UNIT 7 ECONOMIC REFORMS IN INDIA

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7.0 OBJECTIVES

After reading this unit, you will be able to:

- define economic reforms;
- contrast efficiency-seeking reforms with equity-seeking reforms;
- delineate the nature of neoliberal economic reforms;
- narrate the crisis brewing in 1980s and precipitated by Gulf War in 1990;
- shed light into the background necessitating current genre of reforms;
- explain macroeconomic stabilisation and structural adjustment programmes; and
- make a distinction between the first generation and the second generation reforms.

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7.1 INTRODUCTION

Every day, we in India keep hearing, or reading news about some or the other economic reforms that have been brought in or would be brought in shortly. They are either introduction of new interventions or withdrawal of old interventions by the government in managing the economic affairs of the country– particularly in the structure and operation of markets.

In the previous Unit, it was discussed as to why and how government intervenes in the market and also why and how, at times, it chooses to withdraw certain interventions. Introduction, modification, and withdrawal of government interventions depend partly on ideology, partly on evolving situation– both internal and external, and partly on the efficacy of the prevalent institutions to meet the development objectives.

Interventions brought in by the government are said to be 'reforms' when they are significant and, generally pro-active but they are short of being a revolution. It seems significant institutional/instrumental changes have often been called reforms and technological or social ones, revolutions. The latter are not necessarily always prompted or promoted by government but they invariably have a significant consequence for a society. Reforms too could be social– anti-sati or anti-slavery; economic– agrarian and industrial; political– parliamentary and electoral, etc. So could be revolutions– American or French Revolution on political front and Industrial Revolution or Green Revolution on economic front. However, reforms in this Unit will mean economic reforms and only those undertaken by the government. They thus refer to reforms in economic policy and management of the government.

In India, there were a set of reforms carried out after independence in several institutional arrangements, the first being in the sphere of land relations. They were duly referred to as reforms by policymakers and scholars though in legislative parlance few of the Acts were named 'reforms' (Even introduction of expenditure tax in mid-1950s was called a tax reform). Likewise, when in early 1990s steps were taken to liberalise business, privatise government enterprises, and open the economy for international trade and investment, they have been called reforms by policymakers and scholars alike but not necessarily in legalese where the word often used is regulation or management.

This unit proposes to explain the meaning and nature of economic reforms carried out since independence and post 1991, and discuss the features and contours of reforms carried out during these two different periods.

The unit is, however, intended to explain rather than assess the neoliberal reforms in terms of the political economy, which may not be very charitable. Assessment is invariably coloured by one's ideological persuasion.

7.2 ECONOMIC REFORMS: MEANING AND NATURE

Reform means improvement, amendment, correction, or rectification of an intervention that has proved less than satisfactory in its performance or found to be inadequate or inappropriate in terms of meeting its intended outcomes. They

could be carried out in agriculture, industry, labour, and trade sectors; in banking, insurance, and other financial sectors; and even education and health sectors. There could also be fiscal reforms – tax and expenditure reforms; monetary reforms– banking and financial; or currency reforms – exchange rate system and convertibility reforms. Pan-economy reforms are often said to be macroeconomic reforms – particularly when they address stabilisation issues, while sectoral reforms are often said to be microeconomic reforms as they influence production levels and prices of individual commodities. Yet, there may be such macroeconomic policies which embed microeconomic dimensions – say differential rates of interest for different sectors or differential charges for different power or transport categories of users.

As the economic context changed in Europe after industrial revolution, governments slowly but steadily moved towards compulsory education for children or imposing restrictions on their employment in factories. As feudal system gave way to capitalist order, demand for uniform adult suffrage emerged and, after a lot of dilly-dallying, it was eventually granted. These were termed as industrial reforms by scholars.

In India, we know of several social reforms for curbing many evil practices during medieval period as well as during the British Raj. Several political reforms were also undertaken in India after independence– the biggest being universal uniform adult suffrage. Electoral reforms were given shape. Administrative reforms and governance reforms have also been undertaken.

In much of the current Indian discourse, economic reforms have reference to liberalisation of business, privatisation of public undertakings, and globalisation of the economy which were ushered in 1991. If one carefully analyses the purposes behind the reforms undertaken after independence but before 1991 and those undertaken after 1991, one would discover that earlier set of reforms were generally equity seeking while later set of reforms are efficiency promoting. Proponents of equity seeking reforms argued that better distribution of income and wealth will also improve growth via demand side while opponents thought such moves would compromise growth as these would dent improvement in savings. Majority of analysts in those days were proponents of equity seeking reforms. Another way to differentiate the pre-1991 and post-1991 reforms could be in terms of their scope. The latter were more widespread and coordinated, unlike the attempts, even at promoting market efficiency in the pre-1991 period, such as in 1980s. Pre-1991 reforms attempted to establish a socialistic pattern of society where there was a pervasive regulatory control by the State. The public sector was expected to reach the 'commanding heights' of the economy with clearly demarcated priority sector industries reserved for this sector. Reversal of emphasis on public sector from the commanding heights of the economy since 1991, was said to unleash the market forces. Present genre of reforms has variously been said to be market-oriented, pro-market, market-friendly, pro-business and pro-competition, as tilt towards market was seen to be promoting competition. Some have considered it a State- retreat.

Welfare measures undertaken post-independence were considered liberal as similar measures were undertaken by the Liberal Party in early 20th century when it was in power in Britain. These were in contrast to those pursued by Conservative Party. In addition, there were measures which put restrictions on operation of private enterprises, which were said to be left-of-the centre and progressive (as

opposed to reactionary). Since, in the present dispensation, restrictions were to be liberalised, political thinking classified such reforms as neoliberal rather than liberal as (political) liberalism is altogether different from (economic) liberalisation.

Neoliberalism is said to be a phrase for resurgence of 19th century ideas of laissez faire and free-market capitalism. Liberalism in contrast had several shades but largely came to be associated with progressivism which suggested State to regulate market activities from welfare angles and undertake welfare-oriented policies.

Check Your Progress 1

1) Define economic reforms.

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2) Differentiate between equity-seeking reforms and efficiency-seeking reforms.

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3) Explain the meaning of neo-liberal reforms.

