period, as compared to the 1980s. Urban poverty, however, appears to have declined faster during the reform period. Thus, the reform process appears to have an urban bias.

- The fiscal discipline, as indicated by the fall in fiscal deficit, has been achieved through drastic reduction in public investment, particularly in the social sector, rather than through cutting down of wasteful government expenditure. In the year 2000-01 alone, the shortfall was about Rs.19,000 crore. The cut mostly fell on agriculture and rural development.
- Critics also point out that in many FDI, money has flown from parent companies to their subsidiaries. This has been through the device of acquiring the shares of the subsidiaries by the parent companies at below market price. Such companies then have proceeded to introduce new consumer products and compete with domestic manufactures of similar products. It is also true that the contribution of the Multi National Corporations (MNCs) to the exports from the country has not been impressive.
- There has been lot of associated pains and apprehension with structural reforms. For example, in our country we still do not have an effective social safety network against loss of industrial employment as a result of the reform process.
- The disinvestment policy of the government has not taken off as anticipated. This has resulted in borrowed funds, continuing to sustain the unviable public sector undertakings (PSUs), pending their eventual divestment.
- Conservative observers also point out that the reforms have exposed the Indian economy to the unpredictable fluctuations in different economies of the world. Despite our growth being driven mostly by domestic demand, our capital market is increasingly exposed to the interest rate changes in the federal reserve system of the USA, the Balance of Payment (BOP) situation in Japan, expectation of growth in China , and problems like that of sub prime loans in the USA. This curtails, critics maintain, the much 'desirable' isolation of a developing economy from external disturbances.

the fast changing dynamic world. A kind of lethargy was getting in built into the system that was captured by the so called "Hindu Rate of Growth" of about 3.5% that kept the growth of per capita income at a meager 1.5% per annum even after four decades of planning. The factors responsible for such a sorry state of affairs constitute both the background of the crisis of 1991 and the rationale for the economic reforms that were bold and path breaking. In the following we shall briefly discuss some of these important factors.

- **Unsatisfactory Development:** Despite four decades of planning and hundreds of programmes of poverty alleviation, vast majority of the population lived in abject poverty and thereby resulted in a loss of potential human resource and continued and increasing the burden of the State. There were 260 million (about 26% of population) people living below the poverty line. This implied low literacy, low life expectancy, as well as very poor standard of living. Not only this, whatever development had occurred was distributed very unevenly. As a result there were growing inequalities between classes, between regions, and between rural and urban areas. This created socio economic dualism which was detrimental to growth and progress.
- **Faulty Methods:** The ills in the developmental front could be traced to methods adopted for development. Control cum regulation mechanism had turned out to be the biggest hurdle in the growth of genuine entrepreneurs, dynamic investors, efficient managers, and hard working laborers. The public sector was decaying under bureaucratic functioning, time consuming procedures that were inflicting a huge burden on the government's treasury. Over the years, a well entrenched vested interest had emerged that were simply anti development. There was an absolute lack of economic vision, economic leadership which led to sub optimal use and even outright plundering of precious resources.
- **Non Plan Expenditure:** Apart from the ever increasing burden of interest payment, subsidies, and defense expenditure, the non plan expenditure of the Government was increasing year after year. This added to the

fiscal deficit with its disastrous consequences of high debt burden and inflation.

- **Capital Inadequacy:** Given the low level of economic development of the country, the capital requirement was huge to make it a modern, dynamic and growing economy. But such enormous amount of capital could not be raised internally. This meant that capital has to come from external sources. But borrowing will only mean adding to the already ballooning debt burden. Thus the need of the hour was to attract foreign private capital. This required opening up of the economy to the world, thereby reversing the age old inward looking strategy. The import liberalisation, devaluation of the currency, incentives for both foreign portfolio investment and foreign direct investment were the only way out to meet the scarcity of foreign exchange and unproductive protection of domestic industries.



CHECK YOUR PROGRESS

Q 1: What was the foreign exchange reserve of our country in June, 1991?

