ECONOMIC REFORMS SINCE 1991

ZHANG CHENGLIANG / CHINA DAILY

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REASONS BEHIND THE INTRODUCTION OF NEW ECONOMIC POLICY (ECONOMIC REFORMS)

(i) Fiscal deficit: The government's expenditure was much more than its income. So, the government was compelled to borrow money from international organizations. Public debt became very high. A huge amount had to be paid as interest every year.

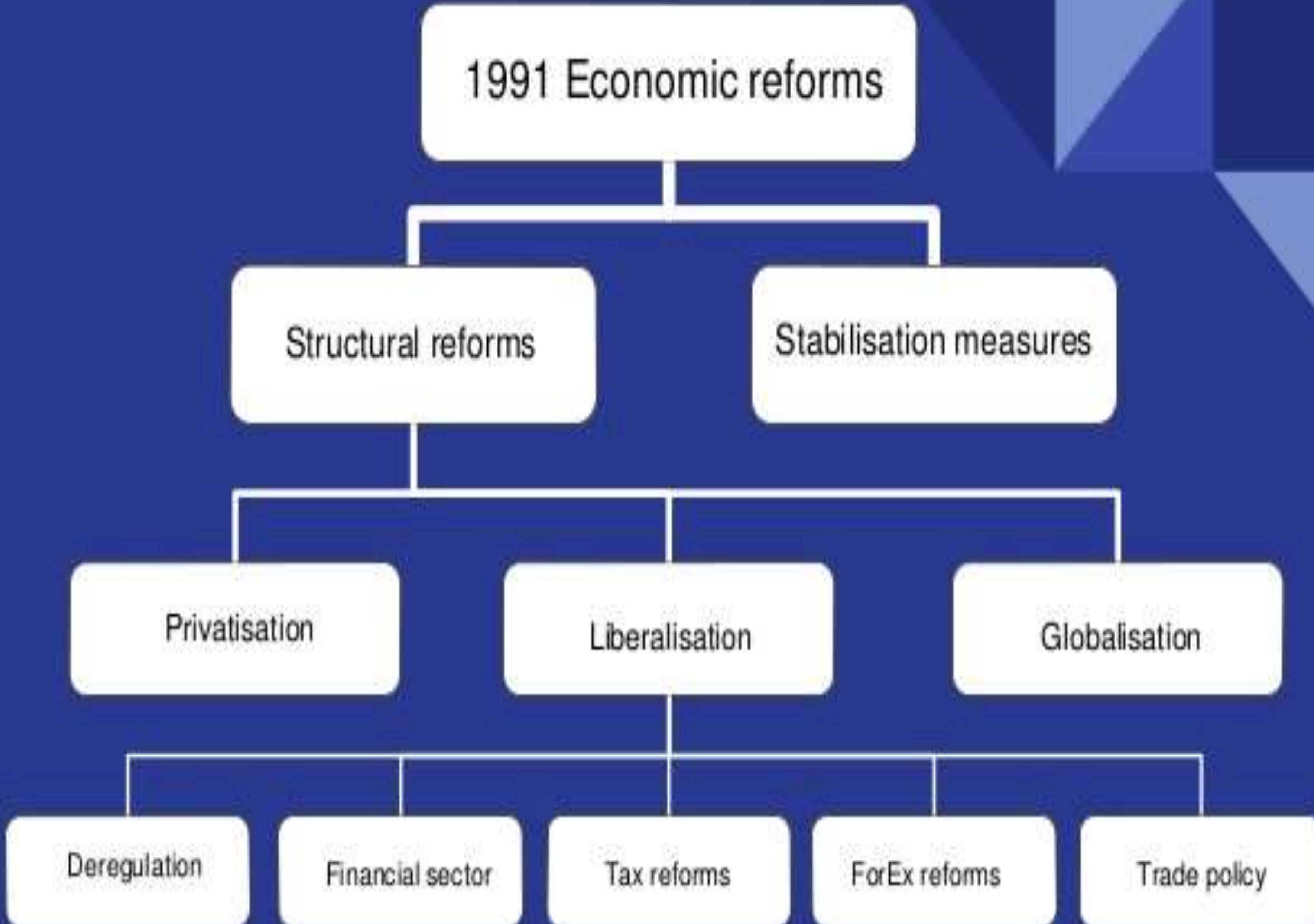
(ii) Unfavourable Balance of Payments*:* Value of import became much more than the value of exports. The foreign exchange reserve became very low. The country was finding it very difficult to meet the import expenditure.

(iii) Gulf Crisis: A large number of Indians are working in Gulf countries. The Iraq war affected them badly. Many of them returned to India. So, the earnings from Gulf countries declined sharply.

