CHAPTER I
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INTRODUCTION

1.1 Introduction:

Disenchantment with the policies and development strategy in India between 1951 and 1991 with regard to productivity, efficiency and growth in several sectors, specially industry, sluggishness in generating employment, alleviating poverty etc, led economists to focus attention on the need for a turnaround in 1991.

In the 70s and 80s numerous critiques and protests emerged from Indian economists and policy makers, but there were not many listeners. A multi-dimensional crisis in 1991 was too obvious to go unnoticed. There were three dimensions of the crisis –

1. Crisis of Resources - This was in the form of huge deficits and drying up of governmental revenues. Infrastructure, defence and social sector began starving for funds.

2. Crisis of Foreign Exchange - India’s creditors refused to give any more credit.

3. Severe Import Cut - The private suppliers of capital goods and raw materials stopped credit resulting in severe import reduction.

The reform programme initiated in June 1991, though gradualist in its approach, (different from the incremental approach to reforms of the 1980s) had clear objectives such as integration with the global economy through trade, investment and technology flows. The instruments were
not to be piecemeal adjustments but system changes affecting several sectors of the economy. The comprehensiveness of the reforms is evident when we look at the main elements of the economic reform programme.

1. Fiscal Stabilisation - The design of India’s reform programme was fully in line with the conclusion that fiscal stabilisation is an essential pre-condition for crisis management, when the current account deficit was high and inflation was in double digits.

2. Industrial Policy and Foreign Investment - The most radical changes implemented in the reform package have been in the area of industrial policy and removal of several barriers to entry. Licensing is now needed only for a small list of industries (only where environmental and pollution considerations are important). The list of industries reserved for the public sector has been drastically pruned and many critical areas have been opened up for private sector participation. The new policy is actively supportive of foreign investment in a wide range of activities.

3. Trade and Exchange Rate Policy - In keeping with the objective of greater openness and outward orientation, trade policy has been substantially liberalised for all except final consumer goods (the Government has indicated that this too will be gradually liberalised). Quantitative restrictions on imports have been largely eliminated. The trade and payments system has moved from a fixed and typically overvalued exchange rate to a market determined exchange rate within a framework of considerable liberalisation on the trade account.
4. **Tax Reform** - Reform of the tax system has been an important element in the government’s reform programme with major changes contemplated in both direct and indirect taxes. These reforms will go a long way towards the objective of creating a system, which avoids economic distortions and ensures adequate buoyancy of revenues to support the task of fiscal consolidation.

5. **Public Sector Policy** - Reform of the public sector is a critical element in the structural adjustment programmes all over the world and is included on India’s reform agenda. However, this is an area where changes are being implemented slowly. Instead of outright privatisation, the government has initiated a limited process of disinvestment of government equity in public sector companies, with government retaining 51% of the equity and also management control. The disinvestment helps provide non-inflationary resources for the government budget, without adding to the fiscal deficit.

6. **Financial Sector Reform** - The reforms in the real sector aim at creating a new set of incentives, which will encourage reallocation of resources towards more efficient uses. This needs to be underpinned by a parallel process of financial sector reform, which will enable that sector to mobilise and allocate savings to support the process of restructuring in the real economy. Several initiatives have been taken in these areas covering both the banking system and the capital markets.

7. **Reforms in the Agricultural Sector** - The new regime not only makes agricultural exports more competitive at the new exchange rate, it also stimulates the growth of the agro-processing industry, with strong
backward linkage to agriculture. A major area where policy reforms can help agriculture is in the area of rural credit. The financial sector reform is to address this problem.

8. Labour Market Reforms - A commonly heard complaint from domestic as well as foreign investors is that labour markets in India are unduly rigid. However it is also important to recognise that reform of labour laws is a politically sensitive issue. Any major change in the labour laws is likely to evoke fears of displacement. Reform of labour laws must come after the creation of credible ‘safety nets’ to deal with the problems of displaced labour. Hence there is the creation of a National Renewal Fund which is to finance compensation payments to labour made redundant in the course of public sector restructuring and closure of unviable units. It is also to finance retraining programmes to help redeploy such labour.

Thus the new economic reforms in India are far-reaching and cover several sectors in a mutually reinforcing fashion.

1.2 Objective of the Study:

1. To analyse the successes and failures of the New Economic Policy/Economic Reforms (1991) in India with reference to -


   ii Role of infrastructure (economic and social infrastructure) in industrial growth.
iii Importance of state intervention in the development of infrastructure.

2. To evaluate the propriety of the oft-repeated criticisms of the New Economic Policy (NEP).

3. To suggest future guidelines in policy formulation.

1.3 Hypotheses tested in the Thesis:

1. The economic reforms (1991) have supported industrial growth. The process of industrial growth is studied through the performance indicators such as annual growth and index of industrial production (IIP) for –

1. Major sectors of industry –
   i  Mining
   ii Manufacturing
   iii Electricity and
   iv General.

2. Use-based classification of industries –
   i  Basic Goods
   ii Capital Goods (32 industries)
   iii Intermediate Goods (36 industries)
   iv Consumer Goods -
      a) Consumer Durables (12 industries)
      b) Consumer Non-Durables (35 industries)
for the time period 1991 to 1996. An analysis of the trend in the growth process is attempted. This provides an insight into some of the deficiencies of the system and enables us to devise ways and means to circumvent the deficiencies.