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Q 2: What is meant by the term 'Hindu Rate of Growth'? (Answer in about 30 words)

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Q 3: What was the immediate crisis that resulted in the economic reforms of 1991? (Answer in about 40 words)

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Q 4: State four factors responsible for creating the 1991 crisis. (Answer in about 50 words)

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growth trajectory of about 9%. The immediate aim of our policy makers is to reach the double digit rate of growth at the earliest. Thus the days of the Hindu rate of growth seem to be finally over.

- The Indian industry grew at the rate of 8.1% during reform decade as against 7% during 1980s. The rate would have been higher but for the deceleration in the industrial sector during 1996-97, 1997-98, and 1998-99. Industrial growth has averaged about 9.5% since 2004-05.
- The growth in agricultural sector has not been uniform, ranging from 0.7% in 1997-98 to 9.1% in 2003-04 and presently about -2.8%. But there has been considerable diversification in this sector.
- The Foreign Direct Investment (FDI) jumped from US$200 million in 1991 to US$14.6 billion in 1997. The flow of foreign capital during the reform period can be gauged from the fact that from a mere US$1billion as foreign exchange reserve (forex reserve) in 1991, the total forex reserve has gone up now to about US$300billion.
- The fiscal deficit has been brought down to manageable level i.e. below 6% of the GDP from the unsustainable level of 7-8% during 1985-91. With the passing of Fiscal Responsibility and Budgetary Management (FRBM) Act, 2003, the government is now legally bound to bring the fiscal deficit down to 3%. However, due to the exceptional circumstances created by the Great Recession (2007-09) , the fiscal deficit has gone up to 6.8% in 2009-10, but targeted to be brought down to about 4% in 2012-13.
- The proportion of trade in India's GDP has gone up from 14% in 1990-91 to 18% in 1998-99. This has been achieved by consistent high growth of imports and exports. In recent years, exports have grown by about 20%, while imports have increased by 25-26%.

However, despite the above mentioned achievements, critics point out that the reforms have not been an unmixed blessing. The following issues are raised in this context.

- The impressive growth rate of the GDP has only led to the widening of the gap between the rich and the poor. All available evidence show that the pace of decline in rural poverty has slackened in the post reform



CHECK YOUR PROGRESS

Q 5: When and by whom the New Economic Policy of India was announced? (Answer in about 20 words)

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Q 6: State two broad components of economic reforms of 1991. (Answer in about 40 words)

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Q 7: State the four distinct areas of actions under the stabilisation programme. Name the components of structural adjustments under the 1991 reforms. (Answer in about 50 words)

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14.5 INDIAN ECONOMY SINCE ECONOMIC REFORMS

Post 1991, the Indian economy has shown many positive features and increasingly establishing itself as a leading emerging market in the world. The positive outcomes of the economic reforms so far may be summarized as follows:

- The rate of growth of GDP has increased appreciably during the reform period. The annual average rate of growth of GDP during 1980-91 was only 5.8%. This has gone up to 7.2% during 2001-07 which is the second largest in the world. During the 2007-08 GDP grew by about 9%. For the Eleventh Five Year Plan the GDP is expected to be on a higher

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14.4 NEW ECONOMIC POLICY OF 1991

The New Economic Policy was launched by Dr.Manmohan Singh in his June, 1991 budget as the Finance Minister of India. This ushered in an era of economic reforms in India which can be broadly classified into the following two groups :

- A short term stabilisation programme to bring the economy back on track.
- A medium to long term structural adjustment programme to correct structural rigidities and bottlenecks in the economy.

In the following, we are shall elaborate on these two aspects.

Stabilisation Programme: The aim of this programme was to control inflation and remove the Balance of Payment (BOP) deficit. It consisted of four distinct areas of actions. These are: fiscal policy, monetary policy, exchange rate policy, and social sector policy.

