Energy Policy 68 (2014) 465–475

Contents lists available at ScienceDirect

Energy Policy

journal homepage: www.elsevier.com/locate/enpol

Economic populism, partial deregulation of transport fuels and electoral outcomes in India☆

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HIGHLIGHTS

- Incumbent politicians' influence on fuel pricing.
- Fuel prices manipulated and increases delayed until after elections.
- Price reductions brought forward.
- *ex ante* Inflation expectations of voter–consumers.
- Electoral outcomes.
- Price manipulation found irrelevant to electoral performance.

ARTICLE INFO

Article history:
Received 6 December 2013
Received in revised form
14 January 2014
Accepted 17 January 2014
Available online 10 February 2014

Keywords:
Administered prices
Coalition governments
Populist measures
Anti-incumbency
Electoral outcomes

ABSTRACT

The Indian political class is known to employ populist, albeit economically unsustainable, measures to replace intrinsic 'valence', especially shortly prior to election windows. Such measures include loan-waivers, interest rate concessions, provision of free electricity for agriculturists, etc. The union government's leverage to maneuver and to micro-manage retail fuel prices within partially deregulated environments is hypothesized to provide incumbents with an advantage over rival contestants in the electoral process. This paper analyzes the evolution in the retail prices of diesel and petrol (gasoline), and the transfer of such evolution, into the inflation index of the 'all commodity' basket. It is observed that when international benchmark prices are relatively low and domestic inflation is moderate, the transfer occurs within about 42 weeks. During periods of high oil prices-frequently above USD 100 a barrel-and high inflation-higher than 5.00–5.50%-prices of petroleum distillates tend to feed into overall inflation more rapidly, within about 34–40 weeks.

The study, covering a total of 82 elections for the central and state (provincial) governments during the period 2000 to 2013, concludes that even as patterns of manipulation of prices are apparent, ceteris paribus, such leverage does not necessarily seem to translate into favorable electoral outcomes. This conclusion reiterates observations that economic im/prudence may not necessarily determine electoral outcomes, and that the basis for electoral choices made by the Indian voter–consumer remains subjective.

1. Background on the Indian political scenario

Elections in a representative democracy provide opportunities for competing political formations to highlight, and to consequently try and obtain endorsement of their ideological positioning, and of the policies that flow there-from. Nordhaus (1989) holds that voters care about the economy and societal well-being, while politicians care about power. This leads to the conclusion that, in a democracy, incumbents' objective is to remain in office, but the incumbents are required to face elections at pre-defined intervals towards this end. While discussions on economic and welfare issues continue to remain relevant, elections in India, the world's largest representative democracy with over 700 million

☆An earlier version of this paper, "The Irrelevance of Political Populism", was published as a part of the author's compilation of articles on Environmental Finance titled, *Enabling Environment: A Worm's Eye View of Environmental Finance*, Springer Verlag, 2013, p. 11–27, http://link.springer.com/chapter/10.1007/978-81-322-0882-2_2.

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[1] *Disclaimer*: The views expressed in this article are of the author himself and do not necessarily reflect those of any organization.

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http://dx.doi.org/10.1016/j.enpol.2014.01.026

voters, seem to have been "dominated by fundamentalist and divisive issues that surface during election time", (Sthanumoorthy and Eapen, 2004). On several occasions, and in many of the provinces (used interchangeably with "states"), it is believed that when people cast their vote, they generally vote their caste, or religion, or ethnic group en masse, though this could never be substantiated by real data. Mohapatra (2000) reflects on this inherent contradiction between intention and consequences and concludes that the election is *not* a perfect mirror in which the essence of the everyday politics is reflected in India, and "in fact, the mismatch, as well as, the occasional overlap between the two, characterizes India's electoral democracy of the last 50 years."

An apparent exception to the norm was the victory for the *Telugu Desam* Party (TDP) in the September 1999 elections to the Andhra Pradesh state legislature (Assembly), which was hailed as a vote in favor of focused effort, transparent administration and sophisticated management of the development process, as opposed to political rhetoric or the usual "irrepressible urge to enthrall audiences", (Harshe and Srinivas, 1999). And yet, ironically, the very economic reforms seem to have led to the TDP government's downfall in 2004, voted out of office by those on the margins of the reform process (Ayyangar, 2004). Consequently, governments in power have tried hard to highlight the 'feel-good' factor across sections of society, and to enhance positive sentiments on the eve of elections, attaining its peak with the, now satirical, "India Shining" campaign by the then in-power *Bharatiya Janata* Party (BJP) in 2004. The National Democratic Alliance (NDA) led by the BJP was defeated by the United Progressive Alliance (UPA) led by the Congress party and supported by the Communist Parties.

