Chapter-3

(LIBERALISATION, PRIVATISATION AND GLOBALISATION: AN APPRAISAL)

3.1 INTRODUCTION

You have studied in the previous chapter that, since independence, India followed the **mixed economy framework** by combining the advantages of the **capitalist economic system** with those of the **socialist economic system.**

Some scholars argue that, over the years, this policy resulted in the establishment of a variety of **rules and laws** which, though aimed at controlling and regulating the economy, ended up **hampering the process of growth and development**.

Others state that India, which started its developmental path from near stagnation, has since been able to:

- Achieve **growth in savings**,
- Develop a **diversified industrial sector** that produces a variety of goods, and
- Experience sustained **expansion of agricultural output**, which has ensured **food security.**

In **1991**, India met with an **economic crisis** relating to its **external debt** — the government was not able to make repayments on its borrowings from abroad. **Foreign exchange reserves**, which are generally maintained to import petroleum and other important items, dropped to levels that were **not sufficient even for a fortnight**.

The crisis was further **compounded by rising prices of essential goods.** All these factors led the government to introduce a **new set of policy measures**, which changed the direction of our **developmental strategies.**

In this chapter, we will look at:

- The **background of the crisis**,
- The **measures adopted by the government**, and
- Their **impact on various sectors of the economy**.

3.2 BACKGROUND

The origin of the **financial crisis** can be traced to the **inefficient management of the Indian economy in the 1980s**.

To implement policies and carry out general administration, the **government generates funds** from various sources such as:

- **Taxation**
- **Public sector enterprises**

However, when **expenditure exceeds income**, the government borrows money to finance the deficit from:

- **Banks**
- **People within the country**
- **International financial institutions**

When India imports goods like **petroleum**, it must pay in **dollars**, which it earns through **exports**.

Growing Fiscal Imbalance

Development policies required the government to **overshoot its revenue**, despite very low income, in order to meet challenges such as:

- **Unemployment**
- **Poverty**
- **Population explosion**

But:

- Continued government spending on development programmes **did not generate additional revenue**
- The government was **unable to generate sufficient income from internal sources** like taxation
- A large share of income was spent on areas like **social sectors and defence**, which **do not provide immediate returns**
- **Public sector undertakings** did not earn enough to meet the growing expenditure

Foreign Exchange Mismanagement

At times, **foreign exchange borrowed from abroad** was used to meet **consumption needs** instead of investments.

Neither was there:

- An attempt to **reduce wasteful spending**
- Nor sufficient attention given to **boost exports** to match the growing imports

By the **late 1980s**, the situation worsened:

- Government expenditure **greatly exceeded revenue**
- Meeting this gap through **borrowing became unsustainable**
- **Prices of essential goods** rose sharply
- **Imports grew rapidly**, while **exports lagged**
- **Foreign exchange reserves** declined to a level **insufficient to cover even two weeks of imports**
- India could not pay **interest on its international loans**
- **No international lender** was willing to assist further

India Seeks International Assistance

India approached:

- The **International Bank for Reconstruction and Development (IBRD)**, known as the **World Bank**
- The **International Monetary Fund (IMF)**

India received a **loan of $7 billion** to manage the crisis.

However, to avail the loan, India had to agree to certain **conditionalities**, such as:

- **Liberalising** and opening up the economy
- **Reducing the role of the government**
- **Removing trade restrictions** with other countries

New Economic Policy (NEP)

India accepted the conditions and announced the **New Economic Policy (NEP)**, which included:

- **Wide-ranging economic reforms**
- Aimed at creating a **competitive economic environment**
- Focused on removing **barriers to entry and growth** of firms

These reforms were broadly classified into two categories:

1. **Stabilisation Measures** (Short-term):
    - Aimed at correcting weaknesses in the **balance of payments**
    - Intended to **control inflation**

- Ensured maintenance of **adequate foreign exchange reserves**

2. **Structural Reform Measures** (Long-term):
    - Aimed at **improving efficiency**
    - **Enhancing international competitiveness**
    - Removing **rigidities in various segments** of the economy

Three Pillars of Economic Reforms

The government introduced reforms under **three major heads**:

- **Liberalisation**
- **Privatisation**
- **Globalisation**

3.3 LIBERALISATION

As pointed out earlier, the **rules and laws** originally intended to regulate economic activities eventually became **major obstacles to growth and development**.

