CHAPTER-1

Prelude

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1.0 Introduction:-

India was pushed to the brink to face a crisis of foreign currency in 1991 which forced the country to mortgage gold from the reserves to get foreign currency for payment of foreign trade. The new government formed after this incident implemented the new economic policy. The effects of these economic reforms were perceived nationwide.

With this backdrop, taking Gujarat as a region, this topic to chosen to study the changes in the industrial development of Gujarat with reference to pre and post economic reforms together with a study and comparative analysis of its industrial development climate juxtaposed with other industrial states.

1.1 Economic Reforms:-

The implementation of economic reforms in India was started in 1985. For some years this reforms had a limited expansion. As deficit increase because of non developmental expenditures and the Gulf war crisis affected our economy. Our foreign exchange reserves decreased. We were forced to use our gold reserves for foreign payment liabilities. This affected our credibility at the international level and reduced flow of foreign investment.

To improve the above situation we had to start economic reforms with revolutionary approach since 1991.
It is generally agreed that the process of economic reforms was initiated in India by the government of P. V. Narasimha Rao in 1991 with the announcement of a number of measures for liberalizing the economy by the finance minister Manmohan Singh.

However, Arvind Panagariya\(^1\) has argued that the process of economic reforms was initiated during the second half of 1980s under the stewardship of Prime Minister Rajiv Gandhi. In support of his contention he quotes from the Kingsley Martin memorial lecture, delivered in Cambridge in 1986 by I.G. Patel who approvingly described the reforms introduced by Rajiv Gandhi in the preceding one and a half years as the “NEW ECONOMIC POLICY”.

This new economic policy had moved the Indian economy toward increased outward and inward competition by the end of 1980s. Panagariya emphasizes the shift in the industrial policy statement, 1990 towards large-scale liberalization of industrial policy. This policy provided compelling evidence that internal and external liberalization had gained considerable political acceptance at least a year before the balance of payments crisis.

1.1.1 Factors Responsible For Economic Reforms:-

(a) We were forced to adopt economic reforms because of the 1991 economic crisis, which is discussed as follows:

- Our internal debt had increase, due to the imbalance between government income and expenses. This increase from 35% of GDP in 1980-81 to 49.8% in 1990-91.
- The 10 percent interest payment ratio with government total expenditure in 1980-81 increased to 22% in 1990-91.

Our balance of payment situation in 1991 was also critical. Our trade deficit of 2.1 billion dollars in 1980-81 increased to 9.7 billion dollars in 1990-91. This increased our foreign debt from 12% of GDP in 1980-81 to 23%.

The annual average inflation rate of 6.7% in the earlier decade increased to 10.3% in 1990-91. In this period, the prices of food rose substantially in spite of three good monsoons in the country.

(b) India had followed the U.S.S.R. planning strategy after independence. The failures of the socialist economy came forward after the disintegration of the U.S.S.R. On the other hand, in spite of huge investments our planning results were discouraging. So we think about economic reforms.

(c) A number of South-East Asian countries like Thailand, South-Korea, Singapore and Malaysia had entered “Tiger Economy” through economic reforms, which encouraged us to think of economic reforms in our economy.

Jagdish bhagawati² has given in brief, the analysis of economic activities during the three decades of 1950 to 1980, while discussing why the reforms finally began to happen in 1991 as follows:

We had started out in the 1950s with:

- High growth rates
- Openness to trade and investment
- A promotional state
- Social expenditure awareness
- Macro stability

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But we ended the 1980s with:

- Low growth rates
- Closure to trade and investment
- A license-obsessed, restrictive state
- Inability to sustain social expenditures
- Macro instability, indeed crisis

1.1.2 **Measures for Economic Reforms**:-

The process of economic reforms undertaken by the P. V. Narasimha Rao government consisted of two distinct strands - **macroeconomic stabilization and structural reforms**\(^3\).

