UNIT 26 GLOBALISATION*

Structure

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26.1 INTRODUCTION

While on the one hand the Indian economy in the 1980s seemed to be doing quite well, (see **Unit 22**) on the other hand there were certain long-term structural constraints building up which were to all add up to a major crisis by 1991 when the country was on the verge of defaulting. Also new global opportunities were emerging which urgently needed to be taken advantage of through economic reform. It is the crisis in the Indian economy along with the global opportunities which brought home to the country the immediate necessity of bringing about structural adjustment and economic reform.

26.2 STRUCTURAL CONSTRAINTS

Broadly there were three sets of problems which had gathered strength in the Indian economy over time and which needed urgent reform.

First, the excessive state intervention in the so called 'licence-quota raj' was leading to the creation of tremendous inefficiency. Prolonged protection to Indian industry from imports through high tariff barriers and import quotas, following the import substituting industrialisation (ISI) strategy, led to the killing of external competition. Similarly, industrial licensing effectively prevented free internal competition. In the absence of internal and external competition Indian industry began to become increasingly inefficient. Other regulations such as the MRTP Act further inhibited industrial development. The Act went against the basic principle of economies of scale, which is at the heart of capitalist development (or for that matter of socialist production). It also punished efficiency, as any company, which expanded due to efficient production, good management and research and development (R & D), would face severe restrictions, including refusal of permission to increase capacity once it crossed a prescribed limit. Again, reserving certain areas for small-scale industries meant excluding these areas from the advantages of scale and larger resources for R & D activities. This made the sector often internationally uncompetitive, leading to India losing out to its competitors in many areas. Also, the policy towards small-scale industry forced entrepreneurs in the reserved areas to remain small, as any expansion as a result of efficient and profitable functioning would deny the enterprise the special incentives and concessions. This inhibited efficiency and innovation in this sector.

Second, the large public sector in India, which controlled 'the commanding heights' of the economy, also began to emerge as a major source of inefficiency. The early emphasis on the public sector was critical to India's industrial development. It is the public sector which entered the core areas, diversified India's industrial structure, particularly with regard to capital goods and heavy industry, and reduced India's dependence on foreign capital, foreign equipment and technology. However, over time, the political and bureaucratic pressure on the public sector undertakings gradually led to most of them running at a loss. They were overstaffed, often headed by politicians who had to be given sinecures, became

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victims of irresponsible trade unionism and were unable to exercise virtually any efficiency accountability on their employees. State run utilities like Electricity Boards and Road Transport Corporation were notorious for incurring enormous losses. Apart from rampant corruption and lack of accountability, these enterprises, under populist pressure, often charged rates that did not cover even a small fraction of the actual costs. The free distribution of electricity being an extreme case in point.

All these factors led to the investment efficiency in India being very low or the capital output ratio being very high. A 1965 study shows that the public sector Heavy Electrical Limited was set up in Bhopal with a capital output ratio of between 12 to 14 – with no questions being asked or enquiry set up! Though this is an extreme case, estimates for the economy as a whole show that the capital used per unit of additional output or the incremental capital output ratio (ICOR) kept rising, it being a little over 2 during the First Plan and had reached 3.6 during the Third Plan. According to one estimate between 1971 and 1976 the ICOR had touched a high of 5.76. This explains why despite substantial increases in the rate of investment, as shown in **Unit 22**, there was an actual decrease in the overall growth rates of aggregate output or GDP between the 1950s and 1970s. The ICOR started declining in the 1980s though it still remained around 4 in the 1990s. Even during the 1980s, one estimate shows that the (simple) average rate of financial return on employed capital in public sector enterprises was as low as 2.5 per cent. Actually, the rate of return was much lower if the 14 petroleum enterprises were excluded, as these accounted for 77 per cent of the profits in 1989-90.

Low efficiency or low productivity levels are of critical consequence as economic superiority is established and transfer of surplus from one country to another occurs not any more through direct political or economic domination but through processes such as unequal exchange occurring between countries with different productivity levels. Economic thinkers of the Left and the Right are agreed on placing the question of productivity at the centre of any national development. In today's context of rapid globalisation, pursuing excessively autarchic policies in search of autonomy may, through fall or stagnation of productivity levels, destroy precisely that autonomy and push the country towards peripheralisation.

