CHAPTER IV

WTO AND INDIA’S STRUCTURAL ADJUSTMENT REFORMS
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This chapter concerns with the conceptual framework of Structural Adjustment Reforms and their application in India. This chapter discusses the role of World Bank and IMF in the launching of Structural Adjustment Reforms by various countries in the World. However, the main focus of this chapter is on the Implementation of Structural Adjustment Reforms Initiatives of the Government and the consequences of these Reforms on different aspects of Indian Economy. Finally, it also analyses the role of WTO in the implementation of Structural Adjustment Reforms in India.

In the recent past, for the less developed countries (LDCs) of the World the Structural Adjustments in the economy have become a fact of life. Sponsored by the World Bank in 1980, the Structural Adjustments policies are supplemented by the stabilisation policies sponsored by the International Monetary Fund (IMF). These packages were originally introduced as short-term remedies to rectify the existing severe imbalances in the external and internal accounts in several countries. However, very few countries have succeeded in overcoming these imbalances. In the case of few countries, their association with the World Bank and IMF has continued, for nearly 17 years. This period is long enough to assess the viability or effectiveness of any
package of policies. Because the structural adjustment has been applied uniformly to a wide variety of conditions.²

The Structural Adjustments involve a wide range of financial measures and a set of conditionalities. These conditionalities have raised several controversies. Some countries viewed them mere banking practices to guarantee repayment. Some others countries saw, in these conditionalities, an attempt to retain the recipient countries as client states perpetually dependent on the rich nations. Those who took a positive view argue that such conditionalities should have been adopted by the countries concerned as they reflect good economics, irrespective of whether these conditionalities are accompanied by funding or not. The conditionalities help to ‘get the basic right’ to avoid trade and price distortions, make resource allocation rational and optimum, and link production decisions to the comparative advantage of the countries concerned.³

Scholars assumed that the New Political Economy (NPE) of development which became popular world wide in the recent past, provides the theoretical basis of Structural Adjustments Programme. The NPE argues that self-interest and group interests, along with the broader distributional coalitions of a number of groups, lead to a situation where perfectly rational individual decisions produce irrational economic results. Since the distributional coalitions thrive in controlled economies, one possible solution
to check them is to remove entry barriers, to make resources mobile and the
market free and perfectly competitive. One interesting aspect of NPE is its
emphasis on the rent-seeking behaviour that characterizes controlled
economies and produces welfare losses in terms of diversion of resources
from more productive activities to unproductive actions such as lobbying, etc.
Another solution is to rely on impartial and competent bureaucrats for
overseeing resource allocation. The NPE holds a poor view of the political
leaders of the LDCs and would prefer them to leave economic issues in the
hands of the private agents operating in a market without barriers.

GENESIS OF STRUCTURAL ADJUSTMENTS PROGRAMME

There is some dispute among the supporters of the NPE, as to the
origin and pacing of Structural Adjustments Programme. Some take the view
that 'reforms should be introduced as quickly as is economically and
technically possible' to take advantage of this period following the takeover by
a new regime. Arguments are also advanced in support of such a 'big bang'
approach. First, improvements brought about following temporary dislocation
during the change over of the regime would be attributed to these Structural
Reforms and would enhance the credibility of the reforms and regime.
Second, the quicker the reforms and the achievement of a certain degree of
success, the more difficult would it be for the opponents of reforms and the
regime to coalesce and undermine these reforms. Further, such reforms
should yield result pretty fast; a slow and painful adjustment process might
alienate the population and place them into the hands of the opposing forces.\textsuperscript{7}

On the other hand, the gradualists argue that the reforms, to be successful eventually, should be carefully implemented, counting every step and not attempting a short cut that does not exist. Any failure resulting from fast-track action in the early stage might jeopardize the reforms process as a whole. This approach also referred to as shock approach can work if there is excess capacity in the economy and the possibility of a high level of financial inflow within a short time; if that not the case, the shock treatment might produce is opposite – a revolution, or a coup, or, at the least, a massive outburst of protest, perhaps leading to the abandonment of the adjustment programme by the leadership.\textsuperscript{8}

