

STRUCTURAL ADJUSTMENT PROGRAMME: INDIA

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Introduction

Structural adjustment Policies (SAPs) have been implemented for many decades and have become the dominant framework for economic development in many countries, mainly in the global South in the 1980s. SAPs require countries to adopt and implement specific policies in order to receive a loan, which are the basis for a conditional lending principle. Thus, economic reforms with respect to SAPs – typically free market reforms – are sought to lead to lasting economic stability, sustainable growth, and functioning market mechanisms in accordance with the global economy in recipient countries. They are typically advocated for and provided by major international financial institutions (IFIs), such as the International Monetary Fund (IMF) and the World Bank, to low and middle-income countries.

Like other Third World countries, India was forced into adopting a SAP along the lines drawn up by the IMF - World Bank combined. There were various gears that were required to be stepped up for satisfying this objective which includes: cutting down government expenditures, tightening of monetary policy, easing economic policies to bring foreign capital and technology, tax reforms, a suitable trade policy etc. In order to suffice these purposes, a series of reforms were introduced in the country in the form of New Economic Policy (NEP) of 1991. Following this, a wide range of changes in public policy have taken place towards liberalization, globalization and privatization that have been aimed to correct India's crisis-ridden economy.

Review of Literature

Since the 1980's, SAP's have been continuously updated and progressed to bring about social and economic developments. Research conducted by the Public Interest Research Group, New Delhi (1992) gives a brief overview about the Structural Adjustment Policies and how they are being planned to adapt in the Indian context. It concludes that the reality of these SAP's is not in relation with their previously set expectations which needs to be bridged for these policies to be effective in the long run. The states should strengthen and support civil societies rather than

subsidizing a few groups. Besides, there should be democratization, towards a more democratic political regime, of the International Financial Institutions like the IMF and the World Bank.

A study published in the Journal of Rural Development by Kyeong-Duk Kim (1997) analyzes the impact of structural adjustment policies across the world and gives a theoretical analysis of Structural Adjustment in terms of unemployment, poverty and food availability in India. It uses various official statistical sources including graphs, tables and comparison charts from the IMF, World Bank, Government of India's Economic Survey 1995-96, etc. to draw an analysis that these reforms can only be effective in the long run.

Findings by Ahmed and Lipton (1997) determine the impact of Structural Adjustment Policies on rural livelihoods and its linkage to sustainability and conclude that the declining support of SAP's is due to their inefficiency in addressing issues like inequality of rural assets, underdeveloped farming techniques and an unstable reform system. It states that there is less overall systematic improvement or decline in the quantity, quality or sustainability of rural livelihoods and hence the government should develop reform policies beneficial for all, not just a certain class.

A study by KJ Joseph (1996) points out how the reforms have been implemented in different Indian sectors including industrial, small-scale, public and agricultural sectors. It highlights the impact of the SAPs in these sectors and concludes that there is a wide scope for improvement in both formulating and implementing policies.

India's Economic Crisis before 1990's

Agriculture has been the main economic activity of India since the time of independence where old and outdated methods of farming were used in the sector. As agriculture was excessively dependent on rainfall, the available resources and technology were not utilized to their full potential. However, agriculture alone was not facing problems as during the 1950-1980's, industrialization was almost limited to a few jute mills with one or two steel plants in operation. The second phase of the Industrial Revolution in India began in 1965 and continued for 15 years, until 1980. However, during this period, the production growth rate declined from 9% to 4.1% (IMF Working Paper). Hence, the Government of India decided to bring balanced economic development not only on the social level but also at the regional level through a series of five-year plans. An organization called the Planning Commission of India (Currently NitiAyog) was established in 1950 to initiate planned development in the Indian economy. A deep respect towards the Gandhian philosophy on self-reliance made the Indian economy an inward-looking one in the post-independence era. But due to the inward- looking character of the economy, protection on imports was levied through tariff and non-tariff barriers. Moreover, due to

government intervention in most industries, private entrepreneurs were facing a complex structure of licensing requirements in order to start business. The protection of imports and opposition of exports along with government interference caused a state of economic suppression in the country. India neither could develop a good international market for its products nor could it build an industrial economy in the home ground. Additionally, since the economy experienced a severe drought for two consecutive years in 1979 and 1980, not only the agricultural but also the industrial output got disrupted.

Indian Economic Situation in 1990 - 1991

The Indian Economic Crisis during 1990's can be attributed to both International and Domestic factors. India exported 25% of goods to the Soviet Union (USSR) before 1990. However, when the USSR disintegrated in 1990, from a high point of Indian exports of Rs.5,255 crores to the then Soviet Union in 1990-91, exports declined to about Rs.1,700 crore in 1992-93. At the same time, The Gulf War broke out as Iraq invaded Kuwait to capture its oil producing industries (University of North Bengal). The situation was further worsened with the entry of the USA into the war. Supply shortage of petroleum, and oil lubricants saw a massive price increase, internationally. The cost of the crisis to India was estimated at around \$1.6 billion making India the third most affected country by the war, in absolute terms. An Economic Survey conducted by the Indian Government (1991-92) had stated that: "*The immediate cause of the loss of reserves beginning in September 1990 was a sharp rise in the imports of oil and petroleum products (from an average of \$ 287 million