Liberalisation was introduced to **end these restrictions** and **open up various sectors** of the economy.

Although some liberalisation measures were introduced in the **1980s**— in areas like:

- **Industrial licensing**
- **Export-import policy**
- **Technology upgradation**
- **Fiscal policy**
- **Foreign investment**

—the **reform policies of 1991** were far more **comprehensive and wide-ranging**.

Let us now examine key areas that received greater attention during and after 1991:

Deregulation of the Industrial Sector

Before liberalisation, India had strict **regulatory mechanisms** in place:

1. **Industrial licensing**: Entrepreneurs needed government permission to:
    - Start a firm
    - Close a firm
    - Decide the quantity of goods to produce
2. The **private sector** was **not allowed** in many industries
3. Certain goods were **reserved exclusively** for **small-scale industries**
4. The government controlled **price fixation** and **distribution** of specific industrial products

Reform measures post-1991 removed many of these restrictions:

- **Industrial licensing** was **abolished** for almost all products, except:
    - Alcohol
    - Cigarettes
    - Hazardous chemicals
    - Industrial explosives
    - Electronics
    - Aerospace
    - Drugs and pharmaceuticals
- Only a few industries—such as **atomic energy generation** and some **core railway activities**—are still reserved for the **public sector**
- Many goods **formerly reserved for small-scale industries** have now been **dereserved**
- In most industries, the **market now determines prices**

Financial Sector Reforms

The **financial sector** includes:

- **Commercial banks**
- **Investment banks**
- **Stock exchange operations**
- **Foreign exchange markets**

This sector is primarily **regulated by the Reserve Bank of India (RBI)**.

The RBI governs:

- The **money reserves** banks must hold
- **Interest rates**
- **Lending policies** across sectors

The **objective of financial sector reforms** was to **reduce the RBI's role from regulator to facilitator**, allowing financial institutions to make more **independent decisions.**

Key financial reforms included:

- **Private sector banks** (both Indian and foreign) were allowed to be established
- **Foreign investment limit** in banks was increased to around **74%**
- Banks meeting certain conditions were allowed to:
  - **Open new branches** without RBI approval
  - **Rationalise existing branch networks**
- Banks were permitted to **raise resources both domestically and internationally**

However, the **RBI retained control** over key **managerial aspects** to protect:

- The **interests of account-holders**
- The **financial security of the nation**

Additionally, **Foreign Institutional Investors (FIIs)**—including:

- **Merchant bankers**
- **Mutual funds**
- **Pension funds**

—were permitted to **invest in Indian financial markets.**

Tax Reforms

Tax reforms refer to changes in the government's **taxation and public expenditure policies**, collectively known as **fiscal policy.**

There are **two main types of taxes**:

1. **Direct Taxes** – levied on:
    - **Incomes of individuals**
    - **Profits of business enterprises**
2. **Indirect Taxes** – levied on:
    - **Goods and services** (commodities)

Reforms in Direct Taxes

Since **1991**, continuous efforts have been made to:

- **Reduce income tax rates**, as high rates were believed to encourage **tax evasion**
- Encourage **savings** and **voluntary disclosure** of income through **moderate taxation**
- **Gradually reduce the corporate tax rate**, which was earlier very high

Reforms in Indirect Taxes

Efforts have also focused on:

- **Simplifying the indirect tax system**
- Promoting the creation of a **common national market** for goods and services

A major step was taken in **2016**, when the **Indian Parliament passed the Goods and Services Tax Act (GST Act)**.