**Macroeconomic stabilization** deals with demand management. Here, factors restraining the purchasing capacity are controlled in the economy. Thus, economic development is accelerated by demand. These are as follows:

- Control of Inflation
- Fiscal Adjustment
- Balance of payments adjustment

**Structural adjustments** deal with to tackle the problems on the supply side of the economy. Here, economic development is accelerated by increasing production capacity in the economy. These are as follows:

- Trade and capital flows reforms
- Industrial deregulations
- Public sector reforms and disinvestment
- Financial sector reforms

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1.2 Economic Development:-

Normally, we do not differentiate “economic growth” and “economic development”. But in the terminology of economics, when we talk of “economic growth”, we suggest increase in the total national production, in the national income or in number of labour in the population is considered as economic growth.

While, when we use the term “economic development”, it indicates qualitative change in the economic, e.g. economic development indicates increase not only in the total national production but it also indicates production of new commodities in the economy and increase not only in the working population, but it also indicates qualitative increase in health and hygiene standards, increase in literacy and improvements in labour population.

Thus, economic development indicates not only growth but qualitative change also. In other words, economic growth is related to quantitative concept, while economic development is related to qualitative concept.

1. 2.1 Definitions of Economic Development:-

It is difficult to give a precise definition of economic development. Different economists have given different definition of economic development. Here, discussed important definitions of them:

- **Gerald M. Meier and Robert E. Baldwin**\(^4\) asserted
  
  “Economic development is a process whereby an economy’s real national income increases over a long period of time. And, if the rate of development is greater than the rate of population growth, then per capita real income will increase”.

• **Charles P. Kindleberger and Bruce Herrick**\(^5\) asserted

“Economic development is generally defined to include improvements in material welfare, especially for persons with the lowest incomes; the eradication of mass poverty with its correlates of illiteracy, disease, and early death; changes in the composition of inputs and outputs that generally include shifts in the underlying structure of production away from agricultural toward industrial activities; the organization of the economy in such a way that productive employment is general among the working age population rather than the situation of a privileged minority; and the correspondingly greater participation of broadly based groups in making decisions about the directions, economic and otherwise, in which they should move to improve their welfare”.

• **Michael P. Todaro**\(^6\) asserted

“Development must therefore be conceived of as a multidimensional process involving major changes in social structures, popular attitudes, and national institution, as well as the acceleration of economic growth, the reduction of inequality, and the eradication of poverty. Development, in its essence, must represent the whole gamut of change by which an entire social system, tuned to the diverse basic needs and desires of individuals and social groups within that system, moves away from a condition of life widely perceived as unsatisfactory toward a situation or condition of life regarded as materially and spiritually better”

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• Dudley Seers\textsuperscript{7} asserted

“The questions to ask about a country’s development are therefore: what has been happening to poverty? What has been happening to unemployment? What has been happening to inequality? If all three of these have declined from high levels, then beyond doubt this has been a period of development for the country concerned. If one or two of these central problems have been growing worse, especially if all three have, it would be strange to call the result “development” even if per capita income doubled”.

1.2.2 Obstacles to Development:-

There are a number of economic, political, social and natural factors obstructing economic development. Some of them are such as capital deficiency, market imperfections, lack of skilled labour, capable entrepreneurs, adequate means of transport, political climate, social structure, natural hurdles.

Besides these, there are external factors such as trends of export-import, foreign investment; foreign relations etc. also affect economic development.

Along with this, it is important to break the “vicious circle of poverty” in the economy so that the economic development is accelerated.

1.2.3 Vicious Circle of Poverty:-

Poverty is the highest hurdle in the way of economic development. A poor man has to live on border line of starvation. He cannot provide himself with the necessary amount of food nor necessary clothing nor

a suitable house. He is unable to rear up his children properly. He is not unable to help himself nor is he able to help and serve others.

But the worst thing about poverty is that a poor man is caught in a vicious circle. Being poor, he lacks the means to prosper and since he lacks the means to prosper, he must remain poor. The vicious circle is complete. Poverty leads to inefficiency and incapacity to do well and inefficiency and incapacity must end in poverty.

