Indian Economy: Some Contemporary Perspectives
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Lecture-05
Indian Economy: Economic Planning 5

Hi everyone. So, we are going to start now with lecture five, and in this lecture, we will be dealing with post-reform period developments and the planning that we have. So, we will be discussing now eighth and ninth plan, and we will be also focusing on certain developments that we may be taking up later, because at this point I will be just giving you some basic introduction and then after that we will be dealing in detail.

For example, the measures were taken regarding disinvestment process, then we also had something called banking sector reforms. So, these two topics, and then we have the current account current convertibility, then capital account convertibility. So, government also gave emphasis on these two developments.

So, lecture five is going to be interesting because in this particular lecture we will be trying to understand the post-reform period developments, basically not from the internal economy but also from the external economic perspective that on exchange rate, on trade, what all measures were taken.

Whatever we see these days in the New India, whatever we have, the term that we use, it is always considered as one of the backbones, post-reform period measures it is considered as back bones, because these measures really helped India to come out strongly in terms of better growth and development.

So, now, you can see that in the beginning, if you trace the history, so from first five year plan, then we had second, third, fourth, fifth, whatever the volatile period that we had to experience, these particular ideas came in mind that now we started focusing on efficiency, that if we have set up some institutions, some firms and if you say that these firms are not functioning or some enterprises are not doing good, then these enterprises were made or were subject to some adjustment. And the government took measures in order to make sure that these PSUs or these enterprises also become efficient.

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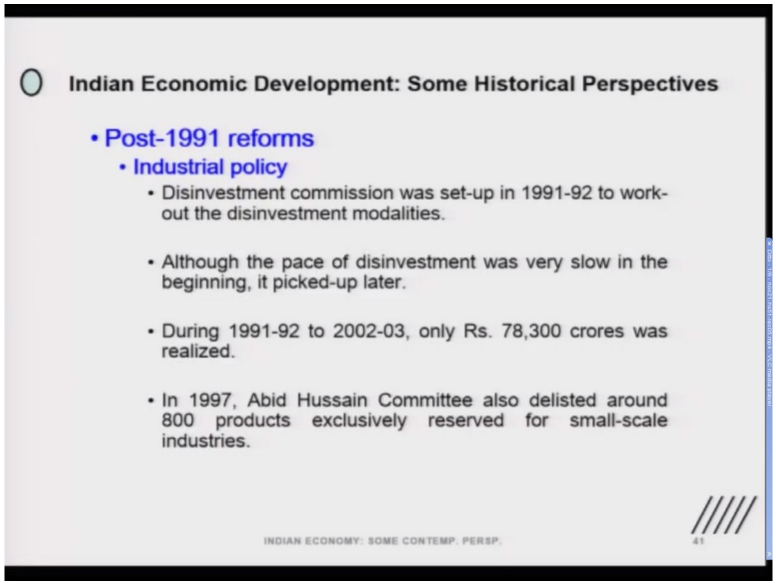

So, after 1991 debacle, we had to deal with the efficiency parameters also. So, to keep in mind, there was a Disinvestment Commission set up in 1991-92 to work out the disinvestment modalities. Now, for the very long time it has been there that most of the institutions which are not doing good or which are not of strategic importance, government would like to cut down the equities.

For example, in most of the PSUs, public sector undertakings, government has the equity of 51 percent and more than 51 percent. So, it was decided that in a phase wise manner, government will go by the reduction of 20 percent stake in PSUs. And the amount that will be received, it will be used for either restructuring or for developmental purposes. But in the beginning, it was designed just to make sure that the losses incurred by these PSUs are compensated back to them in terms of by selling the equity. So, government took measures regarding that.

In the beginning, it was very tough task to implement this particular measure, because there was a complete resistance coming from the PSUs that they should be given autonomy. And with respect to central enterprise norms they were given, but essentially, they were not able to make it in terms of profitable business.