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7.3 INDIA'S PATH TO ECONOMIC TRANSFORMATION

India's journey began as a newly independent poor underdeveloped nation in 1947 – the year of its independence from the British rule. At that time, India was one of the poorest nations in the world in terms of income, wealth and material capacity. The country remained a virtually closed economy for nearly four decades after its independence, following an inward-looking development strategy. The first few plans focused on growth with strengthening of the manufacturing sector emphasizing heavy industries to form the backbone of the economy. Other principal areas of planning were agriculture and social development i.e. housing

and poverty alleviation. Some of the measures that shaped the development process in general and the process of industrialisation, in particular, involved the following:

7.3.1 Planned Economic Development

Post independence, the key goal was to achieve self-reliance in all possible dimensions of economic activities of the nation. Accordingly, a diversified industrial production base was meticulously planned out for India, ranging from simple consumer items to sophisticated capital goods and heavy machinery. Since 1951, India has grown as a planned economy with the inception of First Five Year Plan. India's initial development strategy, aimed at a 'socialistic pattern of development'. There was lack of faith in the market and the role of the State was considered the need of the hour. Trade received very little attention; while the nation's trade policy was characterised by pervasive import and exchange control. The architecture of India's post-colonial development policy framework was inspired by the soviet model of development. Indeed, the foundations of India's 2nd Five Year Plan model (Mahalanobis, 1953) closely resembled Feldman's model developed in the Soviet Union in the 1920s, which argued for a larger share of investment in the capital goods sector that may slow down growth in the short-run but would result in a much higher growth rate in the long run, accompanied with higher levels of consumption. As India was about to launch the Second Five Year Plan, Parliament passed in late 1954, a resolution establishing a socialistic pattern of society in India (which meant no more than seeking to be a welfare state within a capitalist order and a more egalitarian society). The focus thus shifted to industrialisation where a five-fold strategy was invoked: promotion of import-substitution led industrial development, tilt towards heavy industry in the pattern of industrial development, commanding heights of the economy (industrial space) for the public sector, regionally balanced industrial development, and promotion of small scale industries in the sphere left for private sector with a view to improving employment through reservation of items for production. Industrial Policy Resolution of 1948 was revised to strengthen government control in the Industrial Policy Resolution of 1956. Several private enterprises in manufacturing, transport, and services were nationalised in 1950s– and some more after 1955. The purpose was to check concentration of income and wealth and, thus, economic power in a few hands. Freight equalisation policy was implemented right from 1952 up to 1993, whereby transportation cost of industrially 'essential' items such as coal, steel, cement, etc. would be the same irrespective of distance. It is pointed out that eastern and central regions which had natural competitive advantage lost, whereas western, northern and southern regions gained.

7.3.2 Import Substitution in Industrialisation

National Planning Committee (1938) had suggested that India should focus on mother industries so that it is self-reliant. Mother industries are those industries that make other industries run successfully: power industry; industries for production of metals, heavy chemicals, machinery, and tools; and communication industries such as railways, telegraphs, telephones, and radios. Later, atomic energy and space were added. Besides self-reliance, there was a view that India did not have much to offer by way of exports in order to be able to import capital and essential goods for industrialisation.

As there were limited foreign exchange (forex) reserves, in view of low export potential of the economy, quantitative restrictions in terms of import license were imposed, in addition to high tariffs on intermediate and consumer goods, moderate tariffs on capital goods, and ban on import of some items. The control was further tightened in view of foreign exchange crisis during 1957-58 when the first loan had to be negotiated with the IMF. A market developed for use of these licenses and rent-seeking became rampart. Only in mid-1980s, some relaxations were afforded.

7.3.3 License Permit Quota Raj

The Industries (Development and Regulation) Act of 1951 made it compulsory for all new undertakings to seek license and for all existing undertakings to get registered. It was amended in 1953, requiring an undertaking to seek permission to produce new articles, to carry out substantial expansion, and to shift to a new location. And the applications were to be examined for half a dozen factors by the License Committee set up by the Act of 1951. Licensing was itself a cumbersome process: application to be cleared by Directorate General of Technical Development, then forwarded to the License Committee which would issue a letter of intent, based on which applicant could move to seek permission to import goods, enter into foreign collaboration, acquire land, issue new capital beyond a small limit or seek loan from a financial institution. Thus, barriers to entry were high.

This was all done with a view to prevent concentration of economic power, to ensure balanced regional development, and to encourage small scale industry (which were exempt from seeking license) and labour-intensive technology– though reservation of items for exclusive production started only in 1967 with 47 items and the list expanded periodically till 1989.

However, when an assessment of working of licensing system was made, it came to the fore that it did not serve the objective of the Industrial Policy Resolution 1956 as economic-power and regional concentration both increased. Industrial houses were able to manipulate the system and licensing authorities were willing to be manipulated for a consideration. Public sector financial institutions also favoured large industrial houses. The lesson learnt was not the recognition of government failure, but a thinking that led to further tightening of regulation for industries to make them fall in line. So, Monopolies and Restrictive Trade Practices Act was brought in 1970 providing for a Commission, which was set up to pursue the said objectives.

7.3.4 Public Sector Expansion and Nationalisation

Before Independence, there were some departmentally run commercial ventures such as postal service – including telegraph and telephone service, and railways (largely nationalised by 1944), besides captive ventures of 18 ordnance factories and central public works department. Provinces also had irrigation departments and captive public works departments. However, immediately after Independence, some public sector undertakings with ownership of the Government were started and by the time Planning Commission was established their number was five. These include Indian Telephone Industries, Damodar Valley Corporation, National News Print Limited, Oriental Insurance Limited, and Indian Rare Earths Limited.

A new industrial policy resolution was passed in 1956 in the Parliament, following the resolution on socialistic pattern of society. This policy resolution expanded the sphere of public sector and contracted that of private sector. With a view to creating and expanding infrastructure, generating financial resources, redistributing income and wealth, balancing regional development, and substituting imports by domestic production, quite a few industries were nationalised for one or the other reason– some for strategic importance of the industry, some in the interest of working class when industries were found falling sick, and some to safe keep technology.

Government of India and state governments went on creating and expanding public sector undertakings. By 1990, the number had reached 230 under Government of India. Majority of these are under the aegis of Department of Public Enterprises but there are about two dozen other departments which had at least one public sector enterprise– as statutory corporation or government company.

Reserve Bank of India, after its nationalisation in 1949, was entrusted with regulation of banks through Banking Regulation Act of 1949.Imperial Bank was nationalised as State Bank of India in 1955. Life Insurance of India was created in 1956 by merging more than 200 insurance and provident fund companies— including 16 foreign insurers. Most people recall nationalisation of 14 major banks in 1969, of 6 major banks in 1980, and of 107 general insurance companies (55 into companies and 52 insurance arms of companies) into General Insurance Corporation of India in 1972 with four subsidiaries for operations.

With independence, Government had asserted that it could nationalise any private or foreign venture. Starting with Air Corporation Act in 1953, Air India (an initiative of TATA) was nationalised and half a dozen regional airlines were merged and nationalised as Indian Airlines. One by one, electricity, steel, iron, coal, and oil industries were nationalised.

