Economic Reforms in India during the Early Decade of 21st Century

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Introduction

It is generally agreed in studies on Indian economy that the process of economic reforms was initiated in India by the government. of P.V. Narasimha Rao in 1991 with the announcement of a number of measures for liberalizing the economy by the then Finance Minister Manmohan Singh. However, Arvind Panagariya (2001) has argued that the process of economic reforms was initiated during the second half of 1980's under the stewardship of the then Prime Minister Rajiv Gandhi. In support of his contention, he quotes from the Kingsley Martin Memorial Lecture, delivered in Cambridge in 1987 by I.G Patel who approvingly described the reforms introduced by Rajiv Gandhi in the preceding one and a half years as the 'New Economic Policy'. This New Economic Policy had moved the Indian economy towards increased outward and inward competition by the end of 1980's. Panagariya emphasizes the shift in the Industrial Policy statement, 1990 towards large-scale liberalization. This policy provides compelling evidence that internal and external liberalization had gained considerable political acceptance at least a year before the balance of payments crisis. In his own study, Panagariya prefers to term the period since 1988 as the phase of economic reforms. However, he himself admits that the 1991-92 liberalization was substantially at variance from the piecemeal measures preceding it. Whereas the prior liberalization had been undertaken within the essential framework of investment, import licensing, and price and distribution controls, the 1991 reforms abandoned that framework and moved away towards replacing it with the market mechanism. Although the fears of political backlash still compelled Finance Minister Manmohan Singh to project the reforms as the continuation of the past policies, the actual measures represented complete renunciation of the old policy framework and brought liberalization out in the open. It is precisely because of this reason that in most of the studies on Indian economy the process of economic reforms is assumed to have started in 1991.

Immediate Causes of Reforms

The immediate reason for undertaking economic reforms in India in 1991 was mainly a macroeconomic crisis precipitated by both national & international conditions. Some of the more important reasons were as follows:

Increase in Fiscal Deficit

The fiscal crisis in 1990 was not a coincidence. The fiscal situation had deteriorated throughout the 1980's due to growing burden of non-development expenditure. All the indicators of fiscal imbalance reflect that throughout the 1980's it was on the rise. The indicators, which are normally used to measure fiscal imbalance, are the Revenue Deficit, and the Gross Fiscal Deficit. Of these, the first one known as the conventional measure of fiscal imbalance indicates only a part of the resource gap, which is mainly financed by the issue of treasury bills. A large portion of the gap in the resources of the Government is financed by market borrowing, small savings, provident funds, external borrowing, etc. and this does not get reflected in the conventional measure of fiscal imbalance. Fiscal deficit is a sum of budget deficit and market borrowing and other's liabilities of the Government of India. The fiscal deficit was 5.8% in 1980-81 and it became 7.9% in 1990-91. Interest payments, which were 2% of GDP and 10% of total Central Government expenditure in 1980-81, rose to 3.8% of GDP and 22% of total Central Government expenditure in 1990-91. How alarming this fiscal situation was, can be realized from the fact that in 1990-91 interest payments had eaten up 9.1% of the total revenue collections of the Central Government. This obviously was an unsustainable situation.

Gulf Crisis

The Gulf crisis in the late 1990's sharply accentuated macroeconomic problems in India. The import bill of petroleum, oil and lubricants. Rose from a mere $ 180 million in 1970-71 to $ 6028 million in 1990-91. There was also political instability in the country at this juncture. All these developments together eroded international confidence in the Indian economy and as a result of this, country's credit rating in the international capital market declined steeply.

Adverse Balance of Payments

The balance of payments situation of India was highly pre-carious in 1991, but this was not unexpected. The current account deficit, which was $ 2.1 billion or 1.35% of GDP in 1980-81 rose to $ 9.7 billion or 3.69% of GDP in 1990-91. These continuously growing deficits had to be financed by borrowing from abroad and as a consequence India's external debt rose to 12% of GDP at the end of 1990-91. This steadily growing external debt led to an increase in debt service burden from 10% of current account receipts and 15% of export earnings in 1980-81 to 22% of current account receipts and 30% of export earnings in 1990-91. These mounting strains during the 1980s stretched to the breaking point in 1991 due to the Gulf crisis.