So, disinvestment process has been very slow, not just in terms of the target, for instance, the target as of now it has been around more than Rs. 3 lakh crores, but we have been able to achieve only Rs. 1.2 lakh crores, rest of the amount still there has not been. Only I think four instances where we have been able to achieve the disinvestment target, otherwise, in most of the cases whatever the budget had announced the disinvestment target, they have not been able to achieve.

Now, in the modern era, in the contemporary context if you see, then there has been a time where there is a separate dedicated ministry to deal with disinvestment process. Now, we have reached to an extent where we are not just taking care of the sick units, which are not making profit, but we are also thinking about a strategic investment.

So, if the government thinks that, for example, in recent years you might have gone through some newspapers, news that how government is trying to get out of the fossil fuel business because the focus is on electrified vehicles. So, now government is shifting focus from fossil fuel, or I would say, crude oil business to completely going to go in towards electric vehicle. So, once we have that kind of a strategic move, then government is trying to sell the stake in oil companies. So, you may be reading a newspaper about those debate and discussion that how India is progressing in terms of implementing the new norms regarding vehicles.

So, in 1992, so the period from 1991-1992 to 2002-2003, the amount of around Rs. 78,300 crores were realized. And then apart from this disengagement measure, the government also took measures on delisting the 800 products which were exclusively meant for certain enterprises. So, now, delisting implied that anyone can come and produce these products. So, that was also one good move and it was recommended by Abid Hussian Committee.

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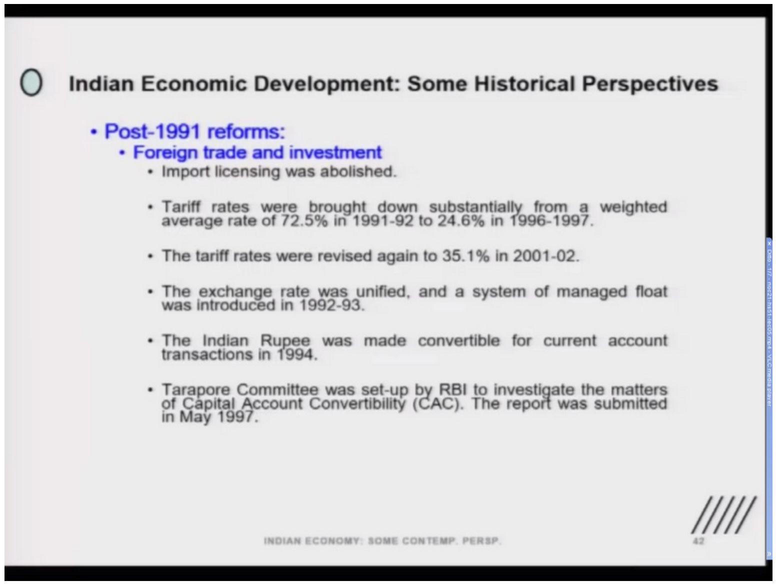

Then on foreign direct investment, it was a time that Government of India decided that they should be focusing on foreign investment. So, it was decided that, first of all, the idea was made that there will not be any import licensing, so import licensing was abolished completely. And then the tariff rates, which means that if you are importing certain goods and services from outside or certain goods from outside, then the government can impose extra taxes on those.

So, that we call it in terms of tariffs. Because of tariffs, it happens that the imported products become costlier in the domestic economy and which has a further disturbance in terms of inflation and other measures. And it is not necessary that most of these products are imported, it may happen that they may also be reused in a different manner.

So, in order to make sure that, that the economy moves in a proper liberalization process, the government took measures and decided to reduce the tariffs from a weighted average rate of 72.5 percent in 1991-1992 to 24.6 percent in 1996-1997. So, this was one very big move, though it was later moved upward. And then we had to see the rise from 24.6 percent in 1996-1997 to again moving up 35.1 percent in 2001-2002.

