TRENDS OF INDIA’S POLITICAL ECONOMY

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ABSTRACT

With the change in democratic pattern of the Indian economy, the research paper throws light on the trends on India’s political economy. It is a notion that all was not good before the ‘reforms’ and all began to change thereafter. For a fitting study, the research paper discusses the Indian economy through the perspective of political trends. It is important to understand the nature of the economy, need for reforms and thus the impact of change on the development pattern of the democratic framework.

India is primarily an agrarian based economy. The British colonization in India had a deeper picture to it which was tactically hidden from the masses. The connection of rail routes, textile and steel plants overshadowed the negligence and regional disparities created. Thus, India’s first and initial reforms post independence were launched in the backdrop of a crisis situation. The grim truth of the British misrule was felt in this period where two in every three people in India lived in absolute poverty and India was facing of a major loss of the jute industry of East Pakistan and the port of Karachi.

The then Prime Minister, Pandit Jawaharlal Nehru looked at a developmental model for modernization, which was lauded by many. This approach was based on deferred gratification. It believed in boosting the Indian small scale industries and then giving a plethora of options of cheap chemicals, power etc to the efficient Indian-run companies. This policy did not go well with a country which had 75% of its population still living in rural areas and agriculture contributing to 58% of the total GDP. It made little sense to plug in resources to the development of industries which could be used for improvement and modernization of the agrarian economy.

The advent of emergency and an exposed agricultural failure, led to the fall of Indira Gandhi, which caused a dynamic change in India’s political economy. It was a phase that created opposition parties and saw deinstitutionalization the Congress party. This changed the political landscape of the Indian economy. The average GDP growth in the 1980s was 2.9% which was barely in terms of per capita income. The major aim of these policies was to shift the pattern of capital formation.
By the fall of 1991 India was in a deep hole and suffered from a massive Balance of Payment crisis, was unable to pay off essential imports, ran a soaring deficit and had to borrow from external sources to meet those deficits which in turn led to high inflationary pressure on the country. The economic reforms initiated by PV Narshimhan Rao transformed the future for India and moved it on the path of becoming the next economic powerhouse. Post 1991, the reforms in India have been evolutionary and incremental in nature. The reforms of 1991, was a diversified strategy which compelled the government to constantly be on its toes and thus embark the nation on the path of economic progress.

With the new government in power, India’s political economy is looking towards revival. India has seen a single majority for the first time after the 1980s. The research paper studies the trends in the Indian Political economy and proposes diversified strategies of new governance, through quantitative and qualitative research methodology. The paper raises a question on the feasibility and applicability of the revised model suggested for economic growth.

INTRODUCTION

A country that uses only 2.4% of the world’s land and yet is home to 17.5% of the world’s population, India is the world’s most populous democracy. India has a legacy of colonial stagnation and economic backwardness but in 1947 when India gained independence, the aim of the leaders was not only to do away with the vagaries of poverty but also to turn India into a vibrant, self-reliant global economy.

Since the beginning of the economic reforms of 1991, India has seen a systematic transition from being a closed door economy to an open economy. These reforms have had a far-reaching impact and have helped India unleash its enormous growth potential. Today the Indian Economy is characterized by a liberalized foreign investment and trade policy. India has now developed into a trillion dollar economy with a largely self-sufficient agricultural sector, a diversified industrial base and a stable financial and service sector.

India is on the path to becoming the next world leader. The turbulence being faced by the economies across the world including India, has called for a new wave of reforms to reverse the worsening economic climate of the country. This paper is aimed at analyzing and assessing the current scenario of the political economy, mapping trends and estimating future prospects of India’s political economy, propelling India to become the next super power.
BODY

The paper tries to map India’s political economy over three phases:

- Post Independence phase – Post 1947 phase of building in the economy
- Liberalization and Economic reforms of 1991
- Current Trends

POST INDEPENDENCE PHASE

After years of struggle the dawn of independence was accompanied by an array of socio-economic challenges. The British had eroded India’s copious reserves and had exploited wealth to their advantage. India as a British colony developed in terms of infrastructure and education but these advancements had a deeper and corrosive meaning which was hidden from the masses. The connection of rail routes, establishment of textile mills and steel plants, starting of English missionaries and educational institutions was a scheme with the farfetched objective of making India a British colony. When India secured independence from the British Empire in 1947, the economy which had just taken a beating from the Second World War had to withstand the repercussions of the Indo-Pak partition. India woke to freedom with large scale refugee camps, illiteracy, and malnutrition, lack of a political and administrative support as their major challenges. The most persistent problem was widespread poverty and chronic lack of resources and to address this dual developmental challenge the policymakers had two ideological pathways to choose from.