(iv) Inflation: Prices of essential goods increased sharply. This affected the poor and salaried people very badly. Living standard of the people came down.

(v) Poor performance of the Public Sector Industries: Many of the PSUs became sick units. Inefficiency and corruption resulted in the downfall of the PSUs.

(vi) Role of IMF and World Bank: India got a loan of $ 7 billion from IMF and World Bank. They instructed India to introduce economic reforms.


1991 Economic reforms
Structural reforms
Stabilisation measures
Privatisation
Liberalisation
Globalisation
Deregulation
Financial sector
Tax reforms
ForEx reforms
Trade policy

The NEP can be classified in to two categories:

(i) Stabilisation measures: They are short term measures to increase foreign exchange reserve and to control Inflation.

(ii) Structural Reforms: They are long term measures. Liberalisation, Privatisation and Globalisation are the structural reform measures.

Liberalisation refers to withdrawing all the control and restrictions imposed on the economy by the government.

LIBERALISATION OF INDUSTRIAL SECTOR

Liberalisation in Industrial Sector (Industrial Sector Reforms)

(i) Abolition of Industrial Licensing: Licensing has been abolished for all most all products except dangerous and harmful goods like alcohol, cigarettes, explosives etc. Licensing is also not needed for increasing production capacity.

(ii) ***De- reservation of production areas:*** The goods which were earlier reserved for the small scale sector have now been opened for large scale units also.

(iii) Freedom to import capital goods: All the restrictions on the import of machines, tools and equipments have been removed.

(iv) Withdrawal of Price Restriction: The practice of Government fixing the prices of necessary goods was stopped. Market is given freedom to decide prices.

LIBERALISATION OF

Financial Sector

Financial Sector Reforms

(i) The role of RBI has been changed from that of a regulator to a facilitator. Banks and other financial institutions are given freedom to take independent decisions.

(ii) Permission was given to start private banks.

(iii) Foreign Direct Investment in the banking sector is increased to 50%.

(iv) Banks are given freedom to set up new branches without the permission of RBI.

(v) Foreign Institutional Investors such as merchant bankers, mutual funds and pension funds are allowed to invest in India.


TAX
REFORMS

Tax Reforms

(i) Income tax rates have been reduced. This was done to discourage tax evasion.

(ii) Corporation tax has also been reduced to encourage investment.

(iii) Goods and Services Tax (GST) was introduced to replace a large number of indirect taxes.

(iv) Tax structure has been made simple.

FOREIGN EXCHANGE REFORMS

Foreign Exchange Reforms

(i) Rupee had been devalued. It was done to encourage exports and discourage imports.

(ii) India changed from fixed exchange rate system to flexible exchange system. Market forces are allowed to determine the exchange rates.

TRADE AND INVESTMENT POLICY REFORMS

Trade and Investment Policy Reforms

(i) Import licensing has been abolished except for dangerous and harmful goods.

(ii) Import and export quotas have been abolished.

(iii) Customs duties were reduced. Export duties have been abolished for most of the goods

Bilateral Trade.

Bilateral Trade agreement is between two countries. They give most favoured nation status to each other. They frame rules and regulations and trade based on those rules.

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Multi – lateral Trade

Multi – lateral trade agreement is an agreement between several countries. All the members have most favoured nation status. Countries trade with each other as per the rules in the general agreement.