In terms of exchange rates, so, after the Bretton Woods agreement, we moved to a pegged currency where we had pegged our rupee with the sterling pound. But after 1975, we realized that we should go for a different set of exchange rate. So, we pegged our currency rupee with a basket of currencies. But after 1993, we had a liberalized exchange rate management system, LERMS, it is called LERMS, L-E-R-M-S.

Now, under this scheme, it was decided that we should be now not focusing on pegging our currency, rather we will be focusing on what is called the managed float system. What was the managed float system? So, the managed float system, it allows the central bank to take measures whenever you experienced high volatility in exchange rate or any kind of a speculative attack that you see on exchange rate behavior. So, if the exchange rate moves in an abnormal manner, then the central bank is tasked to monitor that and take corrective measures. So, this was there.

Then Indian rupee was made convertible for current account transactions, current account means export-imports, so those importers and exporters, those who have money or those traders those who participate in export and import business, it was just to facilitate their business transactions. It was made easier and they were able to go for full convertibility. So, whatever amount of export import that we were doing and if you want to convert in different currencies, you are allowed.

But regarding this there was one more development that took place and it was debated also and still it is in consideration, we have not gone for implementing that kind of measures, that is called capital account convertibility. Capital account convertibility, I can give you one example that if you have some amount of money in rupee, and if you want to convert into foreign currencies, you will be allowed if the capital convertibility is allowed. But capital convertibility also leads to inflow and outflow of unwarranted capital and that may further create instability in the economy.

So, to keep in mind, this Tarapore Committee was set up to investigate this and report was submitted in 1997. The second phase of Tarapore Committee again submitted report in 2005 and then that also recommended that we will be moving towards capital account convertibility in a phased wise manner not in a direct manner that we did in 1994 for current account convertibility.

So, the Tarapore Committee is also very important to understand from the perspective of the India's stabilization program where we did not take measures to just move from highly conservative economy or, I would say, closed economy to completely open economy. We took certain measures to improve our immediate indicators of growth and development, but not in terms of moving completely from what I just mentioned, from the era of conservative to completely open economy.

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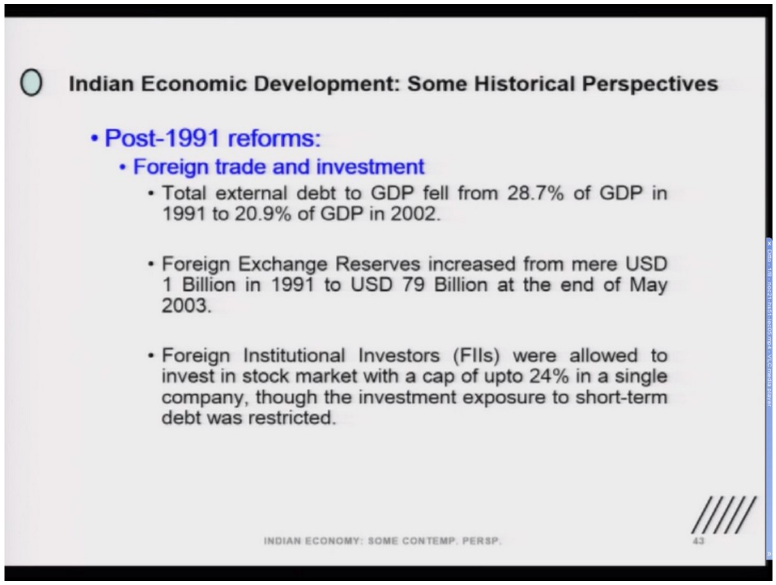

Then we had a foreign trade and investment. So, the total external debt of GDP fell from 28.7 percent GDP in 1991 to 20.9 percent GDP in 2002. And that was quite possible because we started experiencing the good signs of these measures, and these measures were quite useful.

And since the indicators were coming on track, so this also led to the foreign investors having more faith in India's economy and the foreign exchange reserves increased from US 1 billion Dollar that we had in 1991 to 79 billion Dollar by the end of May 2003. And now, we have w past the phase of 480 billion Dollar and now almost going close to 500 billion Dollar. So, now we are in a much more robust and quite comfortable position as compared to what we had seen in 1991, and even after 2003.