Mounting Inflationary Pressures

The rate of inflation rose to 10.3% in 1990-91. In terms of the consumer price index the rate of inflation climbed to 11.2 per annum, which was certainly a cause for concern. However, the most disquietening feature of this inflationary situation was that the prices of food rose substantially in spite of three good monsoons in a row. According to Deepak Nayyar (1996) these inflationary pressures in the economy did not surface out of the blue.

The greatest challenge to the world today is the problem of deep poverty amid plenty of the world's 6 billion people, 2.8 billion live on less than $ 2 a day and 1.2 billion live on less than $ 1 a day with 44% living in South Asia. In rich countries fewer than 1% children do not reach their fifth birthday while in poorest countries as many as 20% do not. While less than 5% children fewer than five years age are malnourished in rich countries, the comparable figures for poor countries are 50%.

This distribution persists even though human conditions have improved more globally in the past century than in the rest of history. But the distribution of these global gains is extraordinarily unequal. The average income in the richest 20 countries is 37 times the average in the poorest 20 - a gap that has doubled in the past 40 years. And the experiences have been vastly different at national and sub national levels and for ethnic minorities & women. Faced with this picture of global poverty and inequality, the international community has set itself several goals — popularly known as Millennium Development Goals — with the sole objective of changing this scenario as early as 2015.

What is Poverty?

Poverty is a state of being poor. It can be defined as a social phenomenon in which a section of society is unable to fulfill its basic necessities. But poverty is much more than this. Poor people often lack adequate food and shelter, education and health, deprivation that heap them from leading the kind of life that everyone values. They also face extreme vulnerability to ill health, economic dislocation and national disasters. They are often exposed to ill treatment by institutions of the state and society and are powerless to influence any decision that affects their lives. Infect, poverty is the result of economic, political and social processes that interact with each other in ways that increase the deprivation in which poor people live. Lack of assets, inaccessible markets and scarce jobs opportunities lock people in material poverty. According to Amartya Sen (1985) "Poverty is not just a matter of being relatively poor than others in the society, but of not having some basic opportunities of material well-being –the failure to have certain minimum 'capabilities'. The criteria of minimum capabilities is 'absolute' in the sense that ------ people's deprivations are judged absolutely and not simply in comparison with the deprivations of others in that society ------ the relevant capabilities are of many different kinds e.g. being free from starvation, from hunger, from undernourishment, participating in communal life; being adequately sheltered, being free to travel to see a friend and so on". In line with Sen's views, the World Bank has also accepted the now established view of poverty as encompassing not only low income and consumption but also low achievement in education, health, nutrition and other areas of human development. According to World Development Report 2000-01 on "Attacking Poverty", "Poverty is more than inadequate income or human development; it is also vulnerability and a lack of voice, power and representation".

Despite the broadening of the concept of poverty over time, using monetary income or consumption to identify and measure poverty has long traditions. On this basis, it is customary to use the concept of poverty in two senses.

Absolute Poverty

In the absolute standard, minimum physical quantities of cereals, pulse, milks, butter, etc. are determined for a subsistence level and then the price quotations are used to convert the physical quantities into money terms. Aggregating all the quantities gives a figure expressing per capita consumer expenditure below which a person is considered to be below poverty line (BPL).

Relative Poverty

Relative standard income distribution of the population in different groups are estimated and a comparison of the levels of living of the top 5% to 10% with the bottom 5% to 10% of the population reflects the relative standards of poverty. The defect of this approach is that it indicates the relative position of different segments of the population in the income hierarchy but is silent about their absolute status.

The approach to reducing poverty has evolved over the past 50 years in response to better understanding of the complexity of development. In the 1950's & 1960's many viewed large investment in physical capital and infrastructure as the primary measures of development. In the 1970's awareness grew that physical capital was not enough and health and education were equally important as articulated by the World Development Report 1980. The 1980's saw another shift of emphasis on improving economic management and allowing greater play for market forces. World Development Report 1990 proposed a two part strategy: promoting labour intensive growth through economic openness and investment in infrastructure and providing basic services to poor people in health and education. In the 1990's governance and institutions moved to the centre stage while the 21st century strategy focuses on inclusion, and participation of the poor in the decision process and their empowerment thereof.

Poverty and Economic Reforms

Economic reforms are known to bring about fast growth in an economy but there is growing concern on their effects on poverty especially in developing countries. The popular belief is that economic reforms, at least in the transitory period adversely affect the poor. Although economists have debated the effect of economic reforms on poverty, it has been observed in developing economies that after the initial phase of reforms, alleviation of poverty has been substantially significant. Economic reforms are primarily directed to attract private investment. Major focus areas of such reforms are privatization, stabilization and deregulation. In the primary stages, these measures may seem to have a negative effect on the poverty factor. Privatization of Public Sector Units for instance may cause retrenchment. Deregulation, on the other hand may give rise to risks and uncertainties in the economy. The process of deregulation leads to state non-intervention in the informal sector. This again can have its own insecurities.

