Lesson from Downturn: Good Governance for Recovery and Resurgence

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Now that a clear recovery is on the way and India can expect to go back to the trend path of 8 percent GDP growth rate next year (2010-11), it is necessary to list the lessons from the last two years to avoid past errors and lay the foundations for good governance practices for a promising future. Ben S. Bernanke, the Federal Reserve Chairman, U.S. said in a recent speech (American Economic Association Address, January 4, 2010) that regulatory failure (involving issues of governance) but not low interest rates was responsible for the housing bubble and financial crisis. Governance was painfully weak. That good governance is at the heart of economic growth (Rangarajan, 2006). Corporate governance is the central and dynamic aspect of business (Drucker Peter, 1980). Good governance is the manner in which the authority of the State is exercised in the management of a country's economic and social resources for maximizing welfare. It has to inject shock-absorbing capacity into the anatomy of an economy. In the ultimate analysis, it is the quality of governance that separates success and failure in economic development. Good governance always calls for accountability for results and actions. Needless to say that leadership is also critical.

Even in downturn, fundamentals do not change. But the specifies to manage them do change greatly with changes in internal and external conditions. The task is to govern what there is and work to create what could and should be. The controlling word is 'must'.

The economic downturn has pointed its glaring fingers at the difference between weak governance and poor policy. The learning failure has adversely affected the governance. This would even undermine the future effectiveness of the governance. The aim of this paper is to ascertain the factors that caused poor governance. The paper also makes an attempt to analyse good governance practices for a promising future.

Problem Identifying

In economics, a recession is a business cycle contraction, a general slowdown in economic activity over a period of time. During recessions, many macroeconomic indicators vary in a similar way. Production as measured by Gross Domestic Product (GDP), employment investment spending, capacity utilization, household incomes, business profits and inflation all fall during recessions; bankruptcies and the unemployment rate rises.

Generally an administration, say, the governance gets credit or blame for the state of economy during its time. This has caused disagreements about when a recession actually started. In an economic cycle, a downturn can be considered a consequence of an expansion reaching an unsustainable state, and is corrected by a brief decline. Thus it is not easy to isolate the causes of specific phases of the cycle. The 1981 recession is thought to have been caused by the tight money policy adopted by Paul Volcker, Chairman of the Federal Reserve Board before Ronald Regan took office. Regan supported that policy. The resulting turning of inflation did, however, set the state for a robust growth period during Reagan's administration.

It is generally assumed that Government activity has some influence over the presence or degree of a recession. They are often unsuccessful, at least at preventing a recession. Could this be referred to an issue of governance failure?

Most mainstream economists believe that recessions are caused by inadequate aggregate demand in the economy and favour the use of expansionary macro economic policy during recessions. Monetarists would favour the use of expansionary monetary policy, while

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Keynesian economists may advocate increased government spending to spark economic growth. Supply-side economists may suggest tax cuts to promote business capital investment. Laissez-faire minded economists may simply recommend that the government not interfere with natural market forces. This naturally raises the issue of sound development management and good governance. It explains the manner in which power is exercised in the management of a country's economic and social resources for development (Shetty,2003). Thus, good governance as a condition for sound development is universally well recognized. This is a must. What is good governance? What are its characteristics? Why failures occur? Let us dwell on these critical aspects.

The term 'governance' derives from the Latin gubernare, meaning 'to steer', usually applying to the steering of a ship, which involves the issues of direction and control. In the literature of economic management of an economy, governance represents effective delivery. In this backdrop, it is worth noting with the World Bank's conception of governance:

▲ Economic role for the state which include (a) maintaining non-distortionary policy environment with macro-economic stability, (b) investment in basic social services and infrastructure, (c) protecting the vulnerable, (d) protecting the environment, and (e) enabling legal foundation;

▲ Policy reforms required to move towards such governance which include fiscal consolidation, reduction and redirection of public expenditure tax reforms trade and investment liberalization, deregulation and privatization of state enterprises;

▲ Non-economic aspects of governance relevant for sound development which include electoral democracy, transparency, accountability, participation and responsive rule of law, effective enforcement of contracts, in dependence of judiciary and protection of human rights.

While discussing about good governance, it is contextual to refer to the debate thrown up by economic reforms on the role of the government. Liberalization implies the state yielding economic space to the market. This has given rise to the stereo type view that in the post-reform scenario, the government has a smaller role because the market now taken over part of what government has been doing. This is a misperception. In the words of C.Rangarajan, "In the reform context, the government has, not a smaller role, but a different role, and arguably a more critical one. More market does not mean less government but different government".

Conceptually, the role of the government in the reform context can be divided into two broad strands. The first strand of the role of the government arises from performing those functions that the government alone can perform. In the transition to a market system, government needs to move out of areas where market can perform , conversely, government needs to concentrate its efforts and resources in areas where market do not exist or cannot perform or deliver. For example, maintaining macro economic stability and sustainability. Then there are government functions which arise as a result of market failure. Market failure represents a set of conditions under which markets fail to allocate resources efficiently because of the myopic nature of the market participants. The second strand of the role of the government in the return context is to 'govern' the market to maximize collective welfare. Market is not self-regulating. The government has a central role in regulating the market. Indeed, this is a true issue of governance in the context of downturn. Now let us understand some of the characteristics of good governance. This includes: (i) rule of law (ii) accountability for actions and results and (iii) style of leadership.