The Gandhians advocated a self-sufficient but empowered village community as the basis for a new nation and others believed in the power of modern technology and industry to transform the Indian economy. In the early 1950’s India adopted a mixed economic growth model, balancing the role of the state and the market forces. In 1956 India moved towards socialistic pattern of governance. The government under our First Prime Minister Pandit Jawaharlal Nehru embarked on the path of economic progress by redeveloping the indigenous industries which had been completely destroyed under the British rule. He was fascinated by the Soviet Union’s Piatilekta or the Five Year plan and wanted to implement it in India to achieve a state control in finances, a strong public sector and import substitutes. He combined the best of socialism and capitalism and tried to implement Democratic Socialism in India. As a planned economy the first few plans were focused on growth and strengthening of the manufacturing industry with heavy industries being the backbone of the economy. Other principal areas of planning and strategic growth were agriculture and social development i.e. housing and poverty alleviation. During this period about 47% of the population was below the poverty line and more than 70% of the population depended on agriculture for their livelihood. On one hand while there was disguised employment in agriculture on the other hand the industrial sector faced a major shortfall of labor with only 2% of the population employed in the industries. The investment levels were touching rock bottom level and the only two industries that existed were cotton and jute areas which also ended up facing a major setback as majority of the jute producing industries were in Pakistan after the partition which resulted in a major shortfall of raw material.
ECONOMICS REFORMS OF 1991-2014

Rajiv Gandhi came into power in 1984. The country at this time faced a dilemma of excessive balance of payment crisis following the Gulf War and the downfall of the erstwhile Soviet Union. The country had to make a deposit of 47 tons of gold to the Bank of England and 20 tons to the Union Bank of Switzerland which was necessary under a recovery pact which was signed with the International Monetary Fund. With the emergence of liberal thoughts, changes started taking place in the country. In 1991, the Narsimhan Rao government realized the importance of de-licensing and reducing involvement of the government in the economic operations. These liberal ideologies believed in the power of private sector and thus encouraged a greater involvement of the private sector in all the sectors of the economy. Thus, the then Prime Minister of the country P.V Narsimhan Rao’s regime initiated ground breaking economic liberalization reforms. The focus now shifted to privatization and globalization.

The Narasimha Rao government started the liberalization process by abolishing the Licence Raj system which ended various monopolies, reforming capital markets, inviting foreign investment, reforming the trade regime and capital markets. Its goal was to reduce the fiscal deficit, privatize the public sector, and increase infrastructure investment. To open up foreign trade, there were trade reforms and foreign direct investment regulation.

There was reduction in industrial licensing and only 18 industries needed licensing. There was rationalized of industrial regulation. The Controller of Capital Issues was abolished in 1992 which regulated the number and prices of shares a company can issue. The Security Laws (Amendment) and SEBI Act of 1992 were introduced and the equity markets of the country were made available for investment through overseas corporate investors. The National Stock Exchange was started as a computer-based trading system from 1994. Tariffs were reduced, the rupee was made convertible, foreign direct investment was encouraged in priority sectors, India’s equity markets were opened up in
1992 for foreign institutional investors. Inefficient loss-inducing government corporations were also privatized.

A shift in the macroeconomic policies from being a controlled based system to private sector led economic development driven by market forces resulted in a significant increase in the growth rate of GDP and massive transformation of the Indian economy. During the period of economic reforms the economy suddenly started seeing an upturn with the agricultural sector growing at more than 3% and the industries accounting for a steady growth of 7% thus resulting in an overall economic growth rate of 6% from a menial rate of 3% for the very first time since independence.

Increased employment in industries, development of infrastructure, increased exports and import substitution industries resulted in an increased per capita income at an average annual rate of 4% from 1985 to 2000. It also impacted the level of poverty and standard of living in the economy as the incidence of poverty declined from around 44% in the mid eighties to around 26% during the same period. The period is also marked by a rapid growth of Indian exports exceeding 11% per annum as against 8% growth in the world market exports.