The vicious circle of poverty is related to both the sides—on the side of demand and supply side discussed as follows:

**On the side of demand,** in a poor country, the level of productivity and so of incomes is very low which means a low purchasing power. Since the purchasing power of the people is law, the scope for business and industry is correspondingly limited. The inducement to investment is practically absent. The rate of investment being low, Productivity is low and the incomes are small completing the vicious circle.

**On the side of supply,** in a poor country having a low level of income, the rate of savings must be small. The resulting lack of capital leads to low productivity and low incomes, this way completing the vicious circle of poverty.

The two vicious circles relating to the demand side and supply side can be presented diagrammatically in figure one and figure two.

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Fig. 1 Vicious circle on supply side

Poverty
OR
Low Income

Low Productivity

Small Capacity to Save

Lack of Capital

Low Investment

Fig. 2 Vicious circle on Demand Side

Poverty
OR
Low Income

Low Productivity

Small Size of the market

Lack of Capital

Low Inducement to Invest
1. 2.4 Strategies of Economic Development:-

It is necessary that the economic development leads to reduction of poverty, inequality and unemployment. For this, a number of strategies can be implemented which is discussed in brief as follows:

- **Strategy of Balanced Economic Development.**
- **Strategy of Unbalanced Economic Development**
- **Strategy of Theory of Big Push**
- **Strategy of Theory of Critical Minimum Effort.**

There are among the development specialists two major schools of thought regarding the pattern and process of growth according to which development should take place.

On the one side, there are economists, like Ragnar Nurkse and W.A. Lewis who are of the view that the pattern of investment should be so designed as the ensure a balanced development of the various sectors of the economy. They, therefore, advocate simultaneous investment in a number of industries so that there is a balanced growth of different Industries.

On the other side, there are economists, like A.O. Hirschman and H.W. Singer believe that rapid economic growth follows concentration of investment in certain strategic industries rather than an even distribution of investment among the various industries. In other words, in the view of these latter economists, unbalanced growth is more conducive to economic development than a balanced one.

According to P.N. Rosenstein Rodan a number of development programs can be implemented by huge investment to rapidly increase the per capita income to break the vicious circle of poverty in the economy. This “big push” can lead to economic development by industrial development in the economy.

According to Harvey Leibenstein “critical minimum effort” (investment) is necessary to break the vicious circle of poverty in the economy
which would increase per capita income, control growth rate of population, and make economic development rapid and continuous.

1. 2.5 **Role of the Government in Economic Development:**

   The government has played a large initiating and active entrepreneurial role in the economy. Various general areas for government action are suggested as follows:

   (1) The government may have to establish markets by promoting suitable institutional arrangements.

   (2) Government enterprise is needed in those fields where profits are too low or the risks are too large to attract private enterprise.

   (3) Government enterprise is justified in those activities in which, even though they might be performed by private enterprise, the results of private performance would be less satisfactory than those of government performance.

   (4) Government direction is needed to promote external economies and, more generally, “balanced growth.”

   Thus, the governments today perform a very wide range of functions for the purpose of affecting the rate of economic development.

   In practice, each country will have to decide where to draw the line between its public sector and its private sector on the basis of its own objectives regarding the sequence and tempo of development, its particular economic circumstances, its institutions, and the administrative strength of its government. If the government is wise and it does the right things at the right time, economic growth is accelerated. On the other hand, if the government is corrupt and inefficient and pursues wrong policies, economic growth is sure to be retarded.
1.3 **Industrial Development**:-

Industrial development is necessary for economic development. As industrial development proceeds the economic and social changes take place in the economy. Changes are also observed in the agricultural sector together with industrial development. **Economic development accelerates with strong interdependence of agricultural development and industrial development.**

1.3.1 **Meaning of Industrialization**:-

Industrialization may be defined as “a process which accelerates economic growth, affects structural changes in the economy, particularly in respect of resource utilization, production functions, income generation, Occupational pattern, Population distribution, and foreign trade, and induces Social change”.

The above definition makes it clear that industrialization is a process which increases income, brings about structural changes such as commercially exploiting unutilized and underutilized resources, employing industrial technology on large scales, making production process more mechanized and efficient, and inducing certain social changes such as awareness of education and health, increase in urban population and industrial training in the economy.