As already stated, the Structural Adjustments are bound to be a painful process. The important question is, how to sustain such reforms over a long period in the face of the hostility which the a programme is likely to face. Further, such pain is unlikely to be distributed uniformly – for most it would be relatively more painful, while the potential long-term beneficiaries are likely to be in the minority, at any rate at the beginning of the adjustments process. In this situation, it is inevitable that various interest groups will try to outwit one another, if possible to secure a free or less costly ride than others. Such a 'war of attrition' can eventually reach a stage where the government, unable to reconcile various conflicting interests, would be forced to abandon
the programme. One way of obviating this is to provide, in the words of John Williamson, "a sweetener that will help the reformers to retain political support during the difficult and perhaps lengthy period before the reform starts to bear fruit".  

Balassa conceptualized Structural Adjustments Programme as 'policy response to external shocks, carried out with the objective of regaining the pre-shock growth path of the national economy'. The expression 'structural', according to Balassa, reflects the need for discrete, as compared to marginal changes in policies in response to discrete shocks. During the period of adjustments, growth was to take precedence over distribution and production over social justice.

As already noted, the Structural Adjustments Programme was introduced by the World Bank in 1980s. However, its origin can be traced to the 1970s, when the World witnessed massive economic upheavals arose from the two oil crises emerged in 1973 and in 1979-80. The sudden and steep rise in oil prices created, on the one hand, an unforeseen opportunity for growth for a group of Less Developed Countries exporting oil, and on the other, at least for while, a feeling of despair in the West, as it was going to involve a massive outflow of resources from the rich countries located in that part of the globe.
The Structural Adjustments Programme aims at achieving three conditionalities viz., liberalization, privatization and globalisation, described by some as the LPG model.¹³

These conditionalities can be described as follows:

(I) LIBERALISATION

The core of the Liberalisation is that economic management should be left to the market. The prices determined by the interaction of demand and supply forces – whether for commodities, labour power, capital, land, or foreign exchange – should be flexible in either direction and should be capable of clearing the market. The resulting allocation of resources, commodities, labour power, foreign currency, etc., would be optimal and efficient, while any deviation from it would involve avoidable social costs.¹⁴

It follows from this that the state should take a back seat in the economic matters. Any intervention by the state – in the form of controls, subsidies, selective protection, etc., would distort prices and make the resulting allocations inefficient, thus hindering economic growth. Controls, by restricting flows of commodities or capital, involve high social costs, distort priorities, and involve rationing in some form or the other.
(II) PRIVATIZATION

Another important feature of this economic philosophy is that whatever public sector economic activities are in operation should be closed down, phased out or trimmed or passed on to the private sector. Public ownership should be allowed only in cases of natural monopolies and strategic industries, i.e., in defence and research establishments, and should not be allowed to become a drain on state resources.\textsuperscript{15}

(III) GLOBALISATION

The third major objective is globalisation, which assumes that more trade is better for all the parties concerned – some may gain more than others, but all would gain. Any action that interferes with the free flow of capital, goods and services, would produce sub-optimal results. Import substitution and consequent protective measures, i.e., tariffs, controls and restrictions; raise the cost of domestic production. Such a policy, by reducing their competitiveness, discriminates against those export items that could be traded in the global market on the basis of the country’s comparative advantage.\textsuperscript{16}

Further, the goal of self-sufficiency makes no sense in a closely integrated world economy with free buying and selling. A country should specialize in production and exports only in those items where it enjoys a comparative advantage, that is, given its factor endowments, where it can
produce best. Earnings from such exports should be able to pay for the required imports. In several poor countries such comparative advantage lies in labour-intensive production such as food products and textiles, and not in large-scale capital and knowledge intensive industries involving long gestation periods such as steel, oil refining, petro-chemicals, or shipbuilding.