Tariff Barriers

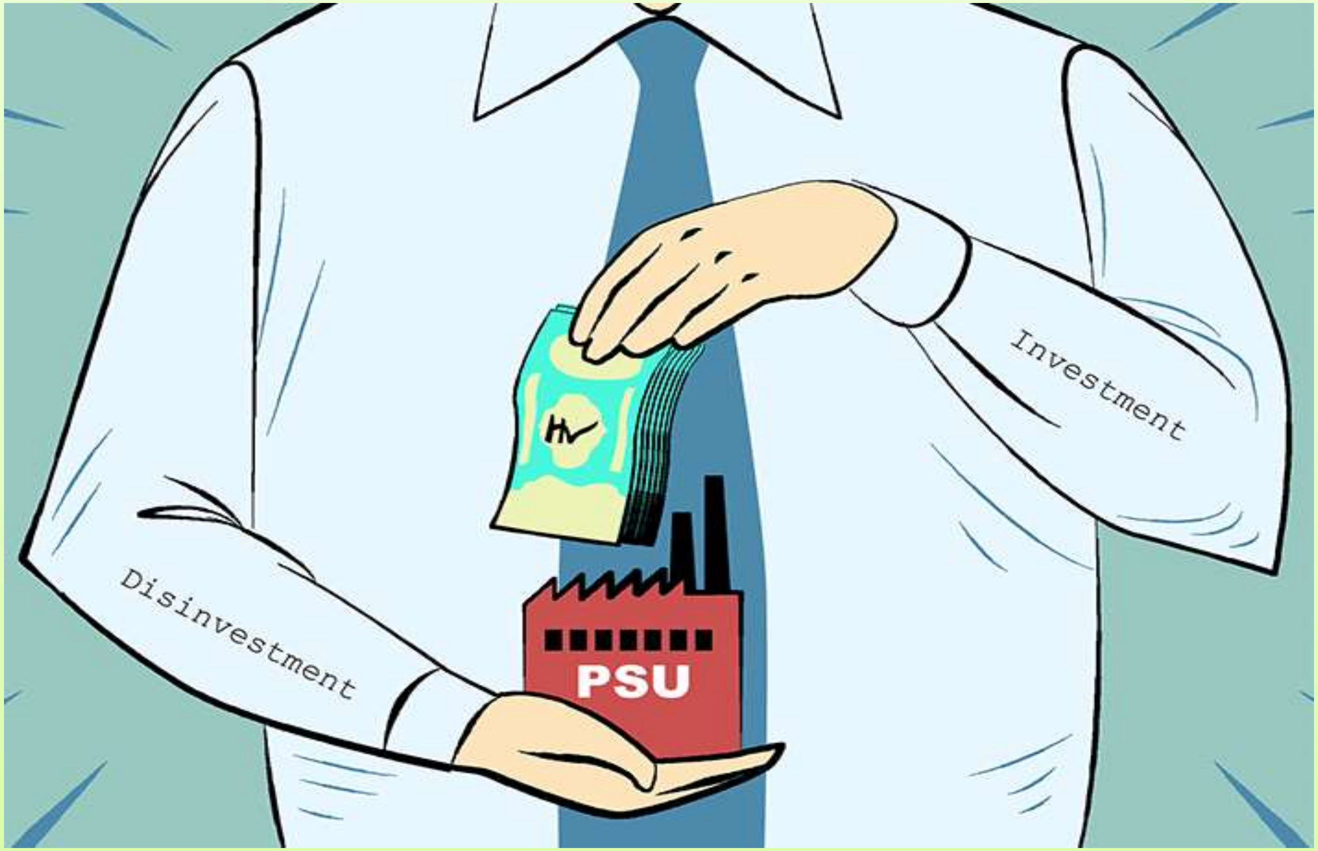
Customs duties can be used as trade barrier. Heavy import duty can discourage import and heavy export duty can reduce exports. Countries used tariff barriers to protect domestic producers and domestic consumers.

Non Tariff Barriers

They are also called quantitative restrictions. The countries impose import quota and export quota. Quota refers to the maximum quantity that can be imported or exported. Quotas discourage import and export.

PRIVATISATION

Privatisation refers to disinvestment in the public sector. The government decided to sell the shares of PSUs to the private individuals. The aim was to improve efficiency in the industrial sector.



REASONS FOR PRIVATISATION

(i) Many of the PSUs became sick units. They became a social burden

(ii) Industrial efficiency and productivity became low.

(iii) The government wanted to raise money for social welfare programmes.

(iv) Corruption became widespread in the Public Sector.

(v) People were not able to get good quality goods and services.

TWO DIFFERENT METHODS OF PRIVATISATION

Strategic Sale

Strategic sale refers to the sale of 51% or more of the shares of Public Sector Undertakings to private sector. Ownership and management of the company will pass on to the private sector.

Minority Sale

Minority sale refers to the sale of less than 49% of the shares of PSUs to the private sector. Ownership and management will remain with the Government.

MERITS OF PRIVATISATION

(i) Efficiency and productivity of industrial sector improved.

(ii) The government could get enough money for social welfare programmes.

(iii) Industrial development became faster. The private enterprises earn profits and reinvest the profits.

(iv) Consumers are able to get good quality goods and services.

DEMERITS OF PRIVATISATION

(i) It is against the national goal of Socialism. It will take the country close to Capitalism.

(ii) Private producers are aimed at maximization of profits. They will not give importance to socially desirable goods and services.

(iii) Workers will be exploited. Their life will become difficult.

GLOBALISATION

Globalisation refers to the integration of our economy with the world economy. It is a system in which goods, services, investment and people move freely across the political boundaries.

Measures taken for the Globalisation of the Indian Economy

(i) Restrictions on foreign investments have been removed. Now in many production areas 100% foreign direct investment is allowed.

(ii) Import and export quotas have been removed. Customs duties have been reduced.

(iii) Partial convertibility of Indian rupee is permitted. The rupee has been devalued.

(iv)The country adopted a long term trade policy.