This brings us to the third set of weaknesses that emerged in the India economy. It relates to the continuation of the inward oriented developmental path followed by India since independence. India failed to make a timely shift from the export pessimism inherent in the first three plans, a pessimism which, one must recognise, was shared widely by development economists the world over in the 1950s. The failure lay not in adopting the policies that emerged from the wisdom of the 1940s and 1950s but in the inability to quickly react to changes occurring in the international situation and to world capitalism after World War II, particularly since the 1960s and 1970s, and change course accordingly.

26.3 GLOBAL OPPORTUNITIES

Some of the important changes that needed to be taken cognisance of were, very briefly, the following:

First, the nature of foreign capital and multinational corporations was changing. A process of 'internationalisation of production' had started. Multi- national corporations, instead of just looking for markets or sources of raw material, now looked for cheaper production areas. Instead of creating enclaves in the backward countries, which had backward and forward linkages with the home country (this was the typical colonial pattern), they were now bringing in investments which had major multiplier effects on the local economy, including of technology transfer. It became common for multi-national companies to 'source' a large part of the components that went into the final product from all over the developing world and even shift entire production plants to the under-developed countries.

Second, along with, and partially as a result of, the above process, there were massive capital transfers between countries, reminiscent of the capital transfers of the 19th century at the height of colonial expansion, but very different in character. The above two processes

contributed to the third major international development, that of an unprecedented explosion of world trade. Between the 1950s and 1970s, world output of manufactures increased four times but world trade in manufactures increased ten times. The percentage of world produce that went for export doubled between 1965 and 1990. What is most significant is that while there was a massive increase in global industrial exports, the Third World was able to rapidly increase its share of total industrial exports, especially since the 1970s, from about 5 per cent in 1970 to double the figure in 1983. (See Hobsbawm, 1994, for a brilliant analysis of the changes in world capitalism since World War II.)

The East Asian Miracle, i.e., the rapid industrialisation of the East Asian countries, beginning in the 1960s, which gradually shifted the industrial base of the world from the West to the East, took advantage precisely of these kinds of opportunities of capital and market availability. Japan's example of explosive post-World War II growth was being repeated by South Korea, Taiwan, Singapore, Hong Kong and, more recently, Thailand, Malaysia, China and Indonesia. The four Asian Tigers, South Korea, Hong Kong, Singapore and Taiwan increased their share in world export of manufactures from 1.5 per cent in 1965 to 7.9 per cent in 1990. Even the newly industrialising economies (NICs), Indonesia, Malaysia and Thailand increased their share form 0.1 per cent to 1.5 per cent over the same period.

India did reasonably well till the mid-1960s, basing herself on an inward oriented, import-substitution based strategy. However, she failed to respond adequately to the new opportunities thrown up by the changing world situation despite the availability of the East Asian experience. In fact India's share in world exports actually shrunk from about 2.4 per cent in 1948 to 0.42 per cent in 1980, rising to a still paltry 0.6 per cent by 1994. In contrast, South Korea's manufactured exports, which were negligible in 1962, amounted to four times those of India by 1980. The volume of India's manufactured exports in 1980-81 was 1/2 that of China, 1/3 of Brazil and 1/4 of South Korea.

India was thus unable to use the opportunities provided by the changed world situation, the new phase of globalisation, to rapidly industrialise and transform its economy, increase income levels and drastically reduce poverty levels, as did many of the East Asian countries.

The fourth set of problems, which overcame the Indian economy, was primarily the result of certain political imperatives, which related to the manner in which the Indian state structure and the Indian democratic framework evolved. On the one hand there was the emergence of more and more sections which made strong, articulate demands on state resources and on the other the governments were increasingly unable either to meet these demands fully or diffuse the clamour for them. This resulted in the gradual abandoning of fiscal prudence from about the mid-1970s. This in turn led to a situation where the macroeconomic balance (such as balance between government revenue and expenditure or balance between exports of goods and services and the liabilities caused by imports of goods and services as well as foreign borrowings), which was maintained in India (unlike many other developing countries) with great caution for the first 25 years or so after independence, was being slowly eroded.

The gradual erosion of fiscal prudence was reflected in government expenditure rising consistently, mainly because of the proliferation of subsidies and grants, salary increases with no relationship to efficiency or output, overstaffing, and other 'populist' measures such as massive loan waivers or making huge budgetary allocations which were aimed at winning over support of a particular section of society rather than at achieving best overall development.