However, as economic reforms gain momentum, higher volume of investment is generated in the economy. Higher investment leads to more employment opportunities, which is a direct benefit of growth in the economy. Increase in employment leads to reduction of poverty in the economy. Moreover, economic reforms are often accompanied by special programs aimed at structural adjustments to address the poverty issue. The International Financial Institutions, specially the World Bank have played important role, in supported such programs in developing countries. Another important aspect of the poverty issue in relation to economic reforms has been the gender related issues.

Structural Adjustment Programs (SAPs) have been formulated and promoted by the World Bank and International Monetary Fund (IMF). These SAPs have been adopted by many developing countries, to overcome poverty through economic reforms. In 1990, the World Development Report published by World Bank, laid down certain important initiatives in economic reforms aimed at poverty reduction. Some of the major initiatives mentioned in this regard are:

1. Giving impetus to investment in labor intensive industries.
2. Investment in health, education and other socially important sectors.
3. Providing safety nets for the poor and unemployed. While in the case of some Latin American and African countries such adjustment programs have not been too successful in delivering desired results, in Asian countries, especially in China and India, the results have shown significant success of the implementation of SAPs.

The World Bank estimates that even today 456 million Indians (42% of the total Indian population) live under the global poverty line of & 1.25 per day (ppp). This means that a third of the global poor now reside in India. The recently released report of the World Bank 'Global Economic Prospect' for 2009 forecasts that 25% of India's population will be living in extreme poverty, on less than $ 1.25 a day in 2015. However, this also represents a significant decline in poverty from 60% in 1981 to 42% in 2005. On the other hand, the Planning Commission of India uses its own criteria and has estimated that 27.5% of the population was living below the poverty line in 2004-05 down form 51.3% in 1977-78, and 36% in 1993-94. The source for this was the 61st round of the National Sample Survey (NSS) and the criterion used was monthly per capita consumption expenditure below Rs. 356.35 for rural areas and Rs. 538.60 for urban areas. 75% of the poor are in rural areas, most of them are daily wagers, self-employed householders and landless labourers. The number of urban poor in India is also not small; the UNDP Report, India: the urban poverty 2009 reports that 81 million Indians subsist in urban areas on incomes that are below poverty line.

Although Indian economy has grown steadily over the last two decades, its growth has been uneven when comparing different social groups, economic groups, geographic regions, and rural and urban areas. Between 1999 and 2008, the annualized growth rates for Gujarat (8.8%), Haryana (8.7%) or Delhi (7.4%) were much higher than for Bihar (5.1%), Uttar Pradesh (4.4%) or Madhya Pradesh (3.5%). Poverty rates in rural Orissa (43%) and rural Bihar (41%) are among the world's most extreme. 80% of Indians live on less then half a dollar a day.

Many intellectuals and policy makers feel that such a dismal poverty situation in India is the direct out come of the Hindu growth rate of about 3.5% per annum between 1950's to 1980's, while the per capita income averaged at merely 1.3%. This low growth rate is attributed mainly to the control and regulations imposed in the economy --- popularly known as the license rate. Many feel that Indian economy which had started out in the 1950's with potential for high growth rates, openness to trade and investment, promotional state, social expenditure awareness and macro stability ended up in 1980's with low growth rates, closed to trade & investment, a licensed obsessed restrictive state, inability to sustain social expenditure and macro instability and crisis. Many therefore argued that economic reforms by promoting growth will help poverty alleviation too. The apparent fall in both rural and urban poverty rates does support this claim but at the same time, critics point out that we should not jump to conclusions. Some of the visible improvements may be due to methodological changes adopted by NSSO in 1999-2000. Further, poverty in relative terms as indicated by the Ginni coefficient shows a worsening over time. And the poorest of the society have not been able to gain anything from growth and have been further marginalized. It is the middle class of India which seems to have got the maximum benefit from reforms. Moreover, the regional impact also varies across India. Hence it is relevant and useful to examine the poverty trends both at national and state level in the post reforms period to draw inferences about the impact of economic reforms on poverty.

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