- The law came into effect in **July 2017**

Expected benefits of GST:

- **Simplified and unified tax structure**
- **Increased government revenue**
- **Reduced tax evasion**
- Establishment of **'One Nation, One Tax, One Market'**

Simplification Measures

To improve **tax compliance**, the government also:

- **Simplified tax procedures**
- **Reduced tax rates** significantly

These reforms aim to make the tax system:

- **More transparent**
- **More efficient**
- **Easier for taxpayers to comply with**

Foreign Exchange Reforms

The first major reform in the **external sector** took place in the **foreign exchange market**.

- In **1991**, as an immediate response to the **balance of payments crisis**, the **Indian rupee was devalued** against foreign currencies.
- This **devaluation increased the inflow of foreign exchange** and set the foundation for **reducing government control** over exchange rate determination.

Since then, the exchange rate of the rupee is **largely determined by market forces**, that is, based on:

- The **demand for foreign exchange**
- The **supply of foreign exchange**

This transition allowed India to **move towards a more flexible exchange rate system**.

Trade and Investment Policy Reforms

The **liberalisation of trade and investment policies** was initiated with several objectives:

- To enhance the **international competitiveness** of Indian industries
- To attract **foreign investments** and **advanced technology**
- To promote **efficiency in local industries** and encourage the **adoption of modern technology**

Earlier Policy Regime:

Before 1991, India had adopted a highly **protective trade policy**:

- There were **quantitative restrictions** on imports
- **High tariffs** (import taxes) discouraged foreign goods
- **Tight controls and import licensing** were in place

These policies:

- Protected domestic industries

- But also **reduced efficiency**, **limited competitiveness**, and led to **slow manufacturing growth**

Key Reforms Introduced:

1. **Dismantling Quantitative Restrictions**:
   - Import and export quotas (limits) were removed.
2. **Reduction in Tariff Rates**:
   - Duties on imports were gradually reduced to encourage trade.
3. **Abolition of Import Licensing**:
   - Licensing requirements were removed for most products, except:
     - **Hazardous materials**
     - **Environmentally sensitive industries**
4. **Removal of Quantitative Restrictions on Consumer Goods**:
   - From **April 2001**, restrictions on importing **manufactured consumer goods** and **agricultural products** were **fully removed**.
5. **Abolition of Export Duties**:
   - Export duties were removed to improve the **competitiveness of Indian products** in international markets.

These reforms helped integrate India's economy with the global market by **encouraging exports, enhancing competitiveness**, and **attracting foreign capital and technologies**.

3.4 PRIVATISATION

Privatisation implies shedding the ownership or management of a government-owned enterprise. Government companies are converted into private companies in two ways:

1. By **withdrawal of the government** from ownership and management of public sector companies, and/or
2. By **outright sale** of public sector companies.

Privatisation of public sector enterprises (PSEs) by selling off part of their equity to the public is known as **disinvestment.** According to the government, the purpose of this sale was mainly to:

- Improve financial discipline
- Facilitate modernisation
- Utilise private capital and managerial capabilities effectively to enhance the performance of PSUs (Public Sector Undertakings)

The government also envisaged that **privatisation could provide a strong impetus to the inflow of Foreign Direct Investment (FDI).** Additionally, it made efforts to improve the efficiency of PSUs by granting them autonomy in managerial decisions.

Box 3.1: Navratnas and Public Enterprise Policies

You may have read in your childhood about the famous Navratnas or *Nine Jewels* in the Imperial Court of King Vikramaditya—eminent figures in art, literature, and knowledge. Drawing from this idea, the government introduced classifications for high-performing PSEs to enhance efficiency and competitiveness in the liberalised global environment. These include:

- **Maharatnas**
- **Navratnas**
- **Miniratnas**

These classifications granted greater **managerial, financial, and operational autonomy** to these enterprises, enabling them to make independent decisions and improve profitability.