This paper is an attempt to systematically assess the impact of populist initiatives launched immediately prior to elections, and consequently, a political party's ability to retain or assume power. The populist measures (or promises) employed to generate short-term gains for incumbents (challengers) include subsidy announcements, loan waivers, softening of interest rates to help reduce loan-payouts, exchange rate manipulation to reduce prices or benefit certain sections, etc. This paper utilizes the management of administered prices of petroleum distillates-petrol and diesel-as a proxy for such populist measures. Although transport fuel prices are important on their own accord, they are tracked more closely for their impact on the price levels of other commodities and services of routine consumption.

Obviously, unrealistic or inconsistent promises, especially relating to energy and fuels, are not exclusively limited to Indian politics. Suspending petrol taxes, slapping windfall taxes on oil companies, clamping down on speculators, or even dragging OPEC (the Vienna, Austria headquartered Organization of Petroleum Exporting Countries) to the World Trade Organization (WTO) for its "anti-competitive behavior" are all ideas aired during the US presidential election campaign of 2008, (Economist, 2008a). It is common knowledge that energy-related issues viz., the phase-out of nuclear energy, oil and gas pipeline projects, sharing of river waters and hydro power generation etc. are debated prior to elections in several countries, across continents, as a means of mobilizing various ideological, interest and pressure groups.

Evidently, the evolution of fuel prices is firmly intertwined with the electoral process in India, with the popular perception that pricing decisions made by the oil marketing companies (OMC) are motivated by the federal government, even if the latter denies any involvement at all. With many of the major OMCs, substantial refining capacity, exploration and production operations etc. being largely government owned, holding power at the central government in India, or participating in the ruling coalition at the federal level, is believed to provide adequate leverage for an incumbent political formation to influence fuel-price policy. Ostensibly, the incumbents alone are in a position to manipulate prices to their advantage, and politicians in opposition can merely oppose price hikes and try and direct public opinion against them.

Since few politicians possess the natural charisma to charm audiences, most resort to campaigning on the basis of an acquired "valence", (Kendall Chad et al., 2013), as with being the managers of fuel prices, in the manner of portraying themselves as poor-people-focused policy makers. The time elapsed in transferring a change in the price of petrol and diesel to commodities of everyday consumption represented by the economy-wide inflation measure-and thereby fading from the voters' recall-is, therefore, a politically significant statistic. This paper assesses (i) the re-election probability for incumbent politicians, consequent to the micro-management of fuel prices or (ii) the possibility for regime change owing to unfavorable pricing scenarios and their adverse impact on the incumbent's political prospects.

2. An overview of price controls and the political process

Price controls are slated to yield immediate political gains, whereas the associated distortions and economic costs become evident only in the long run, even as the same cannot be mapped directly onto the price controls. Such irregularities, combined with the short attention spans of the voting public, are exploited in democracies in general, and in India in particular. Agenor and Asilis (1993) have studied the interactions between electoral considerations and the imposition of price controls by opportunistic incumbent politicians, and have demonstrated that price controls are imposed in periods leading to the election, and are removed immediately afterwards. Stretching the argument further, Ozatay (2005) studies electoral-inflation cycles and provides empirical evidence of pre-election manipulation of public sector enterprise pricing in Turkey during the period 1987–2003. In India, despite the much talked-about liberalization of the economy, the political process and its participants continue to exert a considerable influence on economic outcomes in the country. For instance, Kakani et al. (2006) have found that the Indian parliament's merely being in session, and the consequent uncertainty associated with policy decisions, coincides with wealth destruction on the stock markets, and parliament's being in recess correlates with an increase in wealth. Investor discomfort with the most likely launch of populist measures immediately prior to elections has historically led to higher volatility in the valuation of the Indian Rupee during election seasons, (Economist, 2013).

Over the years, the highly-regulated energy sector, among others, has been subject to intense scrutiny. Illustrating the conflict between economics and populism, Dossani and Ranganathan (2004) stress the importance of the political-will required to reform the heavily subsidized electricity prices, especially in rural India, where revenue collections are meager relative to the numbers of consumers, to ensure cost-recovery for the electricity utilities. Likewise, the prices of petroleum products in India are caught in an opaque web of cross-subsidies, taxation and normative pricing, as refined products such as petrol (gasoline), diesel, kerosene etc., are retailed at prices determined or managed by the federal government (Sridhar, 2008). Despite the phased restructuring of the administered price mechanism (APM), over the years, the upward revision in retail prices of distillates, to remain consistent with cost recovery for the refiners and retailers, continues to test the federal government's ability to push-through politically unpalatable decisions in the larger interest of the economy. Retail fuel prices, which tend to feed into the inflation in commodity prices faced by the voter–consumer, are therefore