While the response to the mid-1960s crisis was fiscal and balance of payments caution, relaxation of fiscal discipline became rampant after 1975 and particularly during 1977-79. The food subsidies doubled between 1975-76 and 1976-77 from Rs. 2.5 billion to Rs. 5 billion. The fertiliser subsidy multiplied ten times from Rs. 0.6 billion in 1976-77 to Rs. 6.03 billion in 1979-80. The export subsidy multiplied by about 4 1/2 times from Rs.0.8 billion to Rs. 3.75 billion between 1974-75 to 1978-79. During 1977-79 procurement prices for foodgrains were increased without corresponding increases in issue prices, taxes on a wide range of agricultural inputs were decreased and budgetary transfers to loss making

public sector units increased. In fact, the 1979 budget has been described by eminent economists Vijay Joshi and I. M. D. Little (1994: 58) as a "watershed marking the change from previous fiscal conservatism."

The fiscal profligacy continued through the 1980s and particularly during the second half of the 1980s reaching absurd limits where, in 1989 government announced a loan waiver for the farmers which would cost the exchequer more than Rs. 100 billion. The direct subsidies from the central budget on only food, fertiliser and exports in 1980-81 have been estimated to exceed Rs. 15 billion, an amount representing nearly half of the total gross capital formation or investment in manufacturing in the public sector that year! While there was this explosive growth of Government spending, the savings generated by the Government or public sector kept falling with their growing losses.

The result of this fiscal profligacy was that the consolidated Government (centre and states) fiscal deficits or the revenue and expenditure gap rose sharply from 4.1 per cent of GDP in 1974-75 to 6.5 per cent in 1979-80, 9.7 per cent in 1984-85, peaking at 10.4 per cent in 1991. Governments in this period tended to seek ways and means of increasing their domestic and foreign borrowing to meet this deficit rather than either trying to increase government savings or reduce government expenditure.

The growing government saving-investment gap and the fiscal deficit had a negative impact on the balance of payments and debt situation, as the Government resorted to heavy borrowing to meet this gap. From a situation of balance of payments surplus on the current account in 1977-78 of $ 1.5 billion (1.4 per cent of GDP), by 1980-81 there was a deficit in the current account to the tune of $ 2.9 billion (1.7 per cent of GDP). The deficit increased to $ 3.5 billion (1.8 per cent of GDP) in 1984-85 and rose very sharply there after to $ 9.9 billion (3.5 per cent of GDP) in 1990-91.

The deteriorating fiscal and balance of payments situation had led to a mounting debt problem, both domestic and foreign, reaching crisis proportions by the end of the 1980s. Total Government (centre and state) domestic debt rose from 31.8 per cent of GDP in 1974-75 to 45.7 per cent in 1984-85 to 54.6 per cent in 1989-90. The foreign debt situation also became very precarious with debt rising from $23.5 billion in 1980-81 to $37.3 billion in 1985-86 to $83.8 billion 1990-91. The debt-service ratio (i.e., payment of principal plus interest as a proportion of exports of goods and services) which was still a manageable 10.2 per cent in 1980-81 rose to a dangerous 35 per cent in 1990. India's foreign exchange reserves fell from $ 5.85 billion in 1980-81 to $ 4.1 billion in 1989-90, and in the next year they fell drastically by nearly half to $ 2.24 billion in 1990-91, enough only for one month's import cover. The Iraqi invasion of Kuwait in August 1990, leading to an increase in oil prices and a fall in Indian exports to the Middle East or Gulf region, partly contributed to this alarming foreign exchange situation. India's international credit rating was sharply downgraded and it was becoming extremely difficult to raise credit abroad. In addition NRI (non-resident Indian) deposits in foreign exchange began to be withdrawn rapidly. In such a situation, where foreign lending had virtually dried up, the government was forced to sell 20 tonnes of gold to the Union Bank of Switzerland in March 1991 to tide over its immediate transactions. By July 1991 foreign exchange reserves were down to a mere two weeks import cover despite loans from the IMF. The country was at the edge of default.

This is the situation (June 1991) in which the minority Congress government of Narasimha Rao took power and with Manmohan Singh as finance minister one of the most important economic reforms since independence were attempted.