Examples of PSEs with Special Status:

- **Maharatnas**:
  - Indian Oil Corporation Limited
  - Steel Authority of India Limited
- **Navratnas**:
  - Hindustan Aeronautics Limited
  - Mahanagar Telephone Nigam Limited
- **Miniratnas**:
  - Bharat Sanchar Nigam Limited
  - Airports Authority of India
  - Indian Railway Catering and Tourism Corporation Limited

Many of these profitable PSEs were originally established in the 1950s and 1960s when **self-reliance** was a key public policy goal. They were intended to:

- Provide infrastructure
- Generate direct employment
- Offer quality products at nominal costs
- Be accountable to all stakeholders

The granting of special status led to improved performance in these companies.

However, **some scholars allege** that instead of supporting the expansion of public enterprises and helping them become global players, the government **partly privatised them through disinvestment**. Recently, the government has shown intent to retain them in the public sector, **enable global expansion**, and **raise resources independently from financial markets.**

3.5 GLOBALISATION

Globalisation is generally understood as the **integration of a country's economy with the world economy**, but in reality, it is a **complex phenomenon**. It is the result of a set of policies aimed at transforming the world into a system of **greater interdependence and integration**.

It involves the creation of networks and activities that **transcend economic, social, and geographical boundaries**. Globalisation seeks to establish links such that **events occurring in one part of the world can influence developments in another**—for example, happenings in India can be affected by events miles away. In essence, it aims to **turn the world into one whole**, creating what is often described as a **borderless world.**

Outsourcing: A Key Outcome of Globalisation

One of the most significant results of globalisation is **outsourcing**. This refers to a practice where a company hires **regular services from external sources**, often from **other countries**, which were previously provided internally or domestically. Examples of such services include:

- Legal advice
- Computer services
- Advertising
- Security

Earlier, these services were handled by respective departments within the company. However, due to globalisation and rapid advancement in **Information Technology (IT)** and **communication systems**, outsourcing has become a prominent economic activity.

In recent times, many services are being outsourced to India, including:

- Voice-based business processes (BPOs or call centres)
- Record keeping
- Accountancy
- Banking services
- Music recording
- Film editing
- Book transcription
- Clinical advice
- Online teaching

With modern telecommunication tools, including the **Internet**, services involving **text, voice, and visual data** can be **digitised and transmitted in real time** across continents and national boundaries.

India as a Global Outsourcing Hub

India has emerged as a **leading destination for global outsourcing** due to:

- **Low wage rates**
- Availability of **skilled manpower**
- **Reasonable quality and accuracy** of service delivery

Multinational corporations, and even small businesses, are increasingly outsourcing their services to India, especially in the **post-reform period**. This has enabled India to play a significant role in the global services sector.

World Trade Organisation (WTO)

The **World Trade Organisation (WTO)** was established in **1995** as the **successor to the General Agreement on Trade and Tariff (GATT)**, which was created in **1948** with **23 founding countries**. GATT served as a global trade organisation to administer multilateral trade agreements and ensure equal trading opportunities for all member nations.

The **WTO aims to establish a rule-based trading regime** where nations cannot impose arbitrary restrictions on trade. Its key objectives include:

- Facilitating the **expansion of production and trade in goods and services**
- Ensuring **optimum utilisation of global resources**
- **Protecting the environment**
- Promoting **fair and open international trade** through the **removal of tariff and non-tariff barriers**
- Providing **greater market access** to all member countries

India and the WTO

India, as an important member of the WTO, has played a proactive role in:

- **Framing fair global trade rules and regulations**
- Advocating the interests of the **developing countries**
- Keeping its **commitments to liberalisation** by:
    - Removing **quantitative restrictions on imports**
    - Reducing **tariff rates**

Debate and Concerns

Some scholars question the usefulness of India's WTO membership, noting that a **large share of international trade happens among developed nations.** While **developed countries often protest against agricultural subsidies**, **developing nations like India** feel that they are:

- **Forced to open their markets** to goods from developed countries
- **Denied fair access** to the markets of developed nations

This raises concerns about **inequity in global trade practices.**

Box 3.2: Global Footprint!