Now, there was one more development that we made it possible, and that is called the hot money. Hot money in the area of economics, it is called when this particular money moves easily from one location to another without any kind of check on that. But this particular money it signals about the economies in terms of future prospects, how the economy is going to do. So, if the hot money moves from one location to another quite frequently, and it goes to a recipient economy, when it is called that, that particular economy is expected to have better outlook and there are more opportunities. So that's why this particular money is flowing.

There was a case of Asian Financial Crisis in 1997 in East Asian countries, but that also led to the debate that whether we should be allowing or not. But we had allowed at that time. So foreign institutional investors were allowed to have the investment exposure of up to 24 percent in a single company, but these intuitions, FII investments were not allowed in short-term debt or even long-term debt, because these two are of strategic importance and it may not be good to expose to these hot capital into debt, because debt is a quite sensitive instrument and any buy or sell in these instruments may destabilize to complete bond market that we have.

So, keep in mind, short-term debt was not allowed because in India we have the government bond market very well developed, but we don't have that much corporate bond market. So, once we have the corporate bond market fully developed and if the firms may start introducing more bonds, launching more bonds to borrow money, then of course this particular limit may be also relaxed. So, this is what we have.

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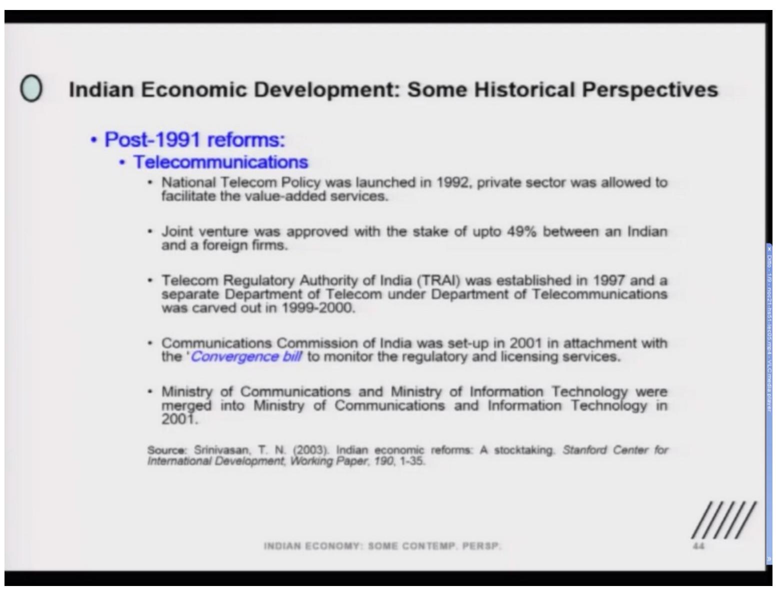

Then the era of telecommunication came, we moved from the period when we had a complete unavailability of telecom services, but Government of India announced the National Telecom Policy in 1992, it was again announced in 1999 also. So, at that time also it was decided that we should be adding the value-added services and this value-added service can be provided by the Indian organization, Indian company or even foreign company would also be allowed under joint ventures.

So, joint venture was approved with the stake of 49 percent between Indian and a foreign form. The Telecom Regulatory Authority of India was established in 1997. And a separate body of Department of Telecom under Department of Telecommunication was carved out in 1999-2000. And this was the time when we were really focusing on telecommunication sector, and because it has a lot of positive spillover on different sectors of the economy. So, keep in mind, it was decided that we should be focusing more on telecommunication.

There was a there was an introduction of Convergence Bill. And this Convergence Bill allowed Communications Commission of India to look after all, not just from the perspective of services, but also from the perspective of technology. So, there is a one unified set up, so that was called Convergence Bill.