Outsourcing
Team search

- Outsourcing is a practice in which a company hires regular services from external sources, mostly from other countries.
- Legal service, computer service, advertisement service, data entry, accounting service etc are outsourced by the companies of developed countries.
- The growth of Information Technology helped in the growth of outsourcing.

INDIA – A FAVORITE OUTSOURCING DESTINATION

India is a favourite outsourcing destination

(i) Wage rates are low in India. So, companies can

reduce their cost of production.

(ii) India has a lot of skilled man power

(III) Indians are fluent in English language.

Outsourcing is good for India

(i) It provides employment opportunities to a large number of educated people.

(ii) It enables India to earn a lot of foreign exchange.

(iii) It improves the GDP of our country. Economic growth rate increases.

Developed countries are opposing outsourcing

(i) It reduces employment opportunities in their countries.

(ii) It leads to the outflow of foreign exchange.

(iii) It affects their growth rate.

WORLD TRADE
ORGANIZATION

(i) WTO (World Trade Organisation) was started in 1995 to replace General Agreement on Trade and Tariff (GATT).

(ii) It is an international organization that promotes foreign trade and foreign investment.

(iii) It aims at the removal of tariff and non tariff barriers to foreign trade.

(iv) WTO discourages bilateral trade agreements and supports multi lateral trade agreements.

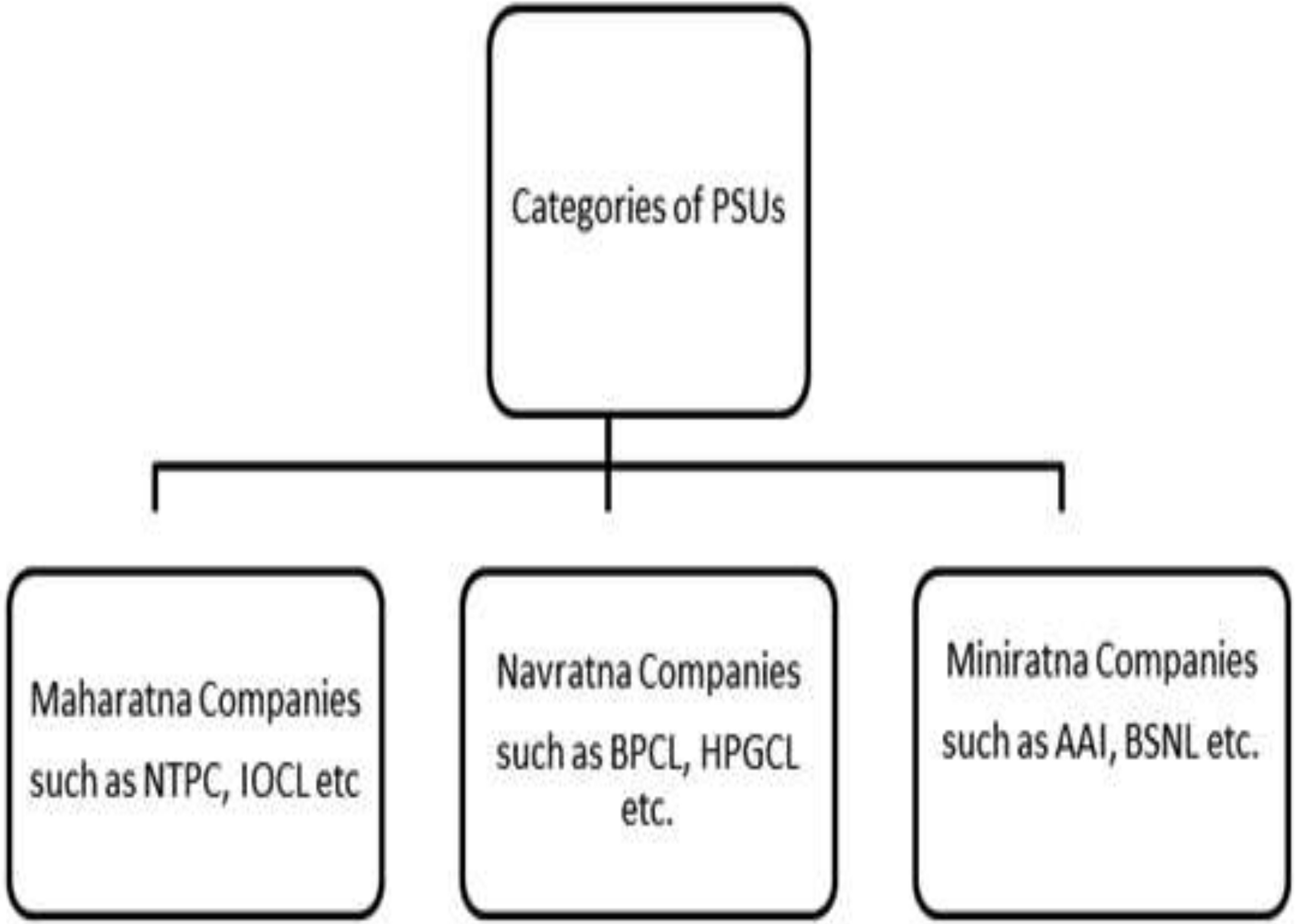
As on 14 July 2016, there are 164 members in WTO.