26.4 ECONOMIC REFORMS SINCE 1991 LIBERALISTION AND GLOBALISATION

The long-term constraints building up over a few decades that were debilitating the Indian economy combined with certain more recent and immediate factors to lead to a massive fiscal and balance of payments crisis, climaxing in 1991. The crisis pushed India into initiating a process of economic reform and structural adjustment.

The need for reform had been recognised early enough in India. Manmohan Singh Jagdish Bhagwati (1970&1994) and others had been arguing for it since the1960s and 70s. Efforts at reform and liberalisation began since the 1980s if not earlier, but, its comprehensive implementation could not occur for various reasons. Governments, especially when in a vulnerable situation were extremely wary of initiating or sustaining reforms which would involve introducing unpopular measures like attempts to regain fiscal discipline, change in labour laws, etc., steps which in the initial phase were bound to be painful. Also, there was (and still remains) persistent opposition to reform from vested interests such as the bureaucracy and even sections of business who benefited from the existing system of controls, using them to earn a sort of 'rent'. Last and certainly not the least, a strong ideological opposition from the orthodox Left, strangely oblivious to the changing global reality, continued to play a role in obstructing reform.

The crisis in 1991, with the country at the edge of default, enabled the government to break through the traditional mindset and attempt an unprecedented comprehensive change at a time when both the ideological opposition and the resistance of the vested interests was at a weak point. Thus, though late, nearly thirteen years after China changed course, a programme of economic reform was initiated in 1991. One reason why the shift took so long and, even when it took place, was not as sharp a turnaround as it was in China in 1978 or the Soviet Union after the mid 1980s was that in a democracy the change from one kind of societal consensus (such as the Nehruvian consensus) to a new consensus (say around reforms) is a process and not an event, and consequently it has its own dynamic, very different from that operating in a non-democratic or totalitarian society. While arriving at a democratic consensus is more time consuming, once a consensus is arrived at it is far more durable or stable than changes brought about by force from the top.

The process of reforms started in 1991 involved, inter alia, an immediate fiscal correction; making the exchange rate more realistically linked to the market (the Rupee underwent about a 20 per cent devaluation at the very outset); liberalisation of trade and industrial controls like freer access to imports, a considerable dismantling of the industrial licensing system and the abolition of MRTP; reform of the public sector including gradual privatization; reform of the capital markets and the financial sector; removing a large number of the restrictions on multinational corporations and foreign investment and in fact welcoming them, particularly foreign direct investment, and so on. In short it was an attempt to free the economy from stifling internal controls as well as equip it to participate in the worldwide globalisation process to its advantage.

The record of the first few years of reform was creditable by any standards, though a lot of problems and challenges still remained. India performed one of the fastest recoveries from a deep macroeconomic crisis. Moreover, the process of structural adjustment, particularly the fiscal reining-in (done initially), was achieved with relatively minimal pain – without it setting off a prolonged recessionary cycle leading to massive unemployment and deterioration of the condition of the poor as was feared and as occurred in the case of several other economies in a similar situation attempting structural adjustment.

For example, the growth rate of India's Gross Domestic Product (GDP) which had fallen to a paltry 0.8 per cent in the crisis year of 1991-92 recovered quickly to 5.3 per cent by 1992-93 and rose further to 6.2 per cent in 1993-94 despite some disturbances in 1992-93 emergent. More important, over the next three years, the Indian economy averaged an unprecedented growth rate of over 7.5 per cent, a rate closer to the high performers of East Asia than it had ever been before. Despite the crisis and the necessary structural adjustment, the Eighth Plan (1992-1997) averaged a growth rate of nearly 7 per cent (6.94), higher, and on a more sustainable basis, than the Seventh Plan (1985-1990) average of 6 per cent. Gross Domestic Savings averaged over 23 percent between 1991 and 1997, higher than the Seventh Plan average of 20.6 per cent. Gross Domestic Capital formation (Investment) and Gross Domestic Fixed Capital Formation between 1992 to 1997 also maintained a respectable average of 25.2 per cent and 22.3 per cent of GDP respectively, considerably higher than the Seventh Plan average of 21.8 and 19.8 per cent.