Ministry of Communications, Ministry of Information Technology were merged into Ministry of Communication and Information Technology in 2001. And since then it has been there, there has been instances where government has now we have a proper auctioning mechanism. We also had the disturbance in this particular sector in the beginning in the form of 2G scam and others, but now we have gone for completely efficient system.

And this particular measure, why I mentioned here, because this particular measure has allowed a different era in India's economy, not just in terms of particular sector development but overall development. And it has a positive implication on all other economies. So, from rural India, from urban India, from industries, from services, it has helped a lot. So, that's why this telecommunication sector is worth mentioning here in this case.

One more case that we always highlight about our services sector is that how NASSCOM body helped the services sector and mostly information communication technology firms to grow faster, and they were allowed and they were given proper incentives. So NASSCOM, as a lobbying organization, it worked a lot in favor of these IT companies and that is why we have IT companies completely ruling all over in every sphere of information technology and services.

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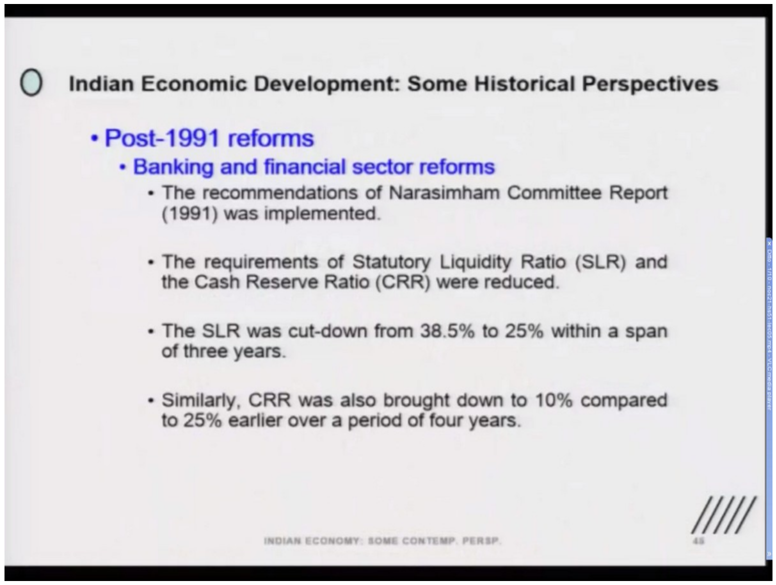

Then we had one more major development that I thought it should be worth mentioning. So post-reform 1991 period is very crucial for India's economy. If you want to detail it, then it may take, I think, longer, more than four weeks to go each and every point. But I am just trying to summarize in terms of major developments. And even if you can grasp these measures also then that will be more than sufficient to convince anyone that how post-1991 era was important for India's economy.

So, the recommendations of Narasimham Committee report were implemented. And this Narasimham Committee report helped a lot in terms of bringing efficiency to the Indian's economy, because at that time we were giving more importance to private sector, disinvestment was happening, there was a lot of credit crunch happening in the domestic economy. So, it was decided that Government of India will go for introducing certain measures to ensure that there is a banking efficiency in the economy.

So, for that, they revised two major indicators of banking sector, one is called Statutory Liquidity Ratio, SLR, and second is called Cash Reserve Ratio. SLR is important to understand because SLR allows or forces the bank to keep aside certain ratios or I would say certain proportion of deposits, in the form of either cash or in the form of precious metals, government securities. And this is one of the measures to control the credit channels in the country.

So, typically what happens is that when you have SLR higher, it means that banks are allowed to mandatorily keep certain amount of deposits in the form of cash, gold and securities. And since this money will not be available for credit, so as a result you have credit expansion completely squeezing, and once we have slowed down or, I would say, reduction in availability of credit, then automatically it will have a positive impact in inflation rate keeping down.

In the case of cash reserve ratio, this is the case, but our only thing is that in this case bank will again be allowed to keep certain amount of the deposits as cash and this is also one of the indicators to control the money supply.