(i) All member countries get Most Favoured Nation status. This will help us to increase our trade with other countries.

(ii) WTO promotes multi lateral trade agreements. It enables us to trade with several countries without any restrictions.

(iii) Removal of trade barriers allow our goods to enter in to the markets of other countries.

(iv) WTO also aims at increase in production capacity and protection of environment. It benefits India.


Categories of PSUs
Maharatna Companies such as NTPC, IOCL etc
Navratna Companies such as BPCL, HPGCL etc.
Miniratna Companies such as AAI, BSNL etc.

Adverse Effects of New Economic Policy on Agriculture

(i) Agricultural growth rate decreased in India during the reforms period.

(ii) Public investment in infrastructure development such as irrigation, power, roads etc decreased.

(iii) Removal of fertilizer subsidy affected the small and marginal farmers. Their cost of production increased.

(iv) Reduction in import duty and the removal of import quota resulted in the arrival of foreign agricultural goods to our markets. Demand for our goods decreased.

(v) Removal of Minimum Support Price made the farmers vulnerable to market risks.

(vi) Farmers were encouraged to produce cash crops for export market. It resulted in the increase in prices of food grains.

EFFECTS OF NEW ECONOMIC POLICY ON INDUSTRIAL GROWTH

(i) Industrial growth rate slowed down in India during the reform period.

(ii) Demand for our industrial products decreased due to the arrival of foreign goods.

(iii) Our markets are opened for foreign goods. However, the developed countries have not opened their markets for our goods.

(iv) Reduction in public investment in infrastructural facilities also affected industrial growth.

EFFECTS OF NEW ECONOMIC PLICY ON WELFARE AND SOCIAL JUSTICE

(i) Fall in agricultural production during the reform period added to poverty and unemployment in rural areas. Several farmers committed suicide.

(ii) Cutting of subsidies increased the cost of production of farmers. Farming became a loss making business.

(ii) Privatisation made the life of workers miserable. They lost job security.

(iv) Profit became the only aim of production. So, the production of socially desirable goods and services is neglected.

(v) International competition resulted in the decline of small scale industries. Several workers became unemployed.

(vi) Coming up of MNCs created a lot of job opportunities for educated people, especially women.

EFFECT OF NEW ECONOMIC POLICY ON ECONOMIC GROWTH

(i) Economic growth is measured in terms of GDP. India's GDP growth rate increased from 5.6% during 1980 – 91 to 8.2 % during 2007 – 12.

(ii) The growth of agriculture declined.

(iii) Industrial sector reported fluctuating growth rate.

(iv) Service sector has grown rapidly. The growth rate of service sector reached 10.3% in 2014 – 15.

EFFECTS OF ECONOMIC REFORMS ON FOREIGN INVESTMENT

(i) Foreign Direct Investment and Foreign Institutional Investment increased from US$ 100 million in 1990 -91 to US$36 billion in 2016 – 17.

(ii) Foreign exchange reserve increased from US $ 6 billion in 1990 – 91 to US $360 billion in 2014 – 15.

(iii) Today, India is one of the largest foreign exchange reserve holders in the world.

(v) Farmers were encouraged to produce cash crops for export market. It resulted in the increase in prices of food grains.

Disinvestment process during the reform period.

(i) In 1991 -92 the target for disinvestment was to collect ` 2500 crores by disinvestment. The actual collection was ` 3040 crores.

(ii) In 2017 – 18 the target was ` 1 lakh crores. The actual collection was ` 1 lakh 57 crores.

Criticisms against the disinvestment policy followed during the reform period

(i) Assets of Public Sector units were undervalued and sold to the private sector. It caused a lot of loss to the Government.

(ii) The money collected from disinvestment was not use for welfare activities. It was used to overcome the revenue deficit of the Government,

(iii) Mostly profit making PSUs were sold to private sector.

Effects of Economic Reforms on the Fiscal Policy

(i) Public expenditure on social sectors reduced during reform period.

(ii) Reduction in taxes affected the revenue receipts of the Government.

(iii) Reduction in customs duties and tax concessions to foreign investors also affected Government's revenue.