7.3.5 Beginning of Economic Reforms

However, after nationalisation of 6 major banks in 1980 (following the nationalisation of 14 banks in 1969), thinking started changing as it was felt that not only the goal of equity was not being satisfactorily realised but that of growth (efficiency) was also getting compromised. As a result of the oil price shock in 1979, there was pressure on forex reserve, the IMF was approached for a loan of SDR 5.0 billion to be availed over four years 1981-1984 under Extended Fund Facility with relatively lower rate of interest but it attracted conditionalities in terms of liberalisation of imports–particularly to exporters, adjusting public expenditure, tilting policies towards supporting private sector, etc. These conditionalities were substantially complied with but there was a lot of domestic criticism. As BoP situation improved, Government of India did not avail the last installment of SDR 1.1 billion. Meanwhile, it may be noted that China, post-Mao, had started moving towards market-oriented reforms around this time, or few years earlier.

With Rajiv Gandhi in power in 1984, and a new generation of ideas, easing of State control on industries in terms of expansion, import requirement, lowering of taxes, were also attempted. Capacities created beyond authorised levels were regularised with some limits. Under 'broad-banding' diversification into related

product did not now require a new license. Cement, steel, and fertilizers industries were decontrolled. Licensing for companies with investment below a certain level, willing to locate away from urban centres was not necessary. Definition of MRTP firms was relaxed. Imports for modernisation were liberalised. List of open general license (OGL) for import of capital and intermediate items was expanded, which permitted imports without tariff. Diversification was made liberal. Security and Exchange Board of India (SEBI) was constituted in 1988 by an executive order, to oversee the security market as price rigging was rampant. Communication infrastructure was laid out. Political reservations on Planning Commission came to the fore: Rajiv Gandhi called it a pack of jokers. These steps had to be halted as political support was lacking and bureaucracy was recalcitrant. These steps were held as hesitant reforms. It was also the time, the USSR adopted glasnost and perestroika and by the end of 1989, expediting the breakdown of the iron-curtain that divided the West from the Soviet East

Noticing that growth rate had considerably slowed down in 1970s for several reasons not the least of which was the bureaucratic over-zealousness in keeping control over everything, certain measures were taken in mid-1980s to relax the controls, particularly on imports. Such measures helped improve the growth performance of the economy, however macroeconomic imbalances also gained current.

While growth rate had improved in 1980s– thanks to relaxations on restrictions, deficit financing on government side, and liberal imports and unrestrained commercial borrowing generally made two macroeconomic parameters of fiscal deficit and current account deficit, unsustainable.

Check Your Progress 2

1) State reasons for adoption of import substitution in industrialisation of the country.

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2) Explain the meaning of license, permit and quota (LPQ) raj.

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3) State two major international developments that help change the development thinking.

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7.4 ONSET OF CURRENT ECONOMIC REFORMS

7.4.1 The Crisis

Fiscal profligacy of 1980s resulted in high fiscal deficit, public debt and external debt, thus creating internal and external imbalances. By 1990-91, gross combined (Union and State) fiscal deficit had crossed 10 per cent of GDP, combined public debt to 70 per cent of GDP, and external national debt ($83 billion) to 30 per cent of GDP– partly because of gradual withdrawal of foreign concessional aid. Debt service burden of the Union Government was more than 35 per cent of its revenue receipts. But more than that, forex reserves were so low as to account for only 7.0 per cent of total debt. Short-term debt to forex reserves was 145 per cent, making its debt-service ratio 35 per cent of exports. Current account deficit in the Balance of Payments crossed 3.0 per cent of GDP, largely on account of a gradual liberalisation of imports without the commensurate improvement in exports. Inflation also accelerated to double digit level despite three consecutive good monsoons and harvest.

Changes in the international context associated with the gulf war, triggered by Iraq attacking Kuwait in mid-1990, put India into a serious crisis as its import bill swelled and export receipts plummeted, and, thus, current account deficit on balance of payment accentuated. In this scenario, NRIs started withdrawing their deposits in foreign currency from banks. Short-term foreign capital also out-flowed. As a consequence, forex reserves depleted down to $1.2 billion in January 1991 and further depleted to $0.6 billion by June 1991– just equivalent to about three-weeks' imports. There was thus a full-blown BoP crisis at hand.

India sought help from the International Monetary Fund (IMF) to tide over BoP crisis by seeking an emergency loan of $2.2 billion. IMF gave a standby loan of $0.72 billion in January 1991 to be utilised in three months' time. For the first time, the country came to the brink of default in servicing the debt. India had to airlift some part of its gold stock (primarily the gold confiscated from smugglers) out of its forex reserves to Bank of England and Union Bank of Switzerland as collateral to secure loan on terms that were not too steep. This was the time when India had a caretaker government headed by PM Chandrashekhar (March-June 1991) at the Centre. With its back against the wall, the country had no option but to set into motion comprehensive economic reforms. It is often said that the crisis of 1991 was predictable, given the buildup of macroeconomic imbalances in 1980s, but the Gulf war precipitated it.

The loan contracted was too little. It was natural for the new Government which came into power with PV Narasimha Rao as Prime Minister and Manmohan Singh as Finance Minister to approach for a loan of $2.5 billion dollars from IMF and another of $0.5 billion from the World Bank. IMF and the World Bank were willing to rescue the Indian economy but sought compliance with conditionalities, as is their wont, in terms of implementing reforms package involving macroeconomic stabilisation policies and microeconomic (sectoral) structural corrections. IMF gave loan of SDR1.656 billion (equivalent to $2.2 billion) under non-concessional stand-by arrangement with a window of 15 months at 7.1 per cent rate of interest. World Bank which normally gives project specific loans, did come around to giving a loan of 0.25 billion for structural adjustment. Though these loans were not concessional, yet they were cheaper

than commercial ones– which were not available easily as the country's credit rating had dropped considerably.

Manmohan Singh and P.V. Narasimha Rao initiated the reforms in June 1991 with the presentation of the Union Budget. They found the conditionalities attached to the loans taken from international financial institutions as prudent pieces of advice but set up committees to suggest details for the path to reform the economic management of the country. These were efficiency seeking reforms. If there had to be a check on merger or acquisition of private firms, it was not to check monopoly or restrictive trade practices but to promote economic efficiency. If a public sector unit had to be sold (privatisation) or partly sold (divested), it was for improving its economic performance. The sole purpose was to improve efficiency in the economic system.

