ECONOMIC REFORMS (LPG)

LIBERALISATION, PRIVATISATION AND GLOBALISATION

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Economic Crisis in 1991

- Crisis in India is figured out because of the inefficient management in the Indian economy in 1980s. The revenues generated by the government were not adequate to meet the growing expenses, So, the government resorted to borrowing to pay for its debts and was caught in a debt-trap.

Causes of Economic Crisis

- 1) The continued spending on development programmes of the government did not generate additional revenue.
- 2) The government was not able to generate sufficient funds from internal sources such as taxation.
- 3) Expenditure on areas like social sector and defence do not provide immediate returns, so there was a need to utilize the rest of the revenue in a highly effective manner, which government failed to do so.

Causes of Economic Crisis

- 4) The income from public sector undertakings was also not very high to meet the growing expenditures.
- 5) Foreign exchange borrowed from other countries and international financial institutions was spent on meeting consumption needs and to make repayment on other loans.

What is the Need for Economic Reforms

- The economic policy followed by the government up to 1990 failed in many aspects and landed the country in an unprecedented economic crisis. The situation was so alarming that India's foreign reserves were barely enough to pay for two weeks of imports. New loans were not available and NRIs were withdrawing large amounts. There was an erosion of confidence of International investors in the Indian economy.

- The Following Points Highlight the Need for Economic Reforms in the Country

1) Increasing fiscal deficit.
2) Adverse balance of payments.
3) Gulf crisis.
4) Rise in prices.
5) High rate of deficit financing.

Emergence of New Economic Policy (NEP)

- Finally, India approached International Bank for Reconstitution and Development, popularly known as World Bank and International Monetary Fund (IMF) and received $7 million as a loan to manage the crisis. International agencies expected India to liberalize and open up economy by removing restrictions on private sector and remove trade restrictions between India and Foreign countries.

- India agreed to the Conditions of world bank and IMF and had announced new economic policy which consist of wide range of economic reforms.

LIBERALISATION

- Liberalisation was introduced to put an end to these restrictions and open various sectors of the economy. It is generally defined as loosening of government regulations in a country to allow for private sector companies to operate business transactions with fewer restrictions. In relation to Developing countries this refers to opening of economic borders for multinational and foreign investment.

Economic reforms under Liberalisation

Deregulation of Industrial sector:

In India, the following steps were taken to deregulate the industrial sector.

- i. Abolition of Industrial Licensing
  government abolished the licensing requirement of all Industries, except for the five Industries which are: Liquor, Cigarettes, Defence equipment, Industrial explosives, Dangerous chemicals and pharmaceuticals.

- ii. Contraction of Public Sector: The number of industries reserved for the public sector was reduced from 17 to 8. Presently only three Industries are ‘reserved for public sector’. They are Raliways, Atomic Energy and Defence.
- iii. De-reservation of Production Areas: The production which were early reserved for SSIs were de-reserved.
- iv. Expansion of Production Capacity: The producers were allowed to expand their production capacity according to market demand. The need for licensing was abolished.
- v. Freedom to Import Capital Goods: The business and Production units were given freedom to import capital goods to upgrade their technology

- **2) Financial Sector Reforms:**

- It includes Financial Institutions such as Commercial banks, Investment Banks, Stock exchange operations and Foreign exchange Market.

- **3) Tax Reforms:**

- Tax reforms are concerned with the reforms in the government's taxation and public expenditure policies, which are collectively known as its fiscal policy. Since 1991, there has been a continuous reduction in the taxes on individual incomes as it was felt that high rates of income tax were an important reason for tax evasion.

- **4) Foreign Exchange Reforms:**
- It includes reforms relating to foreign exchange and foreign trade

- **5) Trade and Investment Policy Reforms:**
- Liberalisation of trade and investment regime was initiated to increase international competitiveness of industrial production and also foreign investments and technology into the economy.

PRIVATISATION

- It implies shedding of the ownership or management of a government owned enterprise. Government companies are converted into private companies. Privatisation of the public sector enterprises by selling off part of the equity of PSEs to the public is known as disinvestment.

GLOBALISATION

- It means integration of the economy of the country with the world economy. Globalisation encourages foreign trade and private and institutional foreign investment. Globalisation is a complex phenomenon as it is an outcome of the set of various policies that are aimed at transforming the world towards greater interdependence and integration.

