CLASS 12 ECONOMICS

INDIAN ECONOMIC DEVELOPMENT

CHAPTER-3

New Economic Policy – Liberalization, Globalization and Privatization (1990- Onwards)

Part A

INSTRUCTIONS:

STEP 1 : Read chapter-3 from NCERT book Indian Economic Development.

Learning Objectives: After studying this chapter, you will be able to:

- Understand the background of the reform policies introduced in India in 1991
- Understand the mechanism through which reform policies were introduced
- Comprehend the process of globalisation and its implications for India
- Be aware of the impact of the reform process in various sectors.

The following topics are covered in this chapter:

i. Defination of New Economic Policy

ii. Need for new economic policy

iii. Components of new economic policy

iv. Privatization

STEP 2 : Watch the video on Chapter 3 Indian Economy (1990-) through the following link:

https://youtu.be/nZK88FXKsQU

STEP 3: Following are the Main points of the chapter.

The reforms were based on the assumption that market forces would steer the economy into the path of growth and development.

Economic reforms started in 1991 in India.

Causes of Economic Crisis

Different causes of economic crisis are given as under

- The continued spending on development programmes of the government did not generate additional revenue.
- The government was not able to generate sufficient funds from internal sources such as taxation
.
- Expenditure on areas like social sector and defence do not provide immediate returns, so there was a need to utilise the rest of its revenue in a highly effective manner, which the government failed to do
.
- The income from public sector undertakings was also not very high to meet the growing expenditures.
- Foreign exchange borrowed from other countries and international financial institutions was spent on meeting consumption needs and to make repayments on other loans
.
- No effort was made to reduce such increased spending and sufficient attention was not given to boost exports to pay for die growing needs.

Due to above stated reasons, in the late 1980s, government expenditure began to exceed its revenue by such large margins that meeting the expenditure through borrowings became unsustainable

Need for Economic Reforms

The economic policy followed by the government upto 1990 failed in many aspects and landed the country in an unprecedented economic crisis. The situation was so alarming that India's reserves of foreign exchange were basely 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

- Increasing fiscal deficit
- Adverse Balance of Payments
- Gulf crisis
- Rise in prices
- Poor performance of Public Sector Units (PSUs).
- High rate of deficit financing.
- Collapse of soviet block.

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 loan to manage the crisis. International agencies expected India to liberalise and open up economy by removing restrictions on private sector and remove trade restrictions between India and other countries.
India agreed to conditions of World Bank and IMF and had announced New Economic Polity (NEP) which consist of wide range of economic reforms.

The measures adopted in the New Economic Policy can be broadly classified into two groups i.e.

,

- Stablisation Measures They are short-term measures which were intended to correct some weakness that have developed in the Balance of Payments and to bring Inflation under control.

- Structural Reforms They are longterm measures, aimed at improving the efficiency of the economy and increasing its international competiveness by removing the rigidities in various segments of the Indian economy.

The various structural reforms are categorised as

- Liberalisation
- Privatisation
- Globalisation

Liberalisation

Liberalisation of the economy means its freedom from direct or physical controls imposed by the government.

Economic Reforms Under Liberalisation

Objectives of Liberalisation

The main objectives of liberalisation policy are

- To increase competition among domestic industries.
- To increase foreign capital formation and technology.
- To decrease the debt burden of the country.
- To encourage export and import of goods and services.
- To expand the size of the market.

Economic reforms under liberalisation- In brief

(i) Industrial Sector Reforms

- Abolition of industrial licensing.
- De-reservation of production areas.
- Expansion of production capacity.
- Freedom to import goods.

(ii) Financial Sector Reforms

Liberalisation implied a substantial shift in the role of the RBI from a regulator to a facilitator of the financial sector.

(iii) Fiscal Reforms Fiscal reforms relate to revenue and expenditure of the government.

Tax reforms are the principal component of fiscal reforms. Broadly taxes are classified

- Direct Taxes and
- Indirect Taxes

(iv) External Sector Reforms It include Foreign exchange reforms and Foreign trade policy reforms.

Economic Reforms Under Liberalisation (In detail)

Reforms under liberalisation were introduced in many areas.

Industrial Sector Reforms

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, chugs and pharmaceuticals.

(ii) Contraction of Public Sector The number of industries reserved for the public sector was reduced from 17 to 8.. Presendy, only three industries are ' reserved for public sector. They are

- Railways
- Atomic energy
- Defence

(iii) De-reservation of Production Areas The production areas which were earlier reserved for SSI were de-reserved.