7.4.2 Assessment and the Response

Following two paragraphs of the budget speech of Manmohan Singh on 24 July 1991, sum up the direction that was to be taken over the subsequent three decades:

"In the macro-management of the economy, over the medium-term, it should be our objective to progressively reduce the fiscal deficit of the Central Government, to move towards a significant reduction of the revenue deficit, and to reduce the current account deficit in the balance of payments. It is only such prudent management that would enable us to curb the exponential growth in internal and external debt and limit the burden on debt servicing, for the Government and the country, to manageable levels. Indeed, we must make a conscious effort to reduce the internal debt of the Government and the external debt of the nation, so that we rely more and more on our own resources to finance the process of development."

"Macro-economic stabilisation and fiscal adjustment alone cannot suffice. They must be supported by essential reforms in economic policy and economic management, as an integral part of the adjustment process, reforms which would help to eliminate waste and inefficiency and impart a new element of dynamism to growth processes in our economy. The thrust of the reform process would be to increase the efficiency and international competitiveness of industrial production, to utilise for this purpose foreign investment and foreign technology to a much greater degree than we have done in the past, to increase the productivity of investment, to ensure that India's financial sector is rapidly modernised, and to improve the performance of the public sector, so that the key sectors of our economy are enabled to attain an adequate technological and competitive edge in a fast-changing global economy. I am confident that, after a successful implementation of stabilisation measures and the essential structural and policy reforms, our economy would return to a path of a high sustained growth with reasonable price stability and greater social equity."

7.4.3 Some Initial Steps Taken by the Government

Immediate response of the Central Government, within 10 days in power, was in terms of devaluation of rupee. The custodian of the value of rupee RBI devalued rupee, in quick succession on 1 July and 3 July 1991, by 9 per cent and 11 per cent against currencies of major trading partners, viz., US Dollar, British Pound, German Deutsch, and Japanese Yen (Chinese Yuan was not that important at that

stage). This was expected to make exports competitive. Commerce Ministry withdrew export subsidy and thus saved some public expenditure, as well as moved towards removing distortion in market prices. After an experiment with dual exchange rate for a year, external value of rupee was allowed to be determined by the market forces. In other words, rupee moved from fixed exchange regime to floating exchange rate. This was most important macroeconomic stabilisation measure on external front.

In the financial sector, RBI had freed banks to charge interest rates beyond floor rate, depending upon the risk perception of the borrower. Budget speech of 1991 suggested formation of a high-level committee (Narasimham Committee) to look into the structure, organisation, functions and procedures of financial institutions. It was felt that administrative intervention on interest rate had outlived its utility. It was pointed out that powers of Capital Controller of India (Government) would be transferred to SEBI which would be empowered through appropriate legislation. Likewise, Foreign Exchange Regulation Act (FERA, 1973) was set to be liberalised for non-resident Indians to make investment in India.

Recognising that entry barriers were promoted by proliferation of licensing regime and that it actually led to increase in the degree of market concentration, Finance Minister announced the new Industrial Policy as a part of his Budget Speech on 24 July 1991 (and second part on small scale industries on 6 August, 1991)). These committed the Government to take a series of initiatives in the five areas of (a) Industrial Licensing, (b) Foreign Investment, (c) Foreign Technology Agreements, (d) Public Sector Policy, and (e) MRTP Act. Highlighting that many small and medium sized entrepreneurs were hampered by the restrictive licensing regime, it was abolished, except for a set of industries in the categories of security and strategic importance, hazardous chemicals, overriding environmental reasons and items of elitist consumption. They were further liberalised. Items reserved for small scale industries were left untouched in 1991 but gradually done away with. List of industries reserved for public sector was pruned from 17 (in 1956) to 8.

While freeing Indian industry from official control, it said, opportunities for foreign investment should be exploited as it would bring in attendant advantages of technology transfer, management techniques, marketing strategies and export potential. Direct approval would be given up to 51 per cent. Likewise, Indian industries would be allowed to negotiate the terms of technology with foreign counterparts and this may induce Indian industry to undertake more research and development activities.

Public sector units which have done very valuable work in early years of the Indian economy, post-independence were now, in many cases, a burden on the public resources. In particular, the sick mills which were taken over by the Government continued to be sick. They were to be referred to the Board for Industrial and Financial Reconstruction. While there was no reason for public sector to supply consumer goods and services, it had expanded into these sectors. Emphasis was for the public sector to operate in reserved or strategic areas or where reasonable profitability was being maintained. Those public undertakings that were performing well were to be given management autonomy. Competition with private sector was to be encouraged. And in some cases, disinvestment of equity share was to be carried out.

MRTP Act was to be so tweaked that industries need not seek any prior approval for expansion, merger, takeover, amalgamation, or diversification. MRTP Commission could, suo moto or on complaint, check if any industrial establishment was indulging in monopolistic, restrictive, or unfair trade practices and take appropriate action.

Check Your Progress 3

1) What triggered the BoP crisis in 1991?

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2) Why did the Government negotiate non-concessional loans with IMF and World Bank?

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3) What were some immediate steps taken by the Government to address the BoP crisis?

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7.5 REFORMS FOR MACROECONOMIC STABILISATION

It can broadly be said that the World Bank as a development bank lends over a long-term horizon which generally helps a country with finances to carry out its long-term projects, while International Monetary Fund help a country to tide over short-term Balance of Payments difficulties. Both generally provide finance in terms of certain foreign currencies constituting Special Drawing Rights (SDR)presently – U.S. dollar, Euro, Chinese yuan, Japanese yen, and Pound sterling. Both help a country in terms of desired foreign currency assets, which can be used for meeting international liquidity obligations. As lenders, both the institutions have been found to impose certain conditions – often referred to as conditionalities if the borrowing country is not able to procure credit from

commercial channels on affordable terms. World Bank insists on reforms in specific sectors– often called structural adjustments, and IMF insists on reforms in macroeconomic policies – fiscal, monetary and exchange rate policies. But both consult each other on each negotiation as IMF has started giving loans for medium terms which goes beyond original mandate of tiding over BoP difficulties.

7.5.1 Fiscal Reforms

An important macroeconomic parameter of focus under the stabilisation framework is fiscal deficit. In a world where fiscal deficit is considered inevitable or unavoidable for spurring growth, containing unemployment, and carrying out welfare measures (not, necessarily reducing inequality), containment of fiscal deficit to a reasonable level is considered a desirable first step in stabilsing an economy. Beyond that desired level of fiscal deficit, not only is the value of domestic currency threatened and can get eroded internally but it can lose value externally as well. This desired level of fiscal deficit would vary from country to country and is usually contested by academicians and scholars, but policy-makers may agree that a for a developing country like India it could be around 3 per cent of GDP.