MERITS OR POSITIVE IMPACT OF THE NEW ECONOMIC POLICY (LPG POLICY)

(i) Economic growth is measured in terms of GDP. India's GDP growth rate increased from 5.6% during 1980 – 91 to 8.2 % during 2007 – 12.

(i) Foreign Direct Investment and Foreign Institutional Investment increased from US$ 100 million in 1990 -91 to US$36 billion in 2016 – 17.

(ii) Foreign exchange reserve increased from US $ 6 billion in 1990 – 91 to US $360 billion in 2014 – 15.

(iv) Service sector developed. It provides employment to a large number of educated people.

(v) Disinvestment enabled India to collect a lot of money and use it for welfare activities.

DEMERITS OR NEGATIVE IMPACT OF THE NEW ECONOMIC POLICY

(i) Industrial growth rate slowed down in India during the reform period. Demand for our industrial products decreased due to the arrival of foreign goods.

(ii) Agricultural growth declined. Our agricultural goods face competition from the goods of other countries.

(iii) Public expenditure on social sectors reduced during reform period. Reduction in taxes affected the revenue receipts of the Government.

DEMONETISATION

Withdrawal of a coin or currency note from its use as legal tender is called demonetisation.

(i) On 8th November 2016, the Government announced demonetization of 500 and 1000 rupee notes. They constituted nearly 86% of India's cash supply.

(ii) People were given time till 31 December 2016, to deposit demonetized notes with the Banks or post offices.

(iii) The Banks and Post Offices were instructed to report all deposits above ` 2.5 lakhs in Savings Account and above ` 12.50 lakhs to income tax department. New 500 and 200 rupee notes were introduced.

MERITS OF DEMONETIZATION

(i) It helps to eliminate black money: Black money refers to unaccounted money. Those who hold black money cannot exchange the demonetized currency with legal tender currency. Either they have to pay tax and make it white money or dispose it off.

(ii) It helps to eliminate fake currency notes: Fake currency notes cannot be deposited in Banks. So, such notes will be eliminated.

(iii) Reduction in illegal activities: Black money and fake currency notes are mostly used for illegal activities such as terrorism and smuggling. Elimination of black money and fake currency resulted in the decline of these activities.

(iv) Promotion of cash less transactions: Demonetisation encouraged people to go for digital transactions. The use of payment applications, debit cards, credit cards and online transfer increased. India is moving towards efficient cash less economy.

(v) Increase in tax revenue: Demonetisation forced several people to disclose their actual income and pay taxes properly. Revenue from income tax, property tax, and wealth tax and land registration fees increased considerably.

(vi) Reduction in Government’s liability: Black money holders who did not want to disclose their income had to dispose off their old currency notes. It reduced the liability of the Government.

Demerits or adverse effects of demonetization

(i)Inconvenience to people: It caused a lot of inconvenience to the people. People had to stand in long queues to deposit, exchange or withdraw notes. Sudden announcement of demonetization created panic and fear among the people. Lack of sufficient currency in the hands created a lot of trouble.

(ii) Negative effect on Economic activities: Demonetisation had negative effect on trade, business and consumption activities. Economy slowed down. It affected the growth of the economy.

(iii) Costly for the Government: The Government had to spend a lot of money to print the new currency notes that replaced the old ones.

(iv) Difficulty in cash less transactions: A large number of people in the country are uneducated and ignorant. They found it very difficult to carry out cash less transaction.

(v) Corruption: Several Bank officers illegally exchanged old notes for the new ones. They misused Jandhan accounts for that.

(vi) Loss to daily wage earners: Slow down of economy affected the daily wage earners. Job opportunities reduced and employers were unable to pay wages.