1.3.2 **Importance of Industrial Development**:-

- Labour productivity in industrial sector is much higher and therefore industrial growth ensures higher wages and hence higher standard of living. Thus, it has been well accepted that the high level of income cannot be reached without industrialization.

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Industrialization is regarded as the key for reconstructing the economy as it changes the sectoral composition of output and employment.

- Increase in industrial output and the availability of surplus production will be useful for exports. This will be an important source for earning foreign exchange.
- If a country wants to achieve “takes off” Stage or self sustaining growth, industrialization is a necessary precondition.
- There is always scope for increasing demand for industrial products.
- In international trade, the industrial products will be having favorable terms of trade.
- It is generally felt that there is a positive correlation between industrial development and per capita income.

1.3.3 Importance of Location in Industrial Development:

Proper selection of location is important for any industrial activity. There can be huge impacts on production costs, so the theory of industrial location is forwarded.

The theory of industrial location attempts to explain why the industries are located where they are, why the locations are shifted, and what can be the best location for a particular industry keeping in view the resource endowments of different regions, transport network, existing demand, potential demand etc.

Different theories of industrial location presented by thinkers like Alfred Weber (Theory of industrial location), Tord palander (Expansion of market), Edgar Hoover (Transportation cost) and Sargent Florence (Measure the degree of concentration and propensity to concentrate- introduced location factor and coefficient of localization) are important in the industrial economics.
1.3.4 Factors Hampering Rapid Industrial Development:

The factors which hamper the process of rapid industrial development as discussed in brief as follows: 10

- Absence of an adequate and efficient transport and communications facilities.
- Shortage of energy and power.
- Inadequate development of training, financial and banking institutions.
- Low rate of saving and investment.
- Rapid growth of population.
- Ineffective implementation of economic planning.
- Inefficient public administrative structure.

1.4 Regional Development:

A country is composed of many varied regions. This requires understanding of regional conditions before study of national conditions. So, solution of regional problems would gradually lead to solution of national problems.

Among the regional disparities are varied state per capita incomes, state industrial developments, state agricultural developments, state literacy ratios, state economic developments. A close study of regional economics is necessary to understand these regional disparities.

1.4.1 The Concept of Region:

It is very difficult to define a region because the concept has been used by different people to mean different things. Sometimes part of a district (even a village) is called a region, sometimes a district is taken to be a region, sometimes a state and sometimes a group of states (or parts of them) is regarded as a region.

A region is delimited by three different methods such as Homogeneity, Nodality, and Programming

To first stresses homogeneity with reference to any one or combination of physical, economic, social or other characteristics.

The second emphasizes the so-called nodality or polarization, usually around some central urban place.

The third is programming or policy oriented concerned mainly with administrative coherence or identity between the area being studied and available political institutions for effectuating policy decisions.

1.4.2 Meaning of Regional Development:

Regional development has played a central role in such disciplines as economic geography, regional economics, regional science and economic growth theory. Regional development is clearly a multidimensional concept with a great socioeconomic variety that is determined by a multiplicity of factors such as natural resource endowments, quality and quantity of labour, capital availability and access, productive and overhead investments, entrepreneurial culture and attitude, physical infrastructures, sectoral structure, technological infrastructure and progress, open mind, public support systems etc.
Balanced regional industrial development should form an essential part of economic planning for the country. Balanced regional development becomes necessary to make maximum use of whatever local resources are available for providing employment opportunities to people in different regions, for reducing concentration of industries in certain regions or localities only with all its evil consequences of overcrowding, excessive pressure on housing accommodation, on transport, water, health and educational facilities and fear of its becoming a target of attack by potential enemies.

Balanced regional development does not mean that all regions in the economy should be developed industrially to the same extent. This is just not possible because industrial resources are not evenly distributed in different regions of the country.

Thus, balanced regional industrial development means is that maximum utilization is to be made of the available natural and human resources in the region to the extent possible by developing industries there on the basis of whatever resources are available in the region.