This fiscal balance has to be ensured by managing efficiently both revenue side – basically taxation and expenditure side so that borrowing is not too high and that debt servicing does not dominate revenue expenditure through rising interest payment. Keeping this in mind, tax rates which went on increasing during 1950-70, were moderated substantially – guided by the thinking underpinning the Laffer's curve hypothesis. Tax nets were widened while exemptions and deductions were pruned; tax structure was reoriented in favour of direct taxes as indirect taxes are seen to be price distortionary and regressive in nature; attempt was made to change the basis of indirect taxes from gross sales proceeds to value added; customs duties had to be brought down in keeping with the new economic thinking as well as in compliance to WTO rules; attempts were made to realise higher profits and dividends from public sector enterprises; efforts were also made to recover cost from sale of services provided by government (whether transport, power or irrigation); and improved fees were realised for use/allocation of natural resources through better price discovery mechanism (whether oil, gas, coal, minerals, or spectrum). There were political impediments and success was limited as some of these steps were also undermined by scams.

Attempts were made to streamline public expenditure by abolishing/and improved targeting of subsidies; downsising/rightsising staff, abolishing administered price mechanism in some sectors like oil and gas; lowering interest payment by improving management of public borrowings; and moderninsing and rationalising defencespending.

Despite a slew of reforms, the two sides of the budget could not match well, necessitating heavy borrowing and at times borrowing to service past borrowing.It was finally considered prudent to bind the government by Fiscal Responsibility and Budget Management (FRBM) Act, which could be passed in 2003. The Act has put limits to fiscal deficit, revenue deficit, level of debt and contingency liabilities and stipulated annual reduction in each of them. Though the Act had provided an escape route to deal with situation that arose during 2008, yet the Act itself had to be amended in 2012 and 2015. Timelines for meeting the FRBM targets had to postponed repeatedly.

7.5.2 Monetary and Financial Reforms

Fiscal policy relates to the Government and has to be formulated to provide finances to the Government and implemented under the guidance of the Ministry of Finance, by different administrative agencies. Monetary policy and financial policy are formulated and implemented largely by the country's Central Bank which is the Reserve Bank of India (RBI) in the case of India. Fiscal and the monetary policy are financially linked through Government's debt instruments. The Indian financial system of the pre-reform period essentially catered to the needs of planned development in a mixed-economy framework where the Government sector had a predominant role in the economic activity. It was felt that there had been too much direction and regulation from government on financial sector operations, in terms of investment, credit allocation, branch expansion, and even internal autonomy of financial institutions. As a result, Public Sector Banks and other financial institutions failed to use their commercial judgement in ensuring efficiency in their operations with respect to rate of return, profitability, maintaining capital adequacy, minimising non-performing assets, or providing satisfactory customer service. They turned to become 'service' organisations whose financial problems would inevitably be taken care of by the Government. This had to change.

Traditional monetary and financial instruments were largely inflexible– not reflecting demand and supply forces of the market, and there was urgent need for reforms. India embarked on a substantial liberalisation in the early nineties. Two official reports, viz., the Report of the Committee on Financial System (Reserve Bank of India, 1991) and the Report of the Committee on Banking Sector Reforms (Government of India, 1998),both chaired by M Narasimham established the foundation of the financial sector reforms post 1991. The Narasimham Committee1991, devoted to enhancing operational freedom in the commercial banking sector, recommended measures like reduction of pre-emption of banks' investible resources [via a reduction of cash reserve ratio (CRR) and statutory liquidity ratio (SLR)[1]] and gradual elimination of the administered interest rate structure. Narasimham Committee 1998 recommended further measures for modernising the banking sector through better regulation and supervision, and introduction of prudential norms. It also suggested a review of the bank ownership structure in India.

Other elements of financial sector reforms in India include significant reduction of fiscal dominance of monetary policy[2] (including removal of automatic monetisation of fiscal deficit); dismantling of the complex administered interest rate structure to enable the process of price discovery; providing operational and functional autonomy to public sector institutions; preparing the financial system for increasing international competition; opening the external sector in a calibrated

[1]gradual reduction of CRR from 15% to about 4%, and reduction in the SLR from nearly 40% to 21.5% between the early 1990s and the mid-2010s have made a huge improvement to the availability of lendable resources to the banking sector.

[2]Fiscal dominance of monetary policy has moderated in India as a result of a series of fiscal and monetary policy reforms that include, (i) moving to a market-determined interest rate system by introducing auctions of government debt, (ii) phasing out of the automatic monetisation of fiscal deficits through the two Supplemental Agreements between the Government of India and the Reserve Bank of India, and (iii) curbing the monetisation of debt by enacting the Fiscal Responsibility and Budget Management (FRBM) Act, 2003 that prevented the Reserve Bank from subscribing to primary issuances of government securities from April 1, 2006.

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manner; and promoting financial stability in the wake of domestic and external shocks. More recently a number of measures have been initiated towards inculcating a credit culture through enforcement of creditors' rights, and hastening the process of credit recovery. All these measures were designed to create an efficient, productive and profitable financial sector.

Information technology has played a key role in this transformative journey of Indian banking. Technology has enabled more effective, lower cost and real-time delivery of financial services, through the establishment of a modern payments system. Also, Information Technology has allowed development of several instruments of liquidity and finance. Following global trends, many development finance institutions also assumed the role of, or converted into, commercial banks and some commercial banks were allowed into insurance and mutual funds business. In the recent years, quite a few non-banking financial institutions – investment companies, loan companies, housing finance companies, infrastructure companies – have emerged and are doing well and some development financial institutions such as NABARD, SIBDI, EXIM, and NHB are also performing well. While banks and non-banking financial institutions are regulated by RBI, quite a few regulatory bodies have been instituted to look after insurance business, pension funds, etc. Securities and Exchange Board of India (SEBI) which regulates capital market/stock exchanges has been strengthen and the Forward Markets Commission (FMC) which looks after commodity futures has also been reformed.

7.5.3 Currency Exchange Reforms

Under import substitution strategy and paucity of earnings through exports, allocation of foreign exchange by RBI was severely restricted through complex import licensing system. Rupee remained linked to sterling pound for along time till 1975 when it was pegged with a basket of currencies involving India's important trade partners. This remained in effect till 1993. In July 1991, in quick succession through two devaluations, value of rupee was brought down by around 20 per cent. This was a part of understanding arrived at with the IMF for securing standby loan. Since 1993, rupee is on floating exchange rate and its external value (with respect to each currency) is determined by market forces though RBI does intervene in foreign exchange market if it finds that there is excessive volatility by buying or selling foreign currencies in spot as well as in futures market. Thus, ours is a managed float system or managed flexible regime as are most of other countries.