OUTSOURCING

- This is one of the important outcomes of the globalisation process. In outsourcing, a company hires regular service from external sources, mostly from other countries, which was previously provided internally or from within the country (like legal advice, computer service, advertisement, security — each provided by respective departments of the company).

3. AN APPRAISAL OF LPG POLICIES

Briefly referred to as LPG policies, the term implies policies related to liberalisation (L), privatisation (P) and globalisation (G). An appraisal of LPG policies implies an appraisal of NEP (New Economic Policy) or an appraisal of Economic Reforms initiated since 1991. Appraisal of LPG or NEP requires that the reader appreciates or understands the merits and demerits of this policy with reference to the Indian economy.

Merits of the LPG Policies

Following observations highlight the merits of LPG policies:

(1) **Vibrant Economy:** Indian economy has definitely become a more vibrant economy. Overall level of economic activity has trended up as indicated by GDP growth. Post LPG policies, the growth of GDP shot up to as high as 8 per cent per annum.

(2) **Stimulant to Industrial Production:** LPG policies have worked as a great stimulant to industrial production in the Indian economy. It is owing to these policies that IT industry in India has achieved global recognition.

(3) **A Check on Fiscal Deficit:** Mounting fiscal deficit has been a serious threat to the process of investment in the Indian economy.

From as high as 8.5 per cent of GDP has been brought down to around 3.5 per cent of GDP.

(4) **A Check on Inflation:** Owing to a greater flow of goods and services in the economy, rate of inflation has been lowered.

In the years 2011-12 to 2013-14, inflation was in the range of 6-9 per cent per annum.

For year 2018-19, it is estimated to be 3.4 per cent.

It may be noted that high inflation leads to a rise in interest rate, implying a rise in the cost of investment. Accordingly, growth rate is adversely impacted.

(5) **Consumer's Sovereignty:** Consumers sovereignty has expanded over time. This is evident from the fact that a large variety of goods and services from the diverse global markets are now within the easy reach of the buyers.

Producers are widely responding to the consumers choice and preference.

Consequently, overall level of expenditure of the households has tended to rise. Implying an overall rise in the welfare status of the people.

(6) **A Substantial Increase in Foreign Exchange Reserves:** Depletion of forex reserves was one of the compelling reasons for the government to shift to LPG policies.

Thanks to these policies, forex reserves of the country have now reached a comfortable level.

Good amount of forex reserves enhances economic confidence of the global investors in the Indian markets.

(7) **Flow of Private Foreign Investment:** Private foreign investment has taken a quantum jump after the adoption of LPG policies.

This has been a matter of great relief to the government in view of the facts that:

(i) domestic economy was not generating enough of surplus for reinvestment, and

(ii) indigenous technology was getting obsolete.

It is significant to note that private foreign investment is often accompanied with innovative techniques of production.

(8) **Recognition of India as an Emerging Economic Power:** It is owing to LPG policies and the consequent rise in the overall level of economic activity, that India is now being recognised as an emerging economic power in the world.

This recognition (particularly by developed nations of the world) not only raises India's economic ranking in the world, but also boosts confidence of the global investors in the Indian economy as their preferred destination of investment.

(9) **A Shift from Monopoly Market to Competitive Market:** Launch of LPG policies has caused a significant shift in the structure of the Indian markets.

Indian markets are now increasingly shedding its monopolistic character, and becoming more and more competitive in nature.

For instance, a couple of decades back, products like cars, refrigerators, ACs and PCs were the monopoly markets of select brands only. Now a variety of these products are available at competitive prices.

Briefly, owing to LPG policies, the Indian economy has definitely gained a 'growth momentum'. The process of growth has not only accelerated, but has also become more diversified. There is a definite change in welfare level of the people. Recognition of the Indian economy as an emerging economic power in the world is of crucial significance.

Demerits of LPG Policies

All that glitters is not gold. There is a negative side of the story as well. Following observations highlight demerits or negative impact of LPG policies in India:

(1) **Neglect of Agriculture:** Post New Economic Policy (NEP) of 1991, growth of GDP has largely been driven by the secondary and tertiary sectors of the economy.

Agricultural sector has suffered a serious neglect and its growth rate has slided/slipped to a miserably low level (2-3 per cent per annum). This has led to a widening gulf between the rural and urban economies. Implying the spread of poverty.