The Indian economy which was predominantly known as an agricultural economy saw an increasing shift in the trend of contribution to the GDP. Over the plan periods the share of agriculture has declined from the developmental point of view and an increased contribution of the industries and service sector has been witnessed thus showing signs of becoming a developing economy.

A key reform involved reducing restrictions on foreign direct investment in a subset of industries. Specifically, according to the Industrial Policy Resolution of 1991, automatic approval was granted for foreign direct investment up to 51% in 46 out of 96 three-digit industrial categories.

The outcome of these reorganizations can be estimated by the fact that the overall amount of overseas investment (comprising portfolio investment, FDI and investment collection from overseas equity capital markets) rose to $5.3 billion in 1995-1996 in the country from a microscopic US $132 million in 1991-1992.

The political economy of India also included other later reforms such as forming Special Economic Zones, initiating the Golden Quadrilateral project for constructing a network of highways, enacting the Right to Information Act (2005), Right to Education Bill (2008) and Indo-US civilian nuclear agreement (2008). The impact of all these reforms is reflected in the amount of foreign investment which grew to $5.3 billion in 1995-96 from $132 million in 1991-92.

India had a dream run of five years during 2003-08 as the GDP growth averaged nearly 9 per cent annually for five years. The economy began to slow down from the middle of 2007-08. A 9 per cent growth apparently could not be sustained. A spell of global financial turbulence caused capital outflows and pressure on the exchange rate, but strong policy measures stabilized the currency, rebuilt reserves, and narrowed the excessive current account deficit. Weaknesses remain, however, and include persistent inflation, fiscal imbalances, bottlenecks to investment, and inefficiencies that require structural reforms. After growing by a tepid 1.0% in FY 2012, industry decelerated further to 0.7% in FY
2013. With rising gap between the rich and poor, India suffered from political indecisiveness. India voiced its opinions in the world corporations. The rising security issues have made defence spending the second most in India’s budget only behind subsidies. Thus, expenditure in unproductive areas has lead to a problem of trade deficit. Growing balance of payments imbalance, crippling unemployment has hampered India’s growth rate despite the world recovery and announcement of various policies. These policies failed to reach the poorest of poor and thus India faced stagnant growth in the period from 2008-2014

CURRENT TRENDS
The question still remains that after 67 years of independence and imposition of strong policies. Why is the Indian economy faltering on so many fronts simultaneously? The principle reason is that in the last few years, India has taken growth for granted and thus has invested less effort into raising the quality of growth. The indecisive Indian government failed to bridge the nexus between the connected and the political elite. As India looks towards a change, the year 2014 will be a watershed for India in political and economic terms.

Despite being home to one of the world’s largest pools of digital talent, India invests only 0.6 percent of its planned budget on using digital technologies to enhance the speed and quality of public transactions and services delivery. As a result of poor growth, inflation and fiscal management, the nation finds itself burdened with high interest rates, high operating costs and low consumer and business confidence. The only silver lining to this cloud remains the consumption growth registered by India’s rural economy.

BUDGET ANALYSIS
The new policies promised a faster economic growth and expansion of foreign investment in key industries with better fiscal discipline. Banking-related actions have dominated policy discussion in the last few years. The low levels of allocations in the current Budget indicate the desire to now move the agenda. To that extent, directionally, it is change for the better. Raising capital from domestic markets, however, skeptically viewed from the liquidity or opportunity perspective, actually sets the right tone.

The budget saw huge investment promises in the field of education which clearly indicates at the government’s motive of youth empowerment and development through the path of education and literacy. Investments into setting up of new institutions and programme to bring more people under the radar of education were the highlights of the budget.

Improved governance through technological up gradation was the key take away from the budget. The new budget comes with a promise of efficiency and indicates to take India towards the path of economic recovery and thus ultimately development. Better allocation of funds and inviting FDI and CSR in key areas for improvement is a great sign of an inclusive growth model. To cite a few, slum development would now be under the umbrella of CSR and increasing the limit of FDI in defence.

The budget proves to be 'pro-growth'. India is looking towards improving hospitality to install investor confidence in the economy. What it lacked was a blueprint for economic revival. Boosting manufacturing was a major mention of the budget. However the constraints remain unaddressed.
Industry was looking for three things: a credible commitment that would signal the government’s intention to a) pursue growth-enhancing policies; b) deepen fiscal consolidation and reform subsidies; and c) bring clarity to India’s messy tax regime. This budget will not overly please or displease industry; it was a “safe” budget which leaves a lot of details for the future.