As India wanted to attract Foreign Direct Investment, it liberalised conversion of rupee into foreign currencies but only on the current account. Once, India built sufficient forex reserves in terms of foreign currency assets, it gradually permitted its resident companies to convert rupee into foreign currencies to facilitate overseas investment. This is in effect conversion of rupee on capital account. Restriction on capital account convertibility however continue, we have some distance to travel before full capital account converitabilty. This is perhaps a lesson drawn from South-East Asian crisis in the late 1990s.

Check Your Progress 4

1) Why was Fiscal Responsibility and Budget Management Act legislated?

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2) Explain the role of Cash Reserve Ratio and Statutory Liquidity Ratio.

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3) State the status of convertibility of rupee.

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7.6 REFORMS FOR MICROECONOMIC STRUCTURAL ADJUSTMENT

We all often hear that Economic Reforms mean liberalisation, privatisation, and globalisation (LPG), which have replaced license, permit, and quota (LPQ) as the latter had run out their course and had become stale, corrupt, and counter-productive creating a high cost economy. This section intends to explain the meaning of LPG and some steps that were taken up in India.

7.6.1 Liberalisation of Business

If restrictions are imposed by the Government on private economic activities, the policy regime may be termed as a regulated and controlled business regime. By contrast, if no restrictions are imposed, the policy regime may duly be called one of *laissez faire* (a French phrase for let do or let go) – a euphemism for free market. However, in a society with State, economy cannot be completely free of restrictions (or incentives). When some of existing restrictions are removed or relaxed, it can be said that economic activity is being liberalised: it is about removing the burden of restrictions. In case restrictions are further tightened, policy can be said to be restraining or constraining one. It is quite possible that in some spheres, in any given period, policies are made more restrictive and other areas, more liberal.

In industrial sector, India had managed to create considerable barriers to entry and expansion: license for entry, license for expansion, license for diversification, license for imports of capital goods and intermediate goods, permission for amalgamation, control on issue of shares and debentures, restrictions on prices – of goods, services and factors, compulsory procurement of a portion of output by government, check on foreign investment, restrictions on foreign collaboration for technology and even on location of industry. These were once the order of the day in the pre-reform era of the 1970s and 1980s. There were certain restrictions on factor markets – particularly, labour – for wages and social security. These were said to be choking the initiative and enterprise of the people. However, it was pointed out that big industrialists could still circumvent almost all the restrictions with connivance or cooperation of rent-seeking bureaucracy for graft. Those who could manipulate the system, developed vested interest in its continuation; they could reap monopoly profits as the competition they faced was very low or even non-existent. The end result was corruption and delays in execution of projects. General assessment was that this hampered growth (efficiency) without promoting social justice (equity).

Government of India, with Prime Minister Narasimha Rao and Finance Minister Manmohan Singh, in July-August 1991 and in April 1993, spearheaded many liberal provisions or undertook promotional measures in the areas of (a) licensing business, (b) foreign investment, (c) foreign technology agreements, (d) establishment, merger, amalgamation, takeover of companies or appointment of directors in corporate governance, and (e) exiting from business. Licensing was made mandatory only for 18 categories– later reduced to 15 by delisting refrigerators, air-conditioners, and washing machines. Procedures for foreign investment and foreign technology collaboration were sought to be promoted. Labour laws were made a little easier for businessman.

One wonders whether the move was to de-bureaucratise the processes or promote marketisation. It was perhaps both.

7.6.2 Privatisation of Public Sector Units and Disinvestment

By 1990, the world had changed; its zeitgeist had changed. The new mantra was 'government's business is not to do business' or 'government has no business to do business'. This was in tune with the trend towards privatisation of public assests. There was a time in 1940s when nationalisation was seen as way forwarded in the capitalist world, particularly in the UK, even in the wake of the World War II and then there came a time in 1980s when privatisation became the mantra for reforming economic management.

It was felt during 1980s in India that government was unnecessarily directly operating industries in many areas where it ought not to and that many of public sector units were not performing up to the mark by parameters set for them. In the former case, Government could simply withdraw by selling its stakes. This is called disinvestment. In the latter case, undertakings were to be so reformed that they perform well even if meant partnership with private sector in terms of ownership and/or management. But the issue soon became who would buy a loss-making unit? Buyers insisted that they would cut down staff which was oversized or non-performing. Short of funds, Government decided to sell shares of performing undertakings. Moreover, shares of such companies could be sold at high premium. In certain cases, one Government company bought the shares

of another Government company and, thus, Government could get non-debt creating capital receipts.

Various models were tried for privatisation. There could be three simple models: (i) ownership, (ii) organisational, and (iii) operational. Disinvestment or divestment is related to ownership question. Sometimes, it is suggested that Indian Railways may be corporatised. Here ownership does not change but organi–ational structure changes; it is no more run by the department or a board under it. Corporation works at arm's length distance. Unit can be leased to private hands for long period.

Disinvestment of ownership, if made for 50 per cent or more along with handing over control and management is called strategic disinvestment. If dilution is for less than 50 per cent, which it has to be in case of undertakings in (strategic) areas reserved for public sector, it is called non-strategic. Government sold some of its hotels and some of the companies like BALCO completely. Government keeps selling part of its shares through several methods. To begin with it sold shares to other public sector financial companies like LIC and GIC. There have been around 200 successful attempts.

There is another experiment called public-private partnership which was attempted particularly in building up the momentum on development of infrastructure projects.

7.6.3 Globalisation of the Economy

The term globalisation has several meanings, varying from exposure to competition with the world leaders in a particular product market to free trade in goods, services and factors. Globalisation of an economy with world economy could be thought in terms of economic relations but they ought to be in terms of interface of markets rather than between governments and in terms of bilateral (or multilateral) flows rather than unilateral flows like aid. But if Government of one country bans imports, puts quota restrictions or creates a high tariff wall by imposing 300 per cent duty, how could producers in a country sell even if there were buyers in another country. There could be rationale behind such restrictions: protection of domestic industry from competition, insufficiency of forex availability due to weak export earnings, etc. However, it is argued that such measures protects inefficiencies of domestic producers and harms the consumers. Removal of such restrictions could induce domestic producers to be either competitive or switch to other products. In other words, open the economy for trade and investment creating the scope for consumers to benefit with better quality and invariably cheaper products.

We know that multinational and transnational corporations have plants in several countries. They produce goods and services in the host countries and sell in the domestic markets of the host country, instead of exporting from home country, as it saves them transportation cost. This requires movement of capital across borders. Thus, globalisation of an economy would mean:

a) Reduction in tariff barriers with a view to allowing freer flow of goods to and from the country;

b) Freer flow of foreign capital in terms of investment – both direct and portfolio – by ensuring conducive atmosphere and easy approval of projects;

c) Freer flow of technology through purchase or lease of IPRs; and

d) Freer movement of labour and manpower.