1.4.3 **Regional Disparity:**

Chakradhar Sinha\(^{11}\) has shown prof. Myrdal’s thoughts about main cause of regional disparities in his paper – “Regional imbalances and five – year plans: A case study of Bihar”, as follows:

According to prof. Myrdal, the main cause of regional disparities has been the strong backwash effects and the weak spread effects in the economies. The genesis of regional imbalances has a non-economic basis which is associated with the capitalist system guided by the profit motive. The profit motive results in the development of those regions where the prospects of profit are high while other regions remain under-developed.

\(^{11}\) Chakradhar Sinha – planning and regional development in India, Published by Gaurav publishing house – Jalandhar (1985).
Myrdal attributes this phenomenon to the free play of market forces. The latter tend to concentrate on economic and social overheads in certain regions, leaving the rest of the country in a backwater. These inequalities are accentuated by migration, capital movements and trade. Migration of young and active people from the backward regions will favour the advanced region and depress economic activity in the former, and capital will move into the developed regions, thereby creating capital shortage in the backward regions. The development of industries in former regions may ruin the existing industries at the latter. So the backwash effects, being stronger than the spread effects, regional inequalities are accentuated.

1.4.4 Factor Affecting Regional Disparity:-

- Regional disparity is observed due to natural differences between two regions.
- Regional disparity is observed due to different location advantages.
- Regional disparity is observed due to the differences in facility of economic overheads. The regions with better facilities such as transportation, Communication, Technology, Power etc. are likely to progress faster than other regions.
- Regional disparity is observed due to inadequate development of ancillary industries.
- Regional disparity is observed due to the lack of encouragement for industrial atmosphere.

1.4.5 Indicator of Regional Disparity:-

Regional disparities may be natural and man-made factors. The natural factors are due to differences in natural endowments, natural resources; and
man-made factors are due to neglecting attitude towards some regions as well as favorable treatment to other regions in regards to the development efforts. The main indicators are as follows:\footnote{12}

- Per Capita net state domestic product and growth rate.
- The proportion of population living below the poverty line.
- The percentage of urban population to total population.
- The percentage of literacy rate.
- Growth of different sectors of the economy.
- Infra Structure development.
- Density of Population (Per Square Kilometer)
- Human development Index.
- Net irrigated area as percentage of net area.

The above factors jointly determine the development of the state in the economy.

1.4.6 Theory of Regional Development:-

Growth pole is an important concept in discussion of regional development. Any region growth appears in a point or a development pole with variable intensities and it spreads along diverse channels and with varying terminal effects to the whole of the economy.

A. O. Hirschman and Gunnar Myrdal have discussed favourable and adverse factors to concepts at Trickling down and polarization (by A. O. Hirschman) and spread effects and backwash effects (by Gunnar Myrdal) for concentration of economic activities.

\footnote{12, Dr. Himanshu N. Desai, Key Paper on Inter-district economic variation in Gujarat, 33 Gujarat Economic Conference February 2003, Sardar Patel Institute of Economic & Social Research, Thaltej, Ahmedabad.}
• **Trickling-down or spread effects**:\(^\text{13}\)

They are the favourable effects. Rapid growth in the relatively advanced regions will benefit the less developed regions in many ways. Expansion in the growth poles will provide more employment opportunities to the people of the less privileged areas, and the consequent decline in disguised unemployment there will tend to raise the marginal productivity and hence the living standards of labour.

Moreover, the developed regions may depend on the backward regions for food and raw materials and may, thus, stimulate the development of agriculture there which, in turn, may lead to the growth of the processing and manufacturing industries. The whole region around the growth poles benefits from the opportunities to increase agricultural exports. Besides, higher productivity of investments in the developed regions will provide large surpluses of investable funds which, after sometime, would lead to the search for, and exploration of, new investment opportunities in the retarded regions. This, in turn, will generate more resources for development.

As a result, new ‘growth points’ will be created in the retarded areas and ‘in good time’ their number would increase sufficiently to provide regional balance. Such developments are bound to occur if the economies of the two types of regions are at all complementary.