**FUTURE PROSPECTS- ESTIMATES AND PREDICTED TRENDS**

![Economic growth graph](source: IMF, October, 2013)

![Foreign direct investment (FDI) flows](source: ECONOMICS INTELLIGENCE UNIT)

![Industrial production](source: ECONOMICS INTELLIGENCE UNIT)

![Current account](source: ECONOMICS INTELLIGENCE UNIT)
The year ahead

As the Indian growth engine struggles to gain momentum in 2014, the number of heavy “wagons” it must pull has increased. Along with high inflation, the fiscal deficit and the trade deficit constitute two such wagons. The drag will prove enormous, so the engine’s drivers will need to exploit levers such as growing consumption in rural India to keep the “train” on track.

GROWTH

India’s growth engine has slowed considerably. From a solid 6.7 percent increase in gross domestic product (GDP) during 2008-2009, GDP growth is now expected to close at about 5 percent at the end of 2013-2014.

SOURCE: WORLD BANK

As expected, this pessimistic growth outlook has eroded consumers’ confidence. In fact, the number of consumers who believe that the state of India’s economy is worsening is growing every quarter.

The fiscal outlook

The Indian economy remains under extreme fiscal pressure. The economy logged an average fiscal deficit of 5.6 percent of GDP in the last five years (FY2009-FY2013), significantly higher than the 3.6 percent during FY2004-FY2009. And the number promises to hover around 5 percent at the end of FY2013-2014.
Inflation

In the last two years, inflation has become a major barrier to the nation's ability to enjoy the fruits of brisk economic growth. Left unaddressed, inflation could become a permanent feature of India's growth story.

**Food inflation exceeds overall inflation**

![Graph showing food inflation exceeding overall inflation](http://www.pwc.in/en_IN/in/assets/pdfs/budget/2014/union-budget-2014-analysis-booklet.pdf)

**Digitalization**

Rural markets are the silver lining in the otherwise cloudy Indian growth story. Latest National Sample Survey Organisation (NSSO) data reveals that in 2011-2012, expenditure by rural households on non-food products and services exceeded 50 percent of total consumption expenditure. NSSO data further shows that rural consumption has outpaced urban consumption since 2009.

**Internet usage in rural areas**

![Bar chart showing internet usage in rural areas](http://www.pwc.in/en_IN/in/assets/pdfs/budget/2014/union-budget-2014-analysis-booklet.pdf)
Consistent positive income growth and digital penetration in rural India pose unprecedented opportunities. For instance, governments can now share downloadable skilling modules, information on agricultural technologies and other value-creating information with rural populations over mobile Internet at affordable prices, And businesses can offer insightful product-related guidance to their rural customers in more interactive formats.

**Business confidence**

India Inc. is facing stagnating industrial production, rising labor costs, inflationary pressure and high interest rates paired with a weakening rupee. As a result, its self-confidence is slipping despite new sources of demand arising in rural regions. The latest Confederation of India Industries (CII) Business Confidence Index fell 5.5 points to 45.7 for the July-September 2013 quarter, down from 51.2 in the previous quarter and sinking to its lowest value ever.

**Business confidence index**

![Business confidence index chart]

The dip below the psychological 50-level mark does not augur well for Indian industry, because it mirrors the underlying weakness in the economy. Eroded business confidence has resulted in shrinking capital investment in key sectors of the economy.

In this backdrop, the new government, a single party majority government was formed. With increased expectations the budget 2014-15 was delivered by finance minister Arun Jaitley.
CONCLUSION

India has seen various colourful years of ups and down through the phases. India has come a long way in moving towards development from the British colonization era. The question still remains, is India really shinning or are these mere policies and frameworks. The main challenges India faces are implementation and enforcement, bridging the gap between the rich and the poor and spreading and distribution of benefits to all parts of the society. The implementation of policies and the impact of the new government have to be studied. Will the government stand up to the expectations and anticipations it was elected is a question in itself.

In conclusion, after analyzing the trends and their impact, it is evident that India has a strong policy framework and policies. What India needs is it impacts to reach to the lowest strata of society. The anarchic and traditional policies need to be amended with changing times. As in the 21st century no country can live in isolation and thus is more vulnerable to external and global conditions. Dealing with global interactions and maintaining economic stability are of utmost importance in the constantly changing business and socio-political environment.

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