When India started liberalising its economy, WTO was under negotiation in Uruguay Round. It became operational in 1995 and sought freer trade through unrestricted competition by removal of non-tariff barriers and substantial reduction in tariff barriers as also removal or reduction of subsidies. WTO extended the areas traditionally covered by GATT (General Agreement on Trade and Tariff) by including GATS (General Agreement on Services) and TRIPS (Trade Related Intellectual Property Rights), and TRIMS (Trade Related Investment Measures). Thus, goods, services, technology, and capital were covered in some way.

Since Doha Round of WTO could not be satisfactorily concluded, countries have simultaneously gone for forming Free Trade Areas, Comprehensive Economic Cooperation/Partnership, Customs Union, etc. European Union is the chief example, though not related with failure of WTO. India has negotiated quite a few, in fact more than two dozen, regional or bilateral partnerships.

Check Your Progress 5

1) Distinguish liberalisation from laissez faire.

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2) Explain the meaning of disinvestment in a public sector enterprise.

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3) Delineate the elements of globalisation of an economy.

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7.7 GENERATIONS AND WAVES OF ECONOMIC REFORMS

Reforms are often said to be a continuing process but scholars and policymakers have a tendency to categorise reforms into certain categories– calling them as

levels, generations, waves, or, following digital style, versions. It is also suggested that while neoliberal reforms have a universal constitution, different nations may have different pace and sequence. IMF scholars suggest that they may not exactly fall in neat time sequence. They also suggest that reforms may be guided by two perspectives: (i) global and (ii) national. We shall adhere to national perspective.

While following neoliberal direction, different nations will have some uniqueness of their own in terms of pace and sequencing as their economic conditions differ. Politics and bureaucracy will determine the pace and sequencing. For example, such reforms were halted when India had unstable governments with limited terms in the late 1980s and the late 1990s. Reforms may have suffered, rather reversed, during the East Asian Currency Crisis or the Great Recession of 2008-09 and there was call for more open global financial architecture.

At the end of last century, it was assessed that reforms that were easy to implement in terms of resistance of bureaucracy or politicians, were carried out in the initial phase. First, they were to be carried out in terms of conditionalities imposed by loan sought from IMF and WB. Second, they could be carried out by executive actions, not seeking political support, as recommended by the committees set up for the purposes. Devaluation of rupee, ease of restrictions for establishing an enterprise and expansion of capacity, easing import restrictions, de-reservation of items for small scale industries, diluting government shares in public sector undertakings, etc. did not require legislative interventions. They have been called first generation reforms and the period was identified as 1991-1999. In terms of digital jargon, they have been termed as Reforms 1.0 under Prime Minister PV Narasimha Rao and Finance Minister Manmohan Singh during 1991-96. Some reforms in the subsequent period were in the nature of deepening of measures previously taken so that reversing them was not easy anymore.

In order to appreciate the distinction between generations of reforms, one should remember the difference between an Act and the Rules under it. Practically, every Act passed by a Legislature has a clause “Power to Make Rules” by the Executive. Rules generally describe the procedure, forms, schedule, direction, fees, fines, etc. but can include regulations, orders, bylaws, etc. Executive makes them and is obliged to submit to the Legislature for scrutiny within a limited period, which in practice is scant. Changing rules is far easier than changing Act. Second generation reforms are said to be those that require legislative sanctions through enactment or amendment. There are others who think that the second generation reforms refer to consolidation of first generation reforms plus reforms related to legal, regulatory, and political institutions. During 1999-2004, for example, many Acts were passed under NDA government, which had bearing on Economic Reforms. Some of them are: Repeal of Urban Land Ceiling Act, Prevention of Money Laundering Act, Fiscal responsibility and Budget Management Act, Central Vigilance Commission Act, and Competition Act. In compliance, several regulatory authorities were instituted. Subsequently, many Reform Acts were passed by UPA government: Factory Regulation Act, Limited Liability Partnership Act, Replacement of Companies Act of 1956 by Companies Act of 2013, etc. It does not mean that no legislative attempts were made in 1991-96. For example, SEBI was given statutory status in 1992.

Some scholars and policymakers, deliberating on 25 years of Economic Reforms in 2016, recommended an agenda for Economic Reforms 2.0. Others have referred

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to this agenda forpost-2014 reforms as Reforms 3.0 or even Third Wave of Reforms. What does it mean? Some say it is about reforms in governance, including judiciary. Some say it is formalisation of the economy, which means, thanks to ILO, formalisation of informal enterprises and informal jobs. Others have included in this agenda steps for extension of taxation nets/base, digital modes of payments, etc. Still others like to include the formalisation of shadow economy.

Many reforms were carried out since 2014, Goods and Service Tax being the major one. Monetary Policy Committee was instituting by amending RBI Act in Finance Act of 2016 and is a major step in monetary management where three members are nominated by Government of India.

Though there is no agreement on clearly marking of generations of neoliberal reforms yet there is some convergence. Some would include social security measures and some would include the local government reforms, which have little to do with neoliberal strand. Analytical clarity is lacking in the area. Yet, roughly speaking, first, second and third generation reforms can be associated with executive, legislative, and governance actions.

Check Your Progress 6

1) Distinguish between first generation reforms and second generation reforms.

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2) Explain the meaning of formalisation of economy.

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7.8 LET US SUM UP

Indian economy is said to have embarked upon reforms in 1991 though it is acknowledged that a few steps towards present genre of reforms were taken in 1980s– in the wake of conditionalities agreed for a whopping SDR 5.0 billion of loan from IMF in the first half of 1980s. It must be noted that economic reforms carried out in 1950s were quite different in content, orientation and objectives than those which had to be carried out since 1991. There are several ways of distinguishing them. In this unit, they have been distinguished as equity-seeking reforms and efficiency-seeking reforms. Reforms in the post-1991 context are recognised as neoliberal in political terms and market-oriented in economic terms.

A background of policies pursued during 1950-80 is discussed in a way that they present a contrast to the direction taken up thereafter. Our colonial past, huge economic disparities, ideological thinking of the times, nationalisation of industries in the West and success of development planning in the USSR had largely guided our course of economic policy in those days.

Despite improvement in growth performance in the decade of 1980s, the macroeconomic fundamentals were mismanaged and Gulf War of 1990 precipitated the economic crisis at home. By now, mandate of IMF had changed in view of breaking-up of Bretton Woods system of fixed exchange rate and it was seeking more fundamental reforms than just devaluation of currency to correct persistent BoP deficit. IMF-World Bank combine was clear about the direction of change in domestic policies. The domestic economic thinking was also slowly converging towards the same.