Rule of law is essential to maintain an orderly civil society. Enterprises cannot thrive if there is no rule of law. Rule of law has certain distinct characteristics. There is a set of law rules known in advance, second, the law/ rules are effectively enforced, third the law/

rules are enforced in a transparent and non-discriminatory manner. Further, there are established institutional mechanisms for making new laws and for amending/modifying existing laws to reflect the changing situation and finally, the process for making laws are participatory and consultative.

Experts view that in many respects our overall governance is so much worse than in many other developing countries. Our governance structures are quite dismal in our enforcement of law and order, in our economic regulatory framework in civil administration (particularly at the urban municipal and rural panchayat level) and even in the private sector at he factory shop floor level. This is behind our weak implementation of well intentioned laws, our infrastructural deficit our relatively low productivity in manufacturing and the poor transmission of the benefits of high economic growth to the majority of people.

But nowhere is our governance as atrocious as in the case of delivery of basic social services (public health and sanitation rudimentary health care, primary secondary education, etc). Our basic health indicators are so much worse than those in poorer countries like Bangladesh several countries in sub-Saharan Africa.(Just to give an example, the incidence of underweight children in Gujarat, one of our most economically advanced states, is substantially worse than the average for Sub-Saharan Africa). Our civil administration is organized in a way that is not performance based. It is more seniority based and the reward for innovative performance are weak (Bardhan Pranab, 2010) Governance at all levels is bound to be weak when social actors have a rather relaxed attitude to law-breaking as in India.

The government is the ultimate trustee of public resources and is responsible for using them for maximizing collective welfare. This requires that there are institutional ional mechanisms not only for determining how the resources are allocated but also for demanding accountability for results.

Style of leadership is crucial when the economy recovers, things won't return to normal and a different mode of leadership will be required. (HBR,2009). Experts view that today's mix of urgency, high stakes, and uncertainly will continue as the norm even after the recession ends. Economies cannot erect a firewall against intensifying global competition, energy constraints, climate charge and political instability.

The immediate crisis which we will get through with the help of policy makers expert technical adjustments merely sets the stage for a sustained or even permanent crisis of serious and unfamiliar challenges. It is like heart attack. Consider the heart attack that strikes in the middle of the night. After proper medical treatment and surgery –stabilizes the patient and then provide new vessels for the heart. The emergency has passed, but a high stakes, if somewhat less urgent, set of challenges remains. Having recovered from the surgery, now does the patient prevent another attack? Having survived, now does we adapt to the uncertainties of a new reality in order to thrive? This crisis is far from over.

The task of leading during a sustained crisis-whether one is the CEO of a major corporation or the Government is treacherous. Crisis leadership has two distinct phases. First is that emergency phase, when our task is to stabilize the situation and buy time.

Second is the adaptive phase, when we tackle the underlying causes of the crisis and build the capacity to thrive in a new reality. The adaptive phase is especially tricky. People put enormous pressure to respond to their anxieties with authoritative certainly even if doing so means overselling what we knew and discounting what we don't. Twists and turns are the only certainty. Yet a person still have to lead. Adaptive leadership has taken the position here. They seize the opportunity of moments to hit the organizations reset button. They use the turbulence of the present to build on and bring an and bring closure to the past. In the process, they change key rules of the game, reshape part of the organization, and redefine what people should do. The process of adaptation is at least as much a process of conservation as it is of reinvention. Governance is an issue of leadership. Good governance means good and authentic leadership (taking responsibilities for one's actions). Today, leadership is an improvisational and experimental art. The skills that enabled most executives to reach their positions of command – analytical problem solving, crisp decision making, the articulation of clean direction - can get in the way of success. Although these skills will at times still be appropriate, the adaptive phase of a crisis requires some new leadership practices. Executives today face two competing demands in their actions. They must execute in order to meet today's challenges. And they must adapt what and how things get done in order to thrive in tomorrow's world. They must develop "next practices" while excelling at today's best practices. In fine, adaptive leadership is a daily opportunity to mobilize the resources of people to thrive in a changing and challenging world. As Peter Drucker opined, "most people need to feel that they are here for a purpose, and unless an organization can connect to this need to leave something behind that makes this a better world, or at least a different one, it won't be successful overtime."

The Road Ahead

The heart of governance is leadership and leadership is all about better decision making. When we confront a situation, our mind looks for a precedent among actions without regard to whether a decision was made in emotional or unemotional circumstances. Better decision making is crucial for leadership. Decision making has rarely been the focus of systematic analysis inside the firm. (Davenport, 2009). Especially in the context of economic crisis, organizations need to give managers the tools and assistance to "decide how to decide". Managers should be trained to determine whether a particular decision should be made unilaterally by one manager, unilaterally after consultation with a group, by a group through a majority vote, or by a group consenses. In addition, who will be held accountable for results, and who needs to be consulted or informed. The result is a good governance. This is, of course, a reasonably good recipe for everyone. We may now remember the scholarly words of C.Rangarajan indicating the contents of good governance: "Good governance is a combination of transparent and accountable institutions, strong skills and competence, pecuniary and professional integrity, and fundamental willingness them to do the right thing."

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