Due to globalisation and India's integration into the world economy, several **Indian companies have expanded internationally**:

- **ONGC Videsh** (subsidiary of ONGC): Projects in **16 countries**

- **Tata Steel**: Operations in **26 countries**, products sold in **50 countries**, employing **50,000 people abroad**
- **HCL Technologies**: Offices in **31 countries**, employing **about 15,000 persons overseas**
- **Dr Reddy's Laboratories**: Now has **global manufacturing plants and research centres**

3.6 INDIAN ECONOMY DURING REFORMS: AN ASSESSMENT

The reform process has completed three decades since its introduction. Let us now look at the performance of the Indian economy during this period. In economics, the growth of an economy is measured by the Gross Domestic Product (GDP).
Look at Table 3.1.

The post–1991 India witnessed a rapid growth in GDP on a continual basis for two decades. The growth of GDP increased from **5.6 per cent during 1980–91** to **8.2 per cent during 2007–12**.

During the reform period, the **growth of agriculture has declined**. While the **industrial sector reported fluctuation**, the **growth of the service sector has gone up**, indicating that GDP growth is mainly driven by growth in the service sector.

During **2012–15**, there has been a **setback in the growth rates** of different sectors witnessed post–1991. While agriculture recorded a **high growth rate during 2013–14**, it witnessed **negative growth** in the subsequent year. The **industrial sector witnessed a steep decline during 2012–13**, but in the subsequent years, it began to show **continuous positive growth**. The **service sector continued to witness a high level of growth** — higher than the overall GDP growth in 2014–15 — with a remarkable **growth rate of 9.8 per cent**.

The **opening of the economy** has led to a **rapid increase in foreign direct investment and foreign exchange reserves**.

- Foreign investment (FDI and FII) rose from about **US $100 million in 1990–91** to **US $30 billion in 2017–18**.
- Foreign exchange reserves increased from about **US $6 billion in 1990–91** to about **US $413 billion in 2018–19**.
  India is now **one of the largest foreign exchange reserve holders in the world**.

Since 1991, India has emerged as a **successful exporter** of auto parts, pharmaceutical goods, engineering goods, IT software, and textiles. Rising prices have also been **kept under control**.

Fig. 3.2 — *IT industry is seen as a major contributor to India's exports.*

On the other hand, the reform process has been **widely criticised** for **not being able to address** some of the basic problems facing our economy, especially in the areas of **employment, agriculture, industry, infrastructure development**, and **fiscal management**.

Growth and Employment:

Though the GDP growth rate has increased in the reform period, scholars point out that the **reform-led growth has not generated sufficient employment opportunities** in the country. You will study the link between different aspects of employment and growth in the next unit.

International Trade and WTO Concerns

Some scholars **question the usefulness** of India being a member of the **World Trade Organisation (WTO)**, as a **major volume of international trade occurs among developed nations**. They argue that:

- While **developed countries file complaints** over agricultural subsidies given in their countries,
- **Developing countries feel cheated**, as they are **forced to open their markets** for developed countries
- But are **not allowed equal access to the markets** of developed nations.

SECTOR-WISE IMPACT OF ECONOMIC REFORMS

Reforms in Agriculture

Reforms have **not been able to benefit agriculture**, where the **growth rate has been decelerating.** Since 1991, **public investment in agriculture**, especially in **infrastructure** such as irrigation, power, roads, market linkages, and research and extension (which played a crucial role in the Green Revolution), has fallen.

Further, the **partial removal of fertiliser subsidies** has led to a rise in the **cost of production**, severely affecting **small and marginal farmers**.

This sector has also been impacted by **policy changes**, including:

- Reduction in **import duties** on agricultural products
- **Low minimum support prices (MSP)**
- **Lifting of quantitative restrictions** on imports

These reforms have **adversely affected Indian farmers**, exposing them to **increased international competition**.

Additionally, due to **export-oriented strategies** in agriculture, there has been a shift from **production for the domestic market** toward **production for export markets**, focusing on **cash crops** instead of food grains.
This shift has contributed to **rising food grain prices**.