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Industrial production, which showed a dismal, less than one per cent, growth rate in 1991-1992 (it was negative in manufacturing), picked up to 2.3 per cent in 1992-1993 and 6 per cent in 1993-1994, peaking at an unprecedented 12.8 per cent during 1995-1996. The capital goods sector, which demonstrated negative growth rates for a few years, bounced back to nearly 25 per cent growth in 1994-1995, allaying early fears that import liberalisation would hit the domestic capital goods industry adversely. The small-scale sector too grew faster than overall industrial growth, suggesting that abolition of MRTP did not have an adverse effect on it and perhaps encouraged its growth. Agriculture, too, after recording a fall in 1991-92, picked up the following year and by and large maintained till 1996-1997 the high rate of growth of over three per cent which it had been experiencing for some years.

The Central Government fiscal deficit, which had reached 8.3 per cent of GDP in 1990-1991, was reduced and averaged roughly 6 per cent between 1992-1997. The important thing was that out of the total fiscal deficit of 5.2 per cent in 1996-1997, 4.7 per cent was accounted for by interest payments which was a liability emanating from past fiscal laxity. The primary deficit, i.e., fiscal deficit net of interest payments, which represents current fiscal pressures or overspending was only 0.6 per cent in 1996-1997, systematically brought down from 4.3 per cent of GDP in 1990-91 and 2.9 per cent in 1993-1994.

The external sector also showed considerable improvement. Exports, which registered a decline of 1.5 per cent in dollar terms during 1991-1992, recovered quickly and maintained an average growth rate of nearly 20 per cent between 1993-1996. Very significantly, India's self reliance was increasing to the extent that a considerably larger proportion of imports were now paid for by exports, with the ratio of export earnings to import payments rising from an average of 60 per cent in the 1980s to nearly 90 per cent by the mid 1990s. The current account deficit in balance of payments, which had reached an unsustainable 3.2 per cent of GDP in 1990-91, was brought down to 0.4 per cent in 1993-1994 and rose since then to 1.6 per cent in 1995-96. Yet the average deficit between 1991-92 and 1997-1998 was about 1.1 percent, significantly lower than the Seventh Plan (1985-90) average of about 2.3 per cent. The foreign exchange reserves (including gold and SDRs) had grown to a respectable $ 30.4 billion at the end of January 1999, providing cover for about 7 months of imports as compared to a mere two weeks cover in July 1991.

The debt situation has also started moving away from a crisis point. The overall external debt/GDP ratio for India fell from a peak of 41 per cent in 1991-92 to 28.7 per cent in 1995-1996. The debt service ratio also fell from the peak of 35.3 per cent in 1990-1991 to 19.5 per cent in 1997-98. It was however still quite high compared to China, Malaysia and South Korea, who all had (till 1997) debt service ratios below 10 per cent.

Reforms and liberalisation of the stock market since the 1980s and particularly after 1991 produced dramatic results. The total market capitalisation on the Indian stock markets as a proportion of GDP rose from a mere 5 per cent in 1980 to 13 per cent in 1990 and, following further reforms since 1991, it rose rapidly to 60 per cent of GDP by the end of 1993. By 1995 the Indian stock market was the largest in the world in terms of the number of listed companies – larger even than the US. The amount of capital Indian companies could raise in the primary market in India increased from Rs 929 million in 1980 to Rs 2.5 billion in 1985 and Rs 123 billion in 1990. By 1993-4 the figure had reached Rs 225 billion – a nearly 250 times increase since 1980. (Ajit Singh, 1998)

The encouragement to foreign investment bore fruit with foreign direct investment (FDI) increasing at nearly 100 per cent per year between 1991 to 1996, it being $ 129 million in 1991-1992 and $2.1 billion in 1995-1996. Total foreign investment including portfolio investment increased from $ 102 million in 1990-91 to $ 4.9 billion in 1995-1996. Considerable improvement no doubt but yet a far cry from what was being achieved by the East Asian countries. China alone had been absorbing more than $ 30 billion of foreign direct investment every year for some years, the figure for 1996 being $ 40.8 billion. One positive sign however was that one of the most stubborn mind sets – the xenophobia about foreign capital – seems to have been eroded, With the Common Minimum Programme (CMP) of the coalition government (following the defeat of the Congress in 1996), to

which even the Communists were a party, desiring that the foreign direct investment (FDI) in India should rise to $ 10 billion per year. However, the danger emanating from the relatively volatile nature of foreign portfolio investments, with the possibility of their sudden withdrawal (as happened in Mexico and more recently in south- east Asia) due to often unpredictable extraneous factors, was understood by successive Governments and efforts made to control short-term capital inflows and capital flight.