The hypothesis that the economic reforms have supported industrial growth has been disproved.

2. The performance and growth of industry depend on various factors, one of which is infrastructure.

Infrastructure consists of –

1. Economic Infrastructure (physical infrastructure)
   
i  Basic Infrastructure-electricity, coal, steel, crude oil, refinery throughput and cement.
   
ii  Other Infrastructure sectors such as Railways, Ports and Telecommunications.

2. Social Infrastructure
   
i  Education
   
ii  Health and
   
iii  Research and Development (R&D).

The adequacy or otherwise of infrastructure largely determines an economy's success or failure in diversifying production and expanding trade. Here the correlation between industrial growth and growth of infrastructure sectors is examined. The
+ve or –ve, high or low correlation enables us to understand the role and importance of each of the infrastructure sectors to industrial growth. This gives a future direction of infrastructure investment vis-à-vis to industrial growth.

The hypothesis that performance and growth of industry depend on infrastructure has been proved.

3. State intervention has to play an important role in the development of infrastructure specially social infrastructure.

The role of government/public policy in the growth of infrastructure services in the light of increased private sector involvement in the provision of infrastructure services is examined. The provision of infrastructure services solely by the government has been challenged today by a) fiscal constraints and b) technological innovations. Further, the government by confusing its role as owner, regulator and operator has failed to improve infrastructure services. Hence private enterprises are being cajoled into infrastructure in a big way. Nevertheless, the governments are responsible for creating policy and regulatory frameworks.

The hypothesis that state intervention has to play an important role in the development of infrastructure specially social infrastructure has been proved.
1.4 Methodology:

1. Growth and performance of industry is analysed from –

- Data on industrial production in major sectors of the industry relating to –

  1. Annual growth rates (in percentage).

  2. Index of Industrial Production (IIP) - i.e. growth with weights for each sector.

  The major sectors of industry include –

  i Mining

  ii Manufacturing

  iii Electricity and

  iv General


- Data on industrial production by Use-based classification relating to –

  1. Annual growth rates (in percentage).

  2. Index of Industrial Production (IIP).

  The categories of industries under Use-based classification are

  i Basic Goods

  ii Intermediate Goods
iii Capital Goods

iv Consumer Goods which consists of-

   a) Consumer Durables and

   b) Consumer Non-Durables.


The IIP of major sectors of the industry provides an insight into the trend of industrial growth. It also shows the contribution made by the broad sectors of industry to the pattern of industrial growth in the given time period.

The IIP under the Use-based classification shows the composition of growth in manufacturing industries. The emerging pattern and composition of industrial growth indicates the direction of industrial growth.

Statistics relating to Industrial Growth and Performance are taken from –

i Various issues of Economic Survey.

ii RBI Annual Reports

iii Central Statistical Organisation (CSO)

iv National Accounts Statistics (NAS)

v Annual Survey of Industries (ASI)

vi Handbook of Industrial Statistics.
2. The correlation between industrial growth and growth of infrastructure is studied with the help of correlation coefficient. Time period 1991-1996. The study of +ve or -ve, high or low correlation between industry and infrastructure enables us to focus on the direction of infrastructural investment. Sound and well-directed infrastructural investment helps raise productivity and lower production cost. It also throws light on the role and importance of the infrastructural sectors to industrial growth.

Statistics relating to Infrastructure are collected from –

i Various issues of Economic Survey.

ii India Infrastructure Report – Volume I, Volume II, and Volume III (Published by Rakesh Mohan on behalf of the Ministry of Finance, Government of India.)

iii Annual Reports of –

a) Department of Railways, Ministry of Railways.

b) Department of Telecommunications, Ministry of Communication.

iv Basic Port Statistics, Ministry of Surface Transport, Government of India.

3. The role of state in economic development specially with reference to economic and social infrastructure is studied in the light of the neo-classical views on state and market. Market failures in certain areas in developing countries like India have re-established the need for state intervention in certain critical
sectors—like the social sector, which includes education, health and research and development. However, the huge fiscal deficits have resulted in the social sector receiving the axe. Finally it has been shown that the debate on the preferable or better paradigm of development between the market and the state is inconclusive, as there have been pendulum-like swings between the market and state at different points of time.

For testing this hypothesis, we have drawn on the literature from the


3. Annual Reports of the Ministry of Human Resources pertaining to Education, Health and Research and Development.

4. Various issues which have appeared in Economic and Political Weekly and Economic Times.

1.5 Structure of the Study:

The Chapter Scheme of the study is as follows –

Chapter I - Introduction

Chapter II - Review of Literature.

Chapter III - Industrial Growth and Performance.

Chapter IV - Infrastructure and Industrial Growth.

Chapter V - State Intervention in Infrastructure.

Chapter VI - Summary of Findings and Conclusions.