Reforms in Industry

Industrial growth has also seen a **slowdown** due to:

- **Decreasing demand** for industrial products
- **Cheaper imports** replacing domestic goods
- **Inadequate investment in infrastructure**, especially in power supply

In a globalised world, **developing countries like India are compelled to open up** their economies to the **flow of goods and capital** from developed nations. This has made **domestic industries vulnerable** to **imported goods**, reducing demand for local products.

Moreover, **globalisation has created conditions** favouring the **free movement of goods and services** from foreign countries, **adversely affecting local industries and employment** in developing countries.

India also **lacks access** to developed countries' markets due to **high non-tariff barriers**.
For example:

- Even though **quota restrictions on textile exports** have been removed by India,
- **The USA continues to maintain quota restrictions** on textile imports from India and China.

Disinvestment

Each year, the government sets a **disinvestment target** for Public Sector Enterprises (PSEs).

- In **1991–92**, the target was **Rs. 2,500 crore**, and **Rs. 3,040 crore** was mobilised — exceeding the target.
- In **2017–18**, the target was about **Rs. 1,00,000 crore**, and the achievement was **Rs. 1,00,057 crore**.

However, **critics argue**:

- PSE **assets were undervalued and sold** to the private sector
- This resulted in a **substantial loss to the government**

- The **proceeds** from disinvestment were used to **cover revenue shortfalls**, instead of being used for **developing PSEs or building social infrastructure**

Do you think selling a part of the properties of government companies is the best way to improve their efficiency?

Reforms and Fiscal Policies

Economic reforms have **placed limits** on the growth of **public expenditure**, especially in **social sectors**.

- **Tax reductions** aimed at curbing tax evasion and boosting revenue **did not significantly increase** tax revenue.
- **Tariff reductions** under reform policies **reduced custom duty revenues**, limiting another key source of government income.
- To attract **foreign investment**, the government offered **tax incentives**, further **reducing tax revenue**.

This has had a **negative impact** on **developmental and welfare expenditures**.

Box 3.3: Siricilla Tragedy

Power sector reforms in many Indian states resulted in:

- **Ending subsidised electricity**
- **Steep rises in power tariffs**

This hit **small-scale industries** hard.

One example is the **powerloom textile industry in Andhra Pradesh**.

- Power cuts meant **lower production**, leading to **lower wages** for workers, since their pay was tied to output.
- Combined with high power tariffs, workers suffered huge losses.
- A few years ago, **50 powerloom workers committed suicide** in **Siricilla**, a small town in Andhra Pradesh.

Here is the **logically arranged and refined version** of your passage for **Section 3.7: Conclusion** from the chapter *Liberalisation, Privatisation and Globalisation: An Appraisal*:

3.7 CONCLUSION

The process of **globalisation**, driven by **liberalisation** and **privatisation** policies, has produced **both positive and negative outcomes** for India and other countries.

Some scholars view globalisation as an **opportunity** — offering:

- **Greater access to global markets**
- **Advanced technology**
- Increased potential for **large industries** in developing countries to become **important players on the international stage**

On the other hand, **critics argue** that globalisation is primarily a **strategy of developed countries** to **expand their markets** in developing nations. According to them:

- It has **compromised the welfare and identity** of people in **poorer countries**
- It has led to **market-driven globalisation**, which in turn has **widened economic disparities** among nations and among people within nations

From the Indian perspective, some studies suggest that:

- The **economic crisis of the early 1990s** stemmed from **deep-rooted inequalities** in Indian society
- The **reform policies** introduced in response to this crisis, based on **externally advised policy packages**, have in fact **aggravated these inequalities**

Furthermore:

- The reforms have primarily **increased income and consumption** among **high-income groups**
- **Economic growth** has been **concentrated in select service sectors** such as:
    - Telecommunication
    - Information technology
    - Finance
    - Entertainment
    - Travel and hospitality
    - Real estate
    - Trade

These sectors, though important, do **not employ the majority** of India's population.

Meanwhile, **vital sectors such as agriculture and industry**, which provide **livelihoods to millions**, have **not benefitted proportionately** from the reform process.