In fact, slow growth of agricultural sector must ultimately hinder the process of growth of the industrial sector as well. This is because:

(i) Agricultural sector is an important source of raw material for the industrial sector.

(ii) Agricultural sector is the principal source of labour supply to the industrial sector, and

(iii) Agricultural sector is a significant source of demand for the industrial products like tractors and thrashers.

Economic and Social Dualism

- **Economic Dualism:** It refers to disintegration of the economy into traditional and modern sectors of production. While the traditional sector relies upon traditional technology, the modern sector is driven by modern technology.
- **Social Dualism:** It refers to disintegration of the society into 'haves' (enjoying high social status) and 'have-nots' (living with low social status).

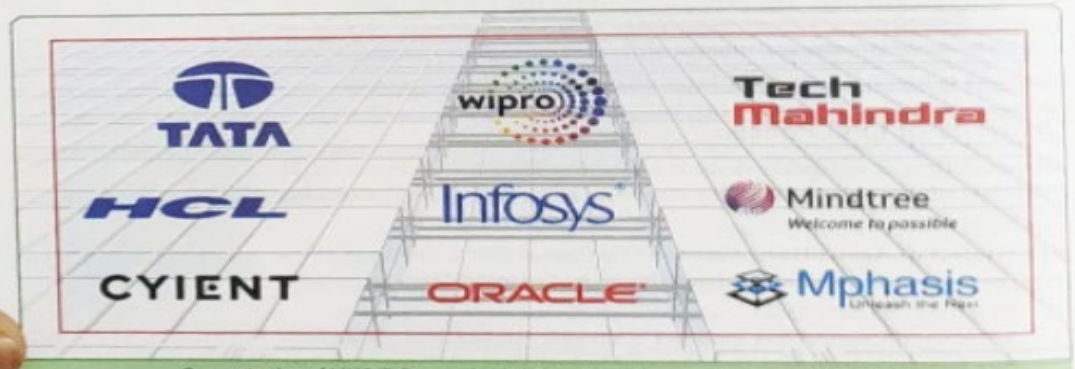
(2) **Urban Concentration of Growth Process:** LPG policies have resulted in the concentration of growth process in urban areas.

Think of any MNC, you will hardly find its trace in the rural areas of the country.

All MNCs are focusing only on urban areas, where they find conducive infrastructural facilities. This has further widened the 'rural-urban gulf'.

Rural-urban gulf implies economic dualism which deepens social dualism as well.

Economic and social dualism are always a big threat to the process of growth and development.



Concentration of MNC IT Companies in Urban Areas deepens the 'Rural-Urban Gulf'

(3) **Economic Colonialism:** India suffered nearly 200 years of political colonialism during the British rule.

Now, while MNCs are expanding their economic control, we might suffer a sort of economic colonialism.

Implying a situation where MNCs are exploiting the Indian markets to sell their products and in the process, domestic producers are marginalised owing to their poor competitive strength.

(4) **Spread of Consumerism:** Spread of MNCs in the country as a consequence of LPG policies has resulted in a large-scale spread of consumerism.

A variety of global brands in the market has induced the masses to become spendthrift, going beyond their means.

The Indian society is adapting itself to the western culture of spending through borrowing.

This may expand size of the market for the traders and the manufacturers, but certainly enhances vulnerability of the households as consumers.

(5) **Lopsided Growth Process:** LPG has accelerated the growth process of the Indian economy, but it is lopsided.

It is not an inclusive growth process. It does not include all the sectors of the economy. Instead, it is increasingly relying on 'service sector' of the economy.

In fact, it is just an 'IT-focused' growth process which is gradually over-shadowing the process of industrialisation, besides neglecting the farming sector.

It is alarming to note that, owing to liberalisation and globalisation, the Indian farmer is shifting to the production of cash crops for the foreign markets, causing a shortfall of domestic supplies of foodgrains.

Alas! We are often forced to import foodgrains despite Green Revolution.

Rising prices of food products towards the end of 2009 should serve as a wake up call to the fact that LPG policies are almost neglecting the farming sector of the economy.

(6) **Cultural Erosion:** Globalisation has also led to cultural erosion in the Indian society. Following are some significant observations in this context:

- Economic prosperity has taken a lead over all other parameters of life.