Some immediate steps were taken like devaluation of rupee much before IMF loan was agreed upon or enunciation of new industrial policy. Some Committees were immediately set up to suggest course of reforms to be taken up in due course. But Indian economy chose its own pace and sequencing, being careful that reforms have 'human face'.

Trends in macroeconomic stabilisation policies are illustrated under captions of fiscal reforms, monetary and financial reforms, and currency exchange reforms while those of microeconomic structural adjustments are discussed under liberalisation of business, privatisation of public sector units and disinvestment, and globalisation of the economy.

A categorisation of reforms in terms of their content and objectives has been provided in terms of identifying different generations or waves of neoliberal economic reforms.

7.9 TERM- END EXERCISE

1) Discuss the nature and features of neoliberal reforms.
2) Differentiate between intervention of restriction and that of liberalisation.
3) What do you mean by disinvestment? Why should ownership of a public sector undertaking be diversified?
4) Delineate characteristics of macroeconomic stabilisation reforms.
5) Approach to define formalisation of an economy.

7.10 KEY WORDS

Disinvestment : Selling government equity in a public enterprise to a private or public enterprise whereby sale proceeds are appropriated by the Government as non-debt creating capital receipt.

Economic Reforms : Correcting mismatch between instruments of intervention and objectives in economic affairs of a country by the government.

Financial Reforms	:	Improving the nature of interventions in financial markets comprising banks and non-bank financial institutions as well as stock market so as to meet the desired level and composition of savings and investment. It may involve regulatory framework.
Fiscal Reforms	:	Correcting interventions in tax- and non-tax instruments, expenditure pattern, and debt mix in a way that they meet the fiscal objectives of the government.
Globalisation	:	Opening economy for trade and investment by relaxing restrictions of movement of goods, services, capital and intellectual property.
Liberalisation	:	Relaxing the restrictions imposed on carrying out business operations.
Nationalisation	:	Acquisition of a private enterprise, in part or full, by a government.
Privatisation	:	Sharing ownership (or management) of an existing public sector enterprise with private parties or completely selling public assests.
Stabilisation Programmes	:	Interventions that improve stabilisation parameters of fiscal balance, balance of payment, price inflation, and unemployment.
Structural Adjustment Programmes	:	Interventions that lead to reduce market distortions—basically, price distortions.

7.11 REFERENCES

There are several sources related to this topic– some explaining, some supporting, some opposing, and some critiquing economic reforms in general or particular reforms or in relation to Indian economy. Any good book on Indian economy would provide the facts. The World Bank and IMF websites would also be good sources to help one understand the direction of reforms that have been suggested, if not imposed, by the duo. Yet, one would greatly benefit from

1) Bhaduri, Amit and Deepak Nayyar, (1996). *The Intelligent Person's Guide to Liberalisation*, New Delhi: Penguin.

2) McCartney, Matthew, (2016). *Political Economy, Growth and Liberalisation in India 1991-2008*, Routledge.

3) Mohan, Rakesh (edited), (2017). *India Transformed: 25 Years of Economic Reforms*, Penguin Random House.

Some websites such as rbi.org.in and indiareforms.csis.org and several entries under Wikipedia could be consulted for developments in areas related with economic reforms.

7.12 ANSWERS OR HINTS TO CHECK YOUR PROGRESS EXERCICES

Check Your Progress 1

1) Correction in instruments and institutions of government intervention to meet the objectives in better terms.

2) Reforms that primarily seek redistribution of income and wealth, and possibly consumption in favour of the disadvantaged sections of the society are equity-seeking ones while those that focus on improving growth performance through efficient use of resources are efficiency-seeking ones.

3) Neoliberal reforms are those reforms which attempt to make market work with less restrictions and withdrawal of State from activities which market could perform. Since political liberalism got historically associated with 'progressivism' which advocated restrictions on market and increased role of State, policy of relaxation of restrictions on market functioning was considered to be neoliberal.

Check Your Progress 2

1) Dominant view of the leaders of Independence was that Indians do deserve to have all comforts of the Western world. Since our limited export potential could not allow to import unrestricted amount of goods and gadgets, we decided on an industrialisation strategy which favoured produced substitutes of imported goods in home.

2) For a pretty long time, one needed a lot of licenses or permits to start and run an industrial enterprise. For purchase of scarce material, say steel or cement or sugar, one needed to have a permit. If one needed imported material needing foreign exchange, in addition to license or permit, one was assigned a quota. The regime was popularly called license, permit and quota raj in contrast to liberalisation, privatisation and globalisation one.

3) One was market-oriented Economic Reforms which were initiated in Communist China in 1978 under the leadership of Deng Xiaoping after the death of Mao Zedong in 1976. The other was enunciation of Glasnost and Perestroika in the erstwhile USSR under the leadership of Mikhail Gorbachev.

Check Your Progress 3

1) Invasion and occupation of Kuwait by Iraq in August 1990 and Iraq's refusal to vacate it led a wide scale War against it under the leadership of the US army in which 35 nations had participated. It swelled import bill and slumped exports, plummeting forex reserves.

2) As India's creditworthiness had come down, external commercial borrowings became difficult. Second, non-concessional loans from international agencies are still cheaper. Internally, also, there was a feeling that reforms are called for.

3) Government of India devalued rupee against foreign currencies, drastically modified the industrial policies, and made several taxation changes, and also set up several committees to make recommendations to the Government.

Check Your Progress 4

1) Despite introduction of several reforms, fiscal parameters such as revenue deficit and fiscal deficit were not reaching the desired levels whether at Union or State level. The Act was a kind of imposition of self-discipline.

2) Cash reserve ratio (CRR) keeps banks fairly liquid while statutory liquidity ratio (SLR) directs credit towards government by purchase of government bonds. Cash reserves with the Central Bank, do not normally earn interest to the bank while government bonds do. However, CRR checks the credit creating activity and SLR crowds out finance for private sector.

3) As of now, rupee is convertible into foreign currencies on the basis of market forces. However, it is not normally convertible on capital account.

Check Your Progress 5

1) Liberalisation means relaxation in restrictions while laissez faire means absence of restrictions.

2) Divestment or dilution of government ownership in a public sector enterprise. Proceeds accrue to government as non-debt creating capital receipt.

3) When residents (including companies) of an economy are free to produce anywhere or consume anywhere or products of anywhere, an economy is said to be globalised. It amounts to freedom to trade and freedom to investment; in practical terms, it means lessening of restrictions on imports/ exports and investment. Movement of labour is not articulated at the same level.

Check Your Progress 6

1) First generation reforms are usually reckoned with those that can easily accomplished through executive orders, with minimal legislative requirement while seconds generation reforms need political sanction through legislation.

2) Bringing informal segments of an economy, including jobs, into formal contact with the government through any channel.

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