In fiscal policy, the objective was to reduce the government's fiscal deficit by reducing government expenditure on the one hand and increasing the tax base on the other. An ambitious target of lowering the fiscal deficit from 8.4% in 1991 to 5% of Gross Domestic Product (GDP) was fixed. A review of food and fertilizer subsidies was undertaken. The Chelliah Committee was appointed to look into the taxation structure and suggest measures to augment revenue. As a result of these measures, fiscal deficit fell to 6% in 1991-92 and to 5.6% in 1992-93.

In monetary policy, credit was tightened by increasing interest rates. The Narasimham Committee was appointed to recommend measures for financial sector reforms. The RBI was given more autonomy and automatic monetisation of government's deficit was given up.

In order to correct the exchange rate, Rupee was devalued by 23%. In February the Government of India announced the Liberalized Exchange

Rate Management System (LERMS) to promote trade. In the next stage Rupee was made convertible on current account in 1994-95 budget.

In the social sector, the experience of African and Latin American countries had shown the stabilisation programme made the poor suffer disproportionately. Drastic cuts in subsidies and increase in taxation impoverish the weaker and vulnerable sections more. Consequently the international organisations like the UNICEF recommended adoption of a stabilisation programme with a 'humane face'. In view of this, Indian reformers built into the reform package measures to protect the vulnerable sections from the fall out of macro economic adjustment. The allocation for merit goods and poverty alleviation schemes was increased. A social safety net programme was launched consisting of Employment Assurance Scheme (EAS), Prime Minister Rojgar Yojana (PMRY), National Social Assistance Programme(NSAP), Mahila Samriddhi Yojana(MSY), and Indira Mahila Yojana(IMY). The Public Distribution System (PDS) was revamped for targeting the deserving beneficiaries.

Structural Adjustment : Structural adjustment consisted of industrial policy liberalisation, public sector reforms, financial sector reforms, and trade policy reforms.

A path breaking new industrial policy was announced in July 1991 with the abolition of licensing of industries on virtually all items except those involving environmental problems or involving national security. The MRTP (Monopolies and Restrictive Trade Practices) Act was liberalized to encourage investment by large industrial houses. As a follow up to this, recently, a new Competition Act has replaced the MRTP Act. Measures were taken to encourage foreign direct investment (FDI) by replacing Foreign Exchange Regulation Act (FERA) by Foreign Exchange Management Act (FEMA) and making foreign investment and collaboration automatic in most cases.

The public sector reforms include getting out of areas where the public sector will be more efficient and disinvestment of equity in selected units. The list of industries reserved for the public sector was reduced from 17 to 6. Subsequently it has been brought down further to 3 items – atomic

energy, some substances used for atomic energy, and railway transport. Even the defense industry has been opened up for the private sector with FDI permissible up to 26% ownership share. The Memorandum of Understanding (MOU) system of monitoring public sector units was introduced. Social safety network has been put in place to protect workers from the adverse effect of restructuring the public sector units.

The financial sector reforms are based on the recommendations of the Narasimham Committee. The main features of these reforms are :

- unshackling of the banking system from excessive government control;
- curtailment of government tendency to rely on credit control measures (like Cash Reserve Ratio, Statutory Liquidity Ratio) and extra budgetary sources of inexpensive credit
- Signing of MOU with the RBI on discontinuation of adhoc treasury bills (1994).

The capital market reforms started with the establishment of Security Exchange Board of India (SEBI) in February, 1992. The other major steps were permitting Foreign Institutional Investors(FIIs) to undertake portfolio investment and letting Indian companies to undertake Euro issues. Over the years several reforms have been introduced in the capital market with SEBI playing a very active role. At present the Indian capital market has become more or less scam free. Defective practices like P note (participatory note) issues etc. have been rectified. As of now, the Indian stock market has been one of the strongest and best performing markets in the world. The primary market is also robust, and thanks to the strength of the macro fundamentals of the Indian economy, the Indian stock market is said to be in a structural bull run.

The trade policy reforms led to major changes in the import licensing system. Except for consumer goods, all non-tariff barriers (NTBs) have been lifted. Peak tariff rates have been brought down from 355% to about 50%. As a signatory of World Trade Organisation (WTO) agreement, India is committed to bring the tariff rate further down.