MULTI-NATIONAL CORPORATIONS

A corollary of the third is an open door policy with regard to the multinational enterprises many of which are vertically integrated, operate with numerous affiliates and subsidiaries spread over the world, and maintain close and tacit understanding with fellow oligopolists, while also engaging in non-price competition with them. Under the Structural Adjustments Programme such enterprises should be treated on par with the local enterprises and should not be discriminated against. In particular, local content requirement eg., to deploy local labour, to purchase local goods and services, to reinvest a part of the profit within the country or to export a proportion of total production, and so on – should be discontinued. Foreign competition, according to this view, would improve the efficiency of the indigenous producers and would drive them towards production of goods that are in line with the country’s comparative advantage. Further, the vast experience, skills and new technologies of the MNCs would facilitate global integration of the national economy.
Not that the state has been left with no role under this new regime. The main task of the government, is to promote literacy particularly extension of technical education and access to safe drinking water and health facilities to all, are seen as major areas of governmental activity. Natural monopolies and the issues of national security are also considered as the exclusive preserves of the state.

STRUCTURAL ADJUSTMENTS PROGRAMME IN INDIAN

In India, the SAP was introduced in July 1991, almost immediately following the formation of a new Government under the Prime Minister P.V. Narasimha Rao. Without losing any time, the Government applied for a loan of $2.3 billion from the IMF and began fulfilling 'anticipatory conditionalities', including two successive devaluations and withdrawal of export subsidies, to smoothen the passage of the application. The Budget of July 1991 fully reflected the SAP, which came to be known as the New Economic Policy (NEP).

Every economic step taken by the Government of India in 1990s was in accordance with the major prescriptions of the Structural Adjustments Programme which can be discussed as follows:

\[ \text{a) It is better to introduce reform following a change of regime. The new Government introduced it almost immediately after coming to power.} \]
b) The blame for the economic ills of the past should be put on the previous regime. This was done quite successfully and in a politically clever manner, never referring to the IMF loan of 1981, and the taking of large loans from private international banks for meeting elite consumption needs.

c) The people should be asked to make sacrifices, as the pain of adjustment was an unavoidable price to pay for the past malfunctioning.

d) The pace of Reforms should be fast enough not to allow the opposition to coalesce. The pace of these Adjustments was terrific. By July 1991, a new trade policy and a new Industrial Policy had been announced, and before the year was over the Narasimha Panel presented its report on financial reforms. The fiscal reforms, under the guidance of Raja Cheliah, was spread over two budgets, while clear goals were specified for controlling inflation and fiscal deficit. Above all, the ideology of Reforms was widely publicized thought he print and electronic media, through seminars and conferences, by way of massive and high quality advertisements, and by street-corner hoardings exhorting the people to buy shares. However, some take the opposite view: that the Government was in fact moving at a 'gradualist' pace, and was not running on the fast track (Ahuwalia, 1995: 13). There are still others who, while
rejecting the ‘big bang’ approach, would not accept gradualism on the ground that it is not consistent with the ‘Political Economy of Reforms’.

e) The potential gainers from the Reforms process should be politically organized against the potential losers. Conforming to NPE, food procurement prices were revised upwards, the agri-food industry entered Indian agriculture with full force to create new production relations and the trading community and stock market brokers were mobilised in support. The campaign against potential losers – such as urban dwellers, workers and bureaucrats – was not actively pursued because of political compulsions. Labour market reforms were also not undertaken for the same political reason.

f) The package should be ‘owned’ as an indigenous creation. Later, when the obvious similarity between the NEP and the SAP could not be concealed, the government fell back on the ‘there is no alternative’ argument.

g) That technocrat – bureaucrats with experience of working with the World Bank and other international organizations and known for their integrity should be made responsible for directing the reforms, and not discredited politicians with axes to grind. In this case, the Finance Minister was picked from outside the arena of politics: both
he and the Finance Secretary had long association with the World Bank and other international agencies.

That the political leadership should be fully, and over a long term, politically committed to reforms. In the first three years, the NEP was implemented with little political resistance, ignoring the protest of the left-wing parties. The support from the business community was overwhelming, and share market activities took off dramatically.