So, these SLR and CRR are the indicators to control the money supply and it helps the bank to not only become a robust organization if the banks are going to have any kind of awkward moment in their deposits then they are allowed, with the permission of central bank, to utilize these kept ratios to just to maintain that there is a normal business happening.

So, the SLR was cut down from 38.5 percent to 25 percent within a span of three years, which means that banks were given more freedom to keep money in the liquid form and give it or lend it to the borrowers. So, which also means that it was indirect hint from the central bank saying that bank should be lending more and more to the borrowers and businessman.

Similarly, CRR was also brought down to 10 percent compared to 25 percent earlier over a period of four years, which means that this is also an indicator that money supply is going to increase. So, if SLR and CRR are going to be lower, it means that money supply is going to increase. Once you have a more money with the bank, they will be happy to lend it to the borrower, even at a cheaper rate. So, which also means that there will be credit expansion in the economy, this may lead to increase in inflation in future.

So, for that you have a central bank coming into picture, they will again revise the SLR and CRR targets and they will be told that you should be now putting up higher amount of deposits in the form of SLR and CRR requirements. So, for the first time, Narasimha Committee gave an indication that India is going to have expansionary monetary policy framework regarding the credit creation, and this credit creation will help facilitate the liquidity or it will bring more liquidity into the system. So, just to make sure that the businesses are expanding, these rates were rationalized and cut down further.

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To promote healthy competition, private sector banks were promoted. So private sector banks were also allowed, licensing norms were revised, which means that private sector banks were also given licensing in commercial banking businesses, so that they can also thrive and they can also provide services. Banks were given freedom to relocate branches and open specialized branches, which means that one is commercial one is called business branch. So, these banks were also allowed to set up their personalized branches for trade, for business, for commoners.

And these which later, after 2008 or 2009, it became incentive for these banks to set up branches in remote areas to become part of the financial inclusion process. That is a separate track that we will be discussing later, maybe in the middle of this particular course when we will be discussing the financial sector developments.

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Then the capital market, there was also a major development that had taken place, it is called Security Exchange Board of India, SEBI. So, SEBI regulates the financial landscape of this particular country. And SEBI is entrusted to have complete control on the stock market activities, inflow and outflow, and also considers or it also monitors the introduction of new product services, if there are any speculative attack on a particular firm, if there is any merger or acquisition happening without the permission of this particular regulator.

So, this particular regulator becomes really important to understand if you want to know that how the stock market functions and how it's different variants, they also work in in tandem with the Securities and Exchange Regulations.

So, this particular development was really important and it was set up in 1992, given a statutory recognition in 1992, based on the same committee recommendation of Narasimham. So, Narasimham Committee is having a very important role in India's banking sector development, plus stock market development, because it helps understand in a much better way.

So, so far what we have discussed is that, we have covered the major development that we thought we should be discussing. So, in this particular lecture what we have discussed so far is some recent, some very new development that we did not talk about when we were discussing first, second, third, fourth, fifth and sixth plan. But after post-1991 reforms, when India had to oblige the structural adjustment program of IMF, and with that they were supposed to open up different sectors, different economies, and accordingly Government of India also acted. And they also realized that it is a time that they should be taking.

Some of the proponents of this particular idea post reform measures they also mentioned that, since China has liberalized its economy in 1979, and they were taking a lot of measures to revive the economy, so India was bound to take such measures because we also wanted our economy to grow. And the best part of these reforms was that it started reflecting on India's economic indicators, and most of the indicators what we discussed so far, it came out good on paper and it also looked quite attractive. And that is why the process continued even after.

So, even in 2019-2020 when we read newspapers and all, we see that there is always a scope for making changes in each and every sector, each and every ministry. And that is way each and every ministry tries to implement such measures.

Now, after this, we will be talking about eighth and ninth plan, and then we will be moving to mid to 11th, 12th. And then we will summarize the whole planning process and we will finish it up. Thank you. Thank you so much.