

Economic Reforms

Liberalisation, Privatisation and
Globalisation

India's Economic Reform

- A move away from Inward looking economy to a more open economy or export oriented strategy of growth.
- That in turn means doing away with government intervention as much as possible and giving greater freedom to private enterprise operations.
- Policy focus is on –
- Deregulating Indian industry;
- Allowing the industry freedom and flexibility in responding to market forces and

India's Economic Reform

- Providing a policy regime that facilitates and fosters growth of Indian industry to let the entrepreneurs make investment decisions on the basis of their own commercial judgment.
- Since the attainment of technological dynamism and international competitiveness requires that enterprises must be enabled to swiftly respond to fast changing external conditions that have become characteristic of today's industrial world, policy changes is aimed at enabling that.

Meaning of Liberalisation

1. Dismantling of industrial licensing system and dilution of MRTP Act;
2. Reduction in quantitative restrictions in imports as well as rate of import duties;
3. Reductions in control on foreign exchange;
4. Financial and banking sector reforms;
5. Reductions in the level of corporate and personal income taxes;
6. Reductions in restrictions on Foreign Investments (Direct as well as Portfolio)

Meaning of Liberalisation

7. De-reservation of basic industries, power, transport, banking etc.
8. Privatisation of PSUs (Public Sector Units)

Measures towards Globalisation

1. INVESTMENT REFORMS

Allowing entry of MNCs by scrapping restrictive laws like FERA and changing into FEMA

Permitting Indian companies to collaborate with foreign companies in the form of joint ventures

Liberalising inflow of foreign direct investment,

Incentives for MNCs and NRIs for investing in India

Measures towards Globalisation

Expanding list of items for automatic approval of foreign equity

2. TRADE REFORMS

Import liberalisation – reduction of import tariffs, replacing import licenses with import tariffs, removing quantitative restrictions on imports

Removing export subsidies, replacing licenses of exports with export duties, low flat tax on export income

Decanalising oil and agricultural trade

3. FINANCIAL AND BANKING REFORMS

Allowing FIIs to invest in Indian Capital Market;

Allowing Indian companies to procure capital from foreign countries through “Euro Issues” and “Global Deposit Receipts” Is to invest in Indian Capital Market;

Allowing Mutual Funds to invest in foreign companies

Interest Rate to be market Determined

Lowering SLR and CRR in banks

Allowing private sector into banking

Measures towards Globalisation

4. EXCHANGE RATE REFORMS

Move towards flexible exchange rate; LERMS
Liberalized Exchange Rate Management
System

Flexible Exchange Regime or Managed float

5. FISCAL CONSOLIDATION

Reduce Fiscal Deficit

Reduction in Public Expenditure

Tax reforms: VAT and Income tax and Corporate
taxes

Privatisation

Measures towards Globalisation

6. INDUSTRIAL REFORMS

- De-Licensing;
- De-reservation;
- Broad banding;
- Dilution of MRTP Act

Major Policy Reforms Contd..):

- Fiscal Consolidation
- Tax Reforms: VAT and Income tax and Corporate taxes
- Subsidies
- Initiatives in the Agricultural Sector

Trade and Exchange Rate Policy

- Trade liberalization and convertibility on current account
- **Flexible Exchange Regime or Managed float**
- **Steep Reduction in Import Tariff** since early 1990s
- **FDI and Investment – Efficiency Issues**

Impact of NEP on Industry

- The external policies in 1960s, 1970s and 1980s were guided by the principle of import substitution, which had been prompted to some extent because of scarcity of foreign exchange. The strategy therefore involved, restricting imports through quotas and high tariff rates as well as there being restrictions on FDI, foreign collaborations, import of technology.
- The general trade and industrial policies that India adopted till mid-80s and till 1990s insulated the Indian industry from competition, domestic as well as foreign.

Impact of NEP on Industry

- However, the environment has changed drastically since New Economic Policies were initiated in 1990s. Globalisation has led to opening up of markets leading to intense competition.
- There is greater competition in domestic market with imports of high quality goods from developed countries and low priced goods from developing countries. Competition has further intensified with the arrival of MNCs as the restrictions on FDI have been removed.

Impact of NEP on Industry

- Thus Indian enterprises, small and large have been forced to improve their quality and productivity in order to (i) compete with imported goods or with goods produced by MNCs; (ii) export successfully without government support.
- A study, based on CMIE (Centre for Monitoring Indian Economy) database to test competitiveness of domestic private sector companies with respect to foreign companies, show that competitiveness of Indian companies; measured in terms of cost management and profitability lag behind that of foreign firms.

Impact of NEP on Industry: Competitiveness of Indian Industry

- Raw materials expenses to net sales lower for foreign companies by 5 per cent vis-à-vis Indian companies. Cost of production to net sales too lower for foreign companies.
- On the profitability side, Profit after Tax (PAT) to capital employed was 5 per cent higher for foreign companies.
- ROCE for the Indian firms fell from 6.3% in 1993-94 to 1.6 in 1999-2000. Foreign firms' ROCE too fell from 10 to 7 per cent in the same period. However there has been increasing gap between the two set of firms.