(iv) Expansion of Production Capacity The producer's 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.

Financial Sector Reforms

Financial sector includes financial institutions such as commercial banks, investment banks, stock exchange operations and foreign exchange market.

The following reforms were initiated in this sector

- Reducing Various Ratio Statutory Liquidity Ratio (SLR) was lowered from 38.5% to 25%.

- Cash Reserve Ratio (CRR) was lowered from 15% to 4.1%.

- Competition from New Private Sector Banks The banking sector was opened for the private sector. This led to an increase in competition and expansion of services for consumers.

- Change in the Role of RBI RBI's role underwent a change from a 'regulator' to a 'facilitator'.
- De-regulation of Interest Rates Except for savings accounts, banks were able to decide their own interest rates

Tax Reforms/Fiscal Reforms

Tax reforms are concerned with the reforms in government's taxation and public expenditure policies which are collectively known as its fiscal policy.

Moderate and Simplified Tax Structure Prior to 1991, the tax rates in the country were quite high, which led to tax evasion. The fiscal reforms simplified the tax structure and lowered the rates of taxation. This reduced tax-evasion and increased government's revenues.

Foreign Exchange Reforms/External Sector Reforms

External sector reforms include reforms relating to foreign exchange and foreign trade. The following reforms were initiated in this sector

(i) Devaluation of Rupee Devaluation implies a fall in the value of rupee against some foreign currency. In 1991, the rupee was devalued to increase our country's exports and to discourage imports.

(ii) Other Measures

- Import quotas were abolished.
- Policy of import licensing was almost scrapped.
- Import duty was reduced.
- Export duty was completely withdrawn.

ASSIGNMENT

1.	Define the following terms: Privatization ……… ….. ……… ….. ……… ….. ……… ….. Disinvestment ………	

	….. ……… ….. Foreign direct investment ……… ….. ……… ….. Public sector undertaking ……… ….. ……… ….. Two examples of companies which have been privatized so far ……… ….. ……… ….. ……… ….. ……… …..	
2.	What is meant by economic reforms? Explain the need for economic reforms (new economic policy) in 1991. ……… ….. ……… …..	

....
.....

....
.....

....
.....

....
.....

....
.....

....
.....

....
.....

....
.....

....
.....

....
.....

....
.....

....
.....

....
.....

....
.....

....

	….. …… ….. …… ….. …… ….. …… ….. …… …..	
3	What is meant by the term privatization? What are the objectives of privatization? (explain any two) …… ….. …… ….. …… ….. …… ….. …… ….. …… ….. …… ….. …… …..	

	…….. …….. …….. …….. …….. …….. ……..	
4	What are the various ways in which privatization can be done? …….. …….. …….. …….. …….. …….. ……..	

	…… …..	
5	Privatisation of the public sector undertakings by selling off part of the equity of PSUs to the private sector is known as_____________. **a.** Privatisation **b.** Origin of private sector **c.** Disinvestment **d.** None of the above	
6	In which year WTO was founded? a) 1995 b) 2005 c) 1985 d) 1975	
7	Identify the indirect tax a) Wealth tax b) Income tax c) GST d) Property tax	
8	In which year new economic policy in India was announced? a) 1981 b) 1991 c) 2001 d) 1971	
9	Which of the following is the aim of Privatisation? **a.** Providing strong momentum to the inflow of FDI **b.** Improving the efficiency of PSU's **c.** Both (a) and (b) **d.** None of the above	
10	Which of the following are the reasons of economic reforms? **a.** The poor performance of public sector **b.** Inflationary Reforms **c.** Terms and conditions of world bank **d.** All of the above	

11	When government disinvests its shares to the extent of 5 to 10 percent to meet the deficit in the budget, this is termed as a. None b. Partial privatisation c. Token privatisation d. Denationalisation	
12	LPG stands for: a. Liberalisation, Production and Global Cooperation b. License, Privatisation and Globalisation c. Liberalisation, Privatisation and Globalisation d. License, Permit and Good	
13	__________ means transfer of ownership, management and control of public sector enterprises to the private sector. **a.** Liberalisation **b.** Privatisation **c.** Globalization **d.** None of the above	
14	Extra questions for practice. These questions may have the same content but asked in a different way. Privatisation has done more harm than good. Justify your answer. **(1)** Why did the Indian Government need to borrow from international organisations? **(1)** Those Public Sector Undertakings which are making profits should be privatised. Do you agree with this view? Why? **(3)**	

	In your opinion, what are the advantages of privatisation to the economy? **(3)**	