Critics of reform, mainly from the orthodox Left, have made the charge that reform was anti-poor. Studies of a large number of countries have shown that barring a few exceptions, rapid economic growth has been associated with fall in poverty levels. India too witnessed significant fall in poverty levels with the relatively faster economic growth of the 1980s. The proportion of population below the poverty line (the poverty ratio) fell from 51.3 per cent in 1977-1978 to 38.9 per cent in 1987-1988. Countries like China and Indonesia, which had much higher poverty ratios of 59.5 and 64.3 in 1975 compared to India's 54.9 in 1973-1974, were able to reduce their poverty levels to much below India's in the span of twenty years. These countries maintained a much higher rate of growth than India during this period and their poverty ratios had fallen dramatically to 22.2 and 11.4 respectively by 1995, while India's had fallen only to 36 by 1993-1994. (*Economic Survey 1998-1999*, Government of India, Tables 10.6 and 10.7: 146.)

To the extent, therefore, that the economic reforms were designed to put India on a higher growth path, it would be expected that poverty levels would decline as well. The key question remaining was what would be the impact on poverty in the transitional phase, especially when the necessary stabilisation had to take place with the attempts to improve the balance of payments position and reduce the fiscal deficit, leading to a possible fall in Government expenditure. India's initial stabilisation programme was said to be "extraordinarily successful" causing "remarkably little suffering" when "compared with most other countries, which were forced to effect a large and rapid reduction in their current external account deficits." (Joshi and Little, 1996, pp. 222,225.) Calculations based on several different indicators of poverty show that poverty, mainly rural poverty, showed a significant rise only in 1992-1993 and its causation was linked mainly to a drought and fall in foodgrain output in 1991-1992, leading to a rise in food prices, and very weakly to the stabilisation programme. Even this was perhaps avoidable to a great extent and the government's failure in not anticipating the situation and maintaining expenditure on rural employment programmes, and its not refraining from making any cuts (in real terms, there being a nominal increase) in the anti-poverty Social Services and Rural Development (SSRD) expenditure in 1991-1992 to achieve fiscal stabilisation, has been criticised even by the supporters of reform. However, all the poverty indicators showed that by 1993-1994 there was much improvement in the poverty situation. The poverty levels, both rural and urban, were significantly lower in 1993-94 than in 1992, by nearly six percentage points, and were lower than the pre-reform average of the five years 1986-1987 to 1990-1991. (Tendulkar, 1998, Tables 12.1, 12.2, 12.3, pp. 290-294.) Thus it may be noted that the stabilisation under the reforms had little negative impact, if any, on poverty levels. Other aspects of structural reform, it is generally agreed, do not threaten the poor and in fact would improve their condition by releasing the full growth potential of the economy.

The improvement in the poverty situation was helped by the fact that the government increased the overall expenditure on Social Services and Rural Development since 1993-1994 – from 7.8 per cent of total Government (Central) expenditure in 1992-93 to an average of nearly 10 per cent between 1993 and 1998. Real agricultural wages, which had decreased by 6.2 per cent in 1991-1992, grew in the next two years at over 5 per cent per year and had by 1993-4 surpassed the pre-reform level. After the low of 1991-1992, additional employment generated in the total economy rose to 7.2 million in 1994-1995, averaging about 6.3 million jobs every year between 1992-1993 and 1994-1995, considerably higher than the average annual increase of 4.8 million in the 1980s. Moreover, inflation, which hurts the poor the most, was kept under control. The annual rate of inflation, which touched a high of 17 per cent in August 1991, was brought down to below 5 per cent in February 1996.

However, though on the whole the reform initiatives look quite successful, there is still a long way to go. Continued political instability, aggravated by no clear majority emerging in parliament of any political party, has made it difficult for any government to move away from populist measures and take tough but necessary decisions. That is why no serious efforts were made to increase public savings and reduce government expenditure and the problem of high fiscal deficits continued.