Impact of NEP on Automobile Industry

- The automobile industry, comprises of four segments, the passenger car and jeep industry, commercial vehicles, two and three wheeler industry and automobile components
- **First Automobile Policy in 1949**, which banned import of completely built automobiles but firms engaged in assembling vehicles from completely knocked down units were permitted to operate.
- By late 1960s, bias against passenger car industry, which was absent earlier came into play. In 1968, for the first time, Statutory Price Control was imposed on the passenger car, segment as it happened to be a 'luxury' good.
- Unlike the '50s and '60s, the period of '70s saw poor performance by car manufacturers. Low demand, high prices, high input costs, low scales of production and low profit were some of the highlights. However, things didn't look up even after Statutory Price Control was lifted in 1975.

Impact of NEP on Automobile Industry

- 1993: De-licensing of the automobile industry.
- Removal of FERA and allowing 100% FDI, saw host of joint ventures entered into by PA (with Peugeot), HML (with GM), TELCO (with Mercedes, Daimler-Benz, Mitsubishi). New entrants like DCM (with Daewoo), Kirloskar (with Toyota). Hyundai has 100% owned subsidiary in India.
- Reduction of import duties on parts and components, in alignment to ASEAN rates.
- Completely Built Up (CBU) allowed since 2001

Impact of NEP on Automobile Industry

- Currently domestic market size is to the tune of 7,55,771 cars. Number of models has gone up from 4-5 in mid-1980s to 25-26 in 2002-03. Over and above this, exports had been 1,30,000 in 2003. Exports projected to grow at 10-15% in the coming years.

Manufacturing Hub for vehicles

- Hyundai- Export base for small cars.
- Ford exporting CKDs of Ikon to S. Africa and CIS countries
- Tata Indica being sold in Europe under Rover brand.
- M&M targeting S. Africa, China, Europe, Russia for export of Scorpio and Bolero.
- Maruti exports cars to EU.

Production of Passenger Cars

Year	No. of Cars
1960	19,097
1970	35,205
1980	30,538
1985	1,02,456
1990	1,76,609
1996	3,76,263
2003	7,55,771

CASE – Ashok Leyland

- **Ashok Leyland**: one of the largest manufacturer of commercial vehicles in India. They were the first to introduce CNG buses in Delhi.
- Entry of global companies like GM, Ford, Honda, Toyota, has forced Ashok Leyland to achieve international competitiveness to survive.
- Therefore company is now focusing on maximum effective utilisation of resources, they have started cost saving measures on operation side, including VRS. They are more consumer-centric now.

Impact of NEP on Steel Industry

1950-70: Pre-liberalisation phase – Nature of controls

Integrated Plants/Primary Steel Sector

- Industry being one of the key inputs in infrastructural sectors and heavy industry goods, was completely regulated through compulsory licensing for capacity expansion, investment. As a result most of the capacity expansion in the pre-liberalisation phase has been in PSUs through, SAIL, Rashtriya Ispat Nigam Ltd. (RINL). TISCO being the only private enterprise.
- Only private player, TISCO, not allowed to increase capacity, till the late 60s. Virtual monopoly of PSUs

Impact of NEP on Steel Industry

1970-91

Secondary Steel Sector

- However, since late 60s, private sector allowed in the secondary sector, using steel scrap for producing steel. And large number no. of small firms or mini-steel plants (MSPs) emerged in this sector in the 1970s and 1980s, though its share was very small in total capacity. Some liberalisation: MSPs allowed to import scrap, customs duties and excise duties lowered for encouraging growth of MSPs. Some selected MSPs, also permitted to diversify production into high grade alloy steel.
- **Primary Steel Sector**
- With nationalisation drive all PSUs brought under one management, SAIL. Also TISCO allowed to go in for modernisation, with help from the state as well as loan from World Bank.

Impact of NEP on Steel Industry

Post-liberalisation phase: 1991 onwards

- De-licensing private investment in steel, abolition of the system of administered prices for steel. Most restrictions lifted on private domestic and foreign companies.
- De-reservation of steel from public sector, no new projects to be in the public sector.
- Import duties on various steel products reduced from the range of 20 -85% to 5-30% by the end of 1990s, forcing domestic firms to be more quality conscious and efficient.
- **Greater no. of private players, like, Lloyds, Sunflag, Essar Gujarat, Jindal Strip. Number of steel plants have gone up from 7 in the pre-91 period to 16 in post-91 period.**
- **Modernised plants and technology, like midi-plants, used by the private firms, more in sync with world state of production.**
- **From being a importer in the 70s, there has been modest rise in exports in the 1990s.**

Impact of NEP on Steel Industry

- However over-capacity in domestic steel industry due to sudden rise in no. of players
- Global over-capacity in steel industry of Korea, Japan, leading to dumping of cheaper imports. Sharp fall in domestic and international demand have plagued the industry since 1995-96 to about 2002-03.
- However, since 2003 world demand has picked up Indian steel Industry doing well.
- Even then, inferior technology of Indian industries makes them energy inefficient and hence places India at a disadvantageous position in terms of cost of production and quality of products.