Effect of Demonetization on the money supply in the economy

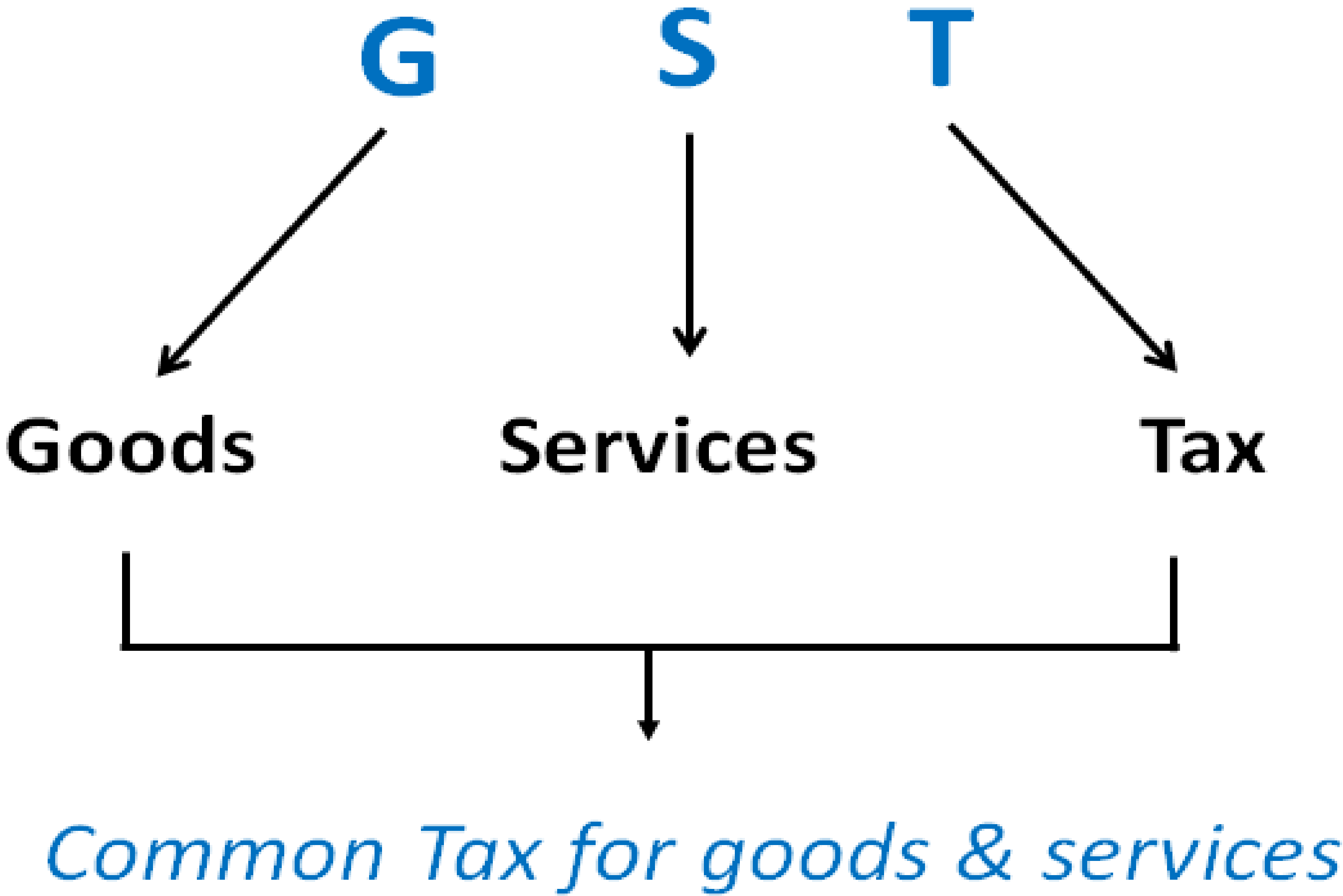
Money supply reduced due to demonetization. Elimination of black money and fake currency resulted in the decline of money supply. Delay in supplying new currency notes also resulted in the decline of money supply.

Effect of Demonetization on the liquidity position of Commercial Banks

People deposited old currency notes in large quantities in their accounts. Banks got a lot of deposits. It increased the liquidity position of Banks.

Effect of Demonetization on Inflation

Demonetisation helped in reducing the rate of inflation. Elimination of black money and fake currency resulted in reduction in money supply. This led to reduction in aggregate demand. Prices started falling in the economy.


G
S
T
Goods
Services
Tax
Common Tax for goods & services

Goods and Services Tax (GST)

GST is an indirect tax levied on the supply of goods and services right from the producer to the consumer.

It is a destination based consumption tax with facility of Input Tax Credit in the supply chain.

It is applicable throughout the country with one rate for one type of goods/service.

GST has replaced many indirect taxes. GST was brought in to effect on 1 July, 2017.

The Indirect Taxes that were replaced by the GST

VAT/Sales Tax, Entry Tax, Luxury Tax, Octroi, Entertainment Tax, Taxes on Advertisements, Taxes on Lottery /Betting/ Gambling, State Cesses on goods.

(i) GST is an indirect tax that was designed to bring the indirect taxation under one umbrella. More importantly, it is going to eliminate the cascading effect of tax. It avoids tax on tax.

(ii) It introduced the concept of One Nation, One Tax and One Market. Rate of taxation is uniform throughout the country. It promoted free movement of goods across the states.

(iii) GST reduced cost of production and helped our producers to compete with the products of other countries.

(iv) GST promoted economic growth rate. Simple and moderate tax system encourages investment and growth.

(v) Taxation system has been made simple. The entire process from registration to filing returns can be made online.

(vi) Several small producers and small service providers are exempted from taxation under GST.