\(\text{13. Dr. O.P. Mahajan – Economic Planning and Regional development in India – Published by ESS ESS publications, New Delhi (1982).}\)
Polarization or Backwash effects:—

In contrast to the spread effects or Trickling-down, the polarization or Backwash effects are those effects emanating from the centers of growth that discourage growth in other areas. Because of their rapid growth, in contrast to the stagnation of others regions, the centers of growth (or progressive regions) attract net immigration from other parts of the country.

There is a net movement of population, capital, and goods in favour of the progressive regions while the backward regions are continually denuded. Since the migration from backward regions to progressive regions is generally selective in the sense that it is normally the young, the educated, and the healthy that migrate, the age structure in the lagging regions becomes lopsided. All these factors have an adverse effect on the growth of backward regions.

1.5 Chapter Scheme:-

- In this chapter One, titled “Prelude”, an attempt is made to understand the concept and theory related to the study. A detailed discussion of concepts of Economic Reforms, Economic Development, Industrial Development and Regional Development is presented here.

- In chapter Two, titled “Review of Literature”, covers subject related explanation of various studies. It is divided into three divisions – studies on Indian economy, state-wise inter-regional comparison studies, and studies on Gujarat State. Here, importance is given to studies related to pre and post economic reforms.

In chapter Three, titled “Methodology”, the objectives of the study, hypotheses, sources of data, period of analysis and importance of the study, together with the explanation of which statistical tools and methods are used for the study are presented. A conceptual explanation of analyses of various statistical tools and techniques is included here.

In chapter Four, titled “Industrial Development of India”, the β-Growth Rate is calculated for Indicators of Industrial growth of India such as Number of Factories, Fixed Capital, Number of Workers, and Wages to Workers, Total Inputs, Value of Output and Profits.

Besides this, the indicators of industrial growth are measured by the statistical techniques such as Average, Standard Deviation and Coefficient of Variation (C.V.). A comparison of pre and post reform positions of these indicators is also made here.

In chapter Five, titled “Industrial Development of Gujarat”, an attempt is made to study the trends of economic growth of Gujarat with reference to important changes in the economy together with changes in Net State Domestic Product and Per Capita Net State Domestic Product.

With reference to the Industrial development of Gujarat, an explanation of the beta growth rate, Correlation Coefficient (r) and Coefficient of Determination (R²) is given for the measurement of the indicators of industrial growth such as Number of Factories, Fixed Capital, Number of Workers, and Wages to Workers, Total Inputs, Value of Output and Profits.

The Null Hypothesis has been checked by significance T-test of Mean in the common group of industries selected by changing NIC codes during 30 years of this study period- pre and post economic reforms- on the basis of the Annual Survey of Industries- Two digit NIC classifications.
In chapter Six, titled “Comparative study of Industrial Development of Gujarat and other states- common geographical perspective states and other developed states”, a comparative study is made between Gujarat and common geographical perspective states (such as Maharashtra, Rajasthan and Madhya Pradesh) and other developed states (such as Maharashtra, Andhra Pradesh, Karnataka and Tamil Nadu).

An analysis of the indicators of industrial growth such as Number of Factories, Fixed Capital, Number of Workers, and Wages to Workers, Total Inputs, Value of Output and Profits is made by measurements of central tendency and dispersion such as Average, Standard Deviation and Coefficient of Variation (C.V.) for the pre and post economic reforms.

Besides this, the Null Hypothesis has been checked by One Way Analysis of Variance (ANOVA) technique of statistical analysis for Gujarat and other developed states. Here, an attempt is made to study the changes in three indicators of industrial growth- Number of Workers, Fixed Capital and Profit for Gujarat and other developed states.

In chapter Seven, titled “Conclusion”, an attempt is made to integrate various threads of analysis developed in earlier chapters pertaining to – “A comparative Analysis of Regional Industrial Development: Pre and Post Economic Reforms with Special Reference to Gujarat”. This chapter has been divided in three parts. Part one, presents brief summary of the analysis in the study, Part two, discusses Findings and Suggestions of the study and Part three, briefly deals with the limitations of the study and points out the areas for further research in this field.