One of the most dangerous reversals is in the sphere of fiscal deficit, where the primary deficit which had been brought down to 0.6 per cent of GDP in 1996-1997 (0.5 percent in the new series data used in *Economic Survey of 1998-1999*) more than doubled to 1.3 per cent in 1997-1998 and for the Centre and States together it was estimated to be 2.4 per cent (revised estimate). The selective acceptance of the Fifth Pay Commission recommendations by the United Front government in 1997, whereby the government expenditure on salaries was to increase very sharply without any compensatory savings, as the measures suggested by the Commission to achieve such savings were not accepted, put further pressure on the fiscal deficit. The situation reached a point where, "given the serious fiscal slippage", even the Economic Survey of the Government of India of 1998-99 was constrained to argue, "the time has perhaps come to reconsider the issue of constitutional limits on the deficit." (*Economic Survey:* 11,18.)

Yet, it is a positive development of enormous significance in a democracy, that there is a broad consensus among all political parties from the Right to the Left (barring the extremists at both ends) that the reform process must continue, a consensus reminiscent of the one around the Nehruvian programme at independence.

The consensus is suggestive of the fact that economic reform or liberalisation did not mean a change of goals set at independence by the Indian people, such as rapid growth, industrialisation, self reliance, removal of poverty and so on. Liberalisation and participation in the globalisation process was not the "final surrender" to international capital or imperialism or the IMF-World Bank combine as has been argued ad infinitum by sections of the orthodox Left. On the basis of the experience with various controls and state intervention at home, of changes occurring in the world such as the collapse of the Socialist world, the new globalisation process after World War II and the experience of various fast growing economies in the recent past, the aspiration towards the same goals set out at independence required an altering of strategy.

However, this is not to say that the earlier 'Nehruvian' strategy was wrong. That strategy had its historical significance. As we saw, it gave the Indian economy a certain depth and spread, increased its bargaining power and independence, and lent the Indian economy and society the dignity it did not possess after the colonial experience. In fact it made the Indian economy capable of participating in the globalisation process without being swamped by it in a manner that the stronger economies in the global framework could establish a dominating or exploitative position vis-à-vis the Indian economy. However, over time, certain negative features developed, and the world context changed. To achieve the earlier goals, there was now a need for a shift in strategy. To give just one example, if self-reliance and rapid growth in the 1950s required import substitution and restrictions on capital and commodity movements, today capital and technology flows and through that keeping up efficiency or productivity levels is the route to self-reliance and rapid growth.

It is no accident that so many of the very people who created, outlined or subscribed to the earlier Nehruvian strategy over time saw the necessity of reform. We have, for example, the economists of the Nehruvian era K.N. Raj, Lord Meghnad Desai, Sukhamoy Chakravarty, C.H. Hanumantha Rao, Arjun Sengupta and Amartya Sen, all implementing or arguing for economic reform involving liberalisation and participation in the globalisation process, though with different approaches and in varying degrees.

There was, in other words, a growing recognition in India of the imperative to be responsive to the external changes and internal experience and change strategy so that this great country was able to come into its own and realise its enormous potential rather than fritter away the considerable achievements made since independence. There emerged a consensus on reforms involving liberalisation and participating in the globalisation process

with the same objectives of equity, growth and independence around which the erstwhile Nehruvian consensus had been constructed. The strategy to achieve those objectives was changed with the changing global and internal situation.

26.5 SUMMARY

Certain structural constraints to India's economic growth were manifesting themselves by the 1980s. These were linked to excessive protection and state control leading to a fall in productivity. The situation of crises was aggravated by a shift from a policy of fiscal prudence to fiscal profligacy. Expenditures outstripped revenues, fiscal deficits soared, the balance of payments situation deteriorated, debts mounted, foreign exchange reserves collapsed and India was at edge of default. The economic reforms of 1991 were initiated in this context.

Reforms meant an attempt at fiscal discipline, liberalization of trade and industrial controls. The industrial licensing system was dismantled, the public sector was reformed, and Foreign Direct Investments were welcomed. In the years after the reforms the growth rate of the Gross Domestic Product (GDP) recovered quickly, industrial production picked up, fiscal deficit was reduced, the overall external debt fell, the stock market boomed, and even poverty levels declined. Indian economy entered the age of globalization.

26.6 EXERCISES

1) What were the structural constraints which led up to the economic crisis of 1991?
2) Describe the new global opportunties that called for a change in economic strategy by India.
3) Account for the shift from the economics of 'fiscal prudence' to that of 'fiscal profligacy'. What were the implications of this shift?
4) Discuss the consequences of the economic reforms of 1991?

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