(vii) Tax rate for essential commodities is very low. This will help poor people.

Demerits of GST

(i) GST was introduced in the middle of the financial year. This created a lot of confusion among the people.

(ii) As the fee structure is totally new, the small producers had to seek the help of professionals. They had to purchase the new software.

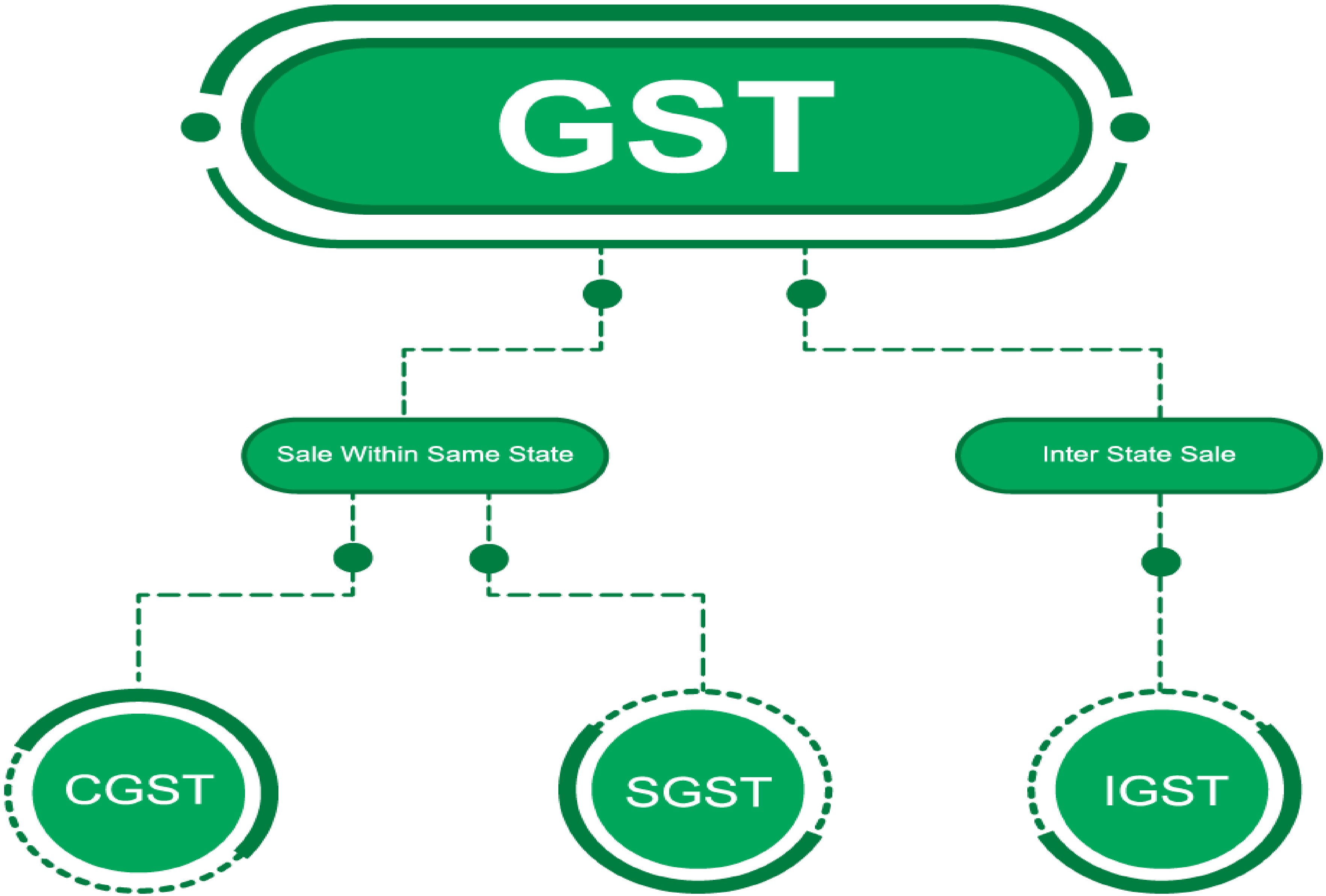
(iii) GST registration in different states became mandatory for the sellers.

Components of GST

(i) CGST: Collected by the Central Government on an intra-state sale (Eg: transaction happening within Maharashtra)

(ii) SGST: Collected by the State Government on an intra-state sale (Eg: transaction happening within Maharashtra)

(iii) IGST: Collected by the Central Government for inter-state sale (Eg: Maharashtra to Tamil Nadu)


GST
Sale Within Same State
Inter State Sale
CGST
SGST
IGST


THANK
YOU