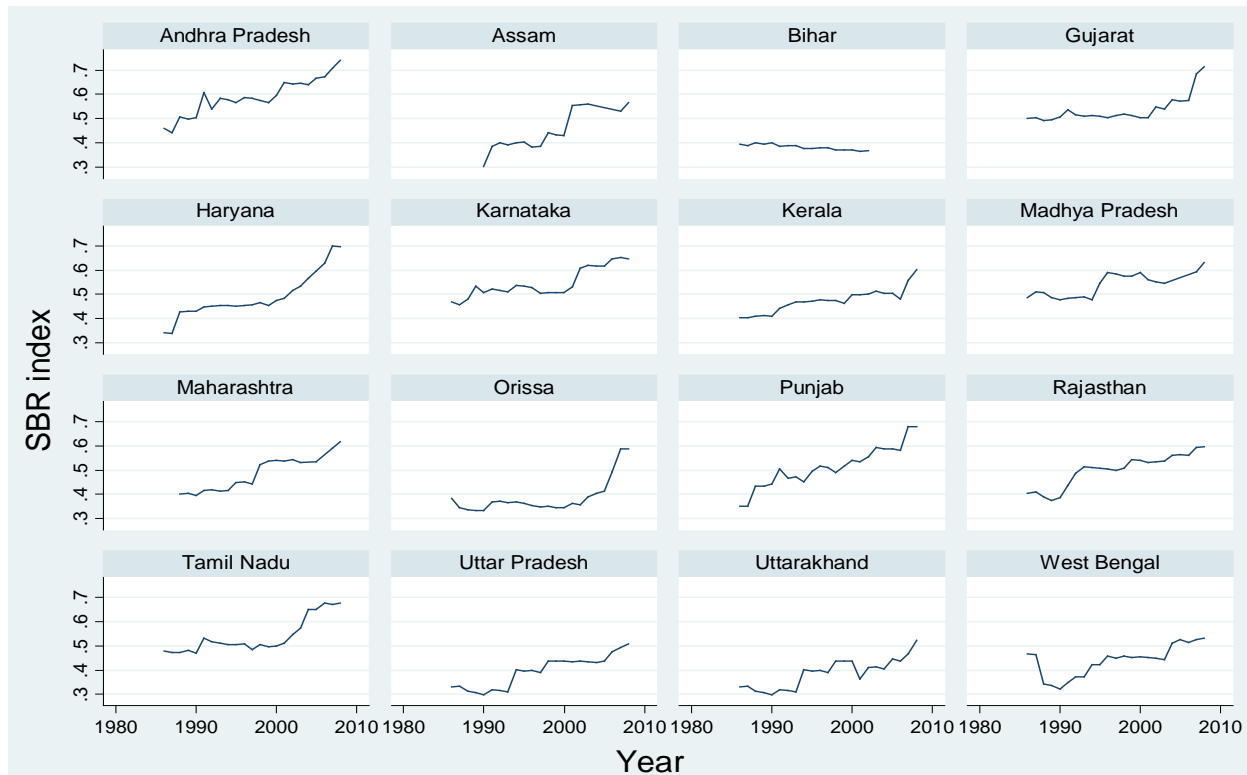
Chart 4 The effect of business association membership on productivity is greater in countries which are better prepared for state-business relations



Explaining Regional Growth in Indian States

- While economic growth in India has been strong since the mid 1980s, not all regions in India have benefited equally from the improvement in overall economic performance.
- India's federal structure and the significant political autonomy and independence in legislative powers enjoyed by state governments, along with regional variations in the collective strength of the economic and political elite, has led to strong variations in SBRs across states in India.

The evolution of SBRs in Indian States



Do effective SBRs matter for State-level Growth in India?

- We estimated dynamic panel data regressions, with 15 states and period: 1985-2004 (two stage to handle endogeneity concerns).
- Range of controls (year and state specific effects, regional effects, demographic, literacy, weather shocks, etc.)
- We found strong evidence of the impact of effective SBRs on growth, with a one per cent increase in our measure leading to a three per cent increase in long-run state-level growth.

What explains the emergence of effective SBRs in some contexts and not in others?

- **Development ideologies and goals of dominant political and economic *elites***
- **Relative power of state vis a vis that of business elite/s**
- **Organization of the bureaucracy and bureaucratic organizations**
- **Form, structure, multiplicity and representativity of Business Associations (BAs).**
- **Formal and informal institutional arrangements linking S and B**
- **Leadership / human agency.**
- ***Establishing, sustaining and renewing effective state-business relations are political processes, and cannot be had to order.***

Malawi vs Mauritius -1

- Malawi: Collusive and Predatory SBRs, shaped by 3 factors:
- i) low level of capitalist development in the country;
- ii) the dominant influence of the Malawian state under Banda in the first 30 years of independence;
- iii) the lack of distinction between the public and the private, due to informal institutions of generalised reciprocity.

(Chingaipe-Leftwichl IPPG DP 7).

Malawi vs Mauritius - 2

- Mauritius: Collaborative and synergistic SBRs
 - Recognition of shared goals between political and economic elites
 - Joint Economic Council (JEC) since the 1970s
 - Regular meetings, consultation, joint delegations

Policy Implications for Southern Govts and Private Sector

- Our research on Africa suggests that formal organisations and institutions such as existence of IPAs, formalised PPDs, private sector umbrella associations and enactment of competition laws seem to matter for economic growth.
- *IPAs and Competition Laws*: Strong signalling by the state that it takes the private sector and competition seriously.
- *Pvt Sector Umbrella Associations and Formalised PPD*: The private sector is able to convey its legitimate concerns and demands to the state in a transparent and credible manner.

Policy Implications for Donors

- A different ‘institutional’ approach to economic growth, that stresses govt-private sector relations and interactions. Clear evidence that these relations and interactions matter for economic growth.
- Supporting and brokering *processes* which facilitate good SBRs.
- **Business associations can be developmental.**
- Support for SBRs should be provided by strengthening the actual practice of SBRs rather than by establishing formal organisations to carry out such interactions.
- The Indian case is a counter-example to the argument that creation of IPAs and peak umbrella associations are enough.