FEATURES OF STRUCTURAL ADJUSTMENTS PROGRAMME

The major features of Structural Adjustments Programme process of in India, can thus be summarized as follows: 19

First, the expectations from the Reforms in India is not in terms of across the board of retreat of state in favour of market but, in terms of enhancing state’s capacity to permit efficiency-gains and expand availability of public and merit goods.

Second, while the state is retreating in some areas, such as pure commercial goods or services, it is both retreating and expanding in other areas such as regulation and is expected to expand further in public and merit goods.

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Third, a variety of options have been initiated by the Central Government to redefine the role of state vs-à-vs market and the framework is comprehensive, though a significant ground is yet to be covered. In general, the direction of reform is retreat as a Producer State and retreat combined with expansion as a Regulatory State.

Fourth, at the provincial level, while there is some marginal retreat as a Producer State, substantive expansion and redefining of the role of State as a Facilitator and Welfare-Provider appears to be in order. A variety of options have been exercised by different states in the country though significant progress is required if the fiscal sustainability is to be combined with an expanded role for the State, at Provincial level.

Fifth, the differences in the pace and direction of reforms in different states are perhaps explicable by the political management of the process, technical capability to design measures, institutional underpinning to implement them and nature of support from the Central Government.

Sixth, there is evidence to show that, even in areas where the state was to expand, mainly at the provincial level and as welfare provider, decentralization of initiative and management away from provincial head quarters down to local levels seems to be a preferred option. This would imply that the state may reorient and expand by changing degree of centralization.
Implementation of Structural Adjustments programme

(1991-96)

The first round of Structural Adjustments ran for five years up to 1996, when the Congress Party was defeated in the General Elections. The new Coalition Government formed at the Centre with the support of Left Parties had pledged to continue the reforms package, without specifying clearly what 'reforms' constitute. In the opinion of financial experts the five year period of the Structural Adjustments Programme (1991-96) did worse than a comparable five-years period proceeding its introduction in 1991 (1986-91).20

It was reported by the official agencies that the India’s foreign exchange reserve rose from around $1 billion at the beginning of the reforms to nearly $21 billion in 1994-95 and then declined to $17 billion in October 1995, for various reasons. This increase did not affect the trade surplus, in any manner but was largely a sum total of various types of foreign borrowing; from the IMF, World Bank and other international agencies and foreign governments, from NRI deposits and unstable foreign portfolio investments. Only a small part was due to increase in FDI, $6 billion in seven years, during 1990-97 and a certain amount was due to the time-bound amnesty declared by the Government to the holders of black money, which passing through several hands in the infamous hawala market, returned to India as foreign exchange. However, it is unstable and unreliable.21
With regard to the GDP growth rate, it can be stated that it declined from 4.7 in 1990-91, to 1.1 per cent in 1991-92, but recovered to 5.1 per cent and 5.0 per cent in the following two years. In the following two years it increased further to the extent of 6.3 per cent and 7 per cent respectively. Overall, the growth rate of GDP in these five years is slightly less than the figure for the 1980s.\(^{22}\)

Analysing the progress of SAP in India, an analyst states thus: The country has failed to achieve substantial economic progress though its policy in the pre-1991 period closely resembled the East Asian policy package based on import substitution. With the regard to the post-1991 experience under the Structural Adjustments it can be stated that during the five years following 1991, the Indian economy has done no better than in the preceding five years, though, at least to start with the new Government more or less followed the guiding rules of the Structural Adjustments Programme. The Programme was operated in full swing in the first three years, but then it lost momentum because of political opposition, and the Programme was not taken to its logical conclusions, became of the withdrawal of subsidy and PDS, and a more committed effort towards disinvestments and closing down of sick industries. It is argued that because the attempt was half-hearted, the outcome was not as bad as it could have been.\(^{23}\)
THE STRUCTURAL ADJUSTMENTS PROGRAMME AND GOVERNMENT INITIATIVES

As a part of the SAP, the Government of India contemplated various steps in the name of stabilization measures right from the beginning of this programme i.e., 1990-91. As a result, the fiscal deficit was reduced initially from 8.1 percent of GDP in 1990-91 to 5.7 per cent of GDP in 1992-93. It was announced that the Government intended to reduce the deficit still further during the coming years, but that intention was not realized.24

A second important measure was the devaluation of the rupee. At the same time, export subsidies were abolished and an import entitlement scheme for exporters was announced. Between 1991 and 1993, a dual exchange rate (with a free market rate for exporters) in fact prevailed, but the exchange rate was finally unified in 1993. It was estimated that the net real devaluation between 1991 and 1993 has been about 25 percent.25

Within a year, the combined impact of the fiscal tightening and the exchange rate change resulted in a reduction in the current account deficit from 2.3 percent of GDP in 1990 to 0.7 percent of GDP in 1993. Consequently, the inflation rate came down but not as much as had been targeted. Even with recession, the wholesale price index rose 11.9 per cent in 1992, 7.5 per cent in 1993, 10.5 per cent in 1994, and 9.3 per cent in 1995.
Overall, the stabilization aspects of policy introduced in 1991 achieved limited success.  

The other measures taken in this direction relate to increase the quantity of exports. Exchange rate depreciation was one such measure. Further, the reduction of protections through tariffs and the removal of quantitative restrictions on imports have positively affected the exports. In addition, some goods whose export had been permitted only through government trading companies were decanalized.

Similarly, the Government of India for the first time attempted to attract foreign direct and portfolio investment by reducing and removing restrictions on it. Until 1991, the foreign investments were permitted only in cases in which they provided technology transfer, and equity participation above 40 per cent was not permitted. In July 1991, foreign technology agreements, foreign direct investments, and industrial licensing were all liberalized.

Thus between 1991 and 1995 (with liberalization concentrated in 1993 and 1994), the Indian trade and payments regime was substantially liberalized. However, despite repeated tariff reductions, Indian tariffs still remain high by world standards, as other countries have also been lowering their tariffs.
Under the SAP the financial sector was significantly liberalized, but again from a very illiberal base and with gradual reforms. Over two-thirds of financial assets in India were held in banks by 1991. The banks themselves had been nationalized since 1969 and were subject to two sets of reserve requirements that effectively meant they held more than half of their assets with the Government. The banks were also subjected to "directed lending", whereby some of the remaining portion of their assets was to be extended as loans to specified activities, such as agriculture.

Nonetheless, economic growth accelerated markedly during the 1990s, due in large part to the stimulus provide by the reforms themselves. While there is some evidence that in 1998 and 1999 the stimulus to growth had diminished, it nonetheless seems clear that what was done in the early 1990s was sufficient to enable the country to attain a more satisfactory economic performance that at any earlier point of time. The Growth Rates reached 7 and 8 per cent during the late 1990s. Moreover, the analysts and policy makers alike became convinced that the Growth Rates of 7 per cent and more were achievable, something that would have been vigorously contested only a decade earlier. Nonetheless, the observers agree that the Reforms have lost their momentum and that, if the economy is to be able to attain and sustain a growth rate of 7 per cent or more, the momentum for Reforms will once again have to be regained.30
In the post-Reforms period the export performance of the country has improved notably. As can be seen, the export volume grew at an average annual rate of 11.45 percent. During the period 1991-97 the growth of the exports recorded the highest rate achieved in any prior decade. This was reflected in an increased share of exports of goods and services in the GDP by the latter part of the 1990s which was 9.94 per cent. In fact, the growth of export earnings was rapid enough to reverse India’s declining share in World’s trade. It had started at 1.42 per cent in the 1950s, fallen to a low of 0.49 per cent in the 1980s. Then, in the 1991-97 period, it rebounded to 0.58 per cent.31

By 2000, it was clear that the Indian economy had changed markedly over the post-crisis years. The Growth Rates did accelerate (although there are questions as to the sustainability of these higher rates without a new wave of reform), the economy was opened considerably, and the extent to which controls stifled economic activity had been reduced. The Indian economy in the year 2000 is vastly different from what was prior to the beginning of Reforms in the early 1990s. Quite clearly, the Reforms to date have improved the functioning of the economy and permitted a higher rate of economic growth than was regarded as attainable on a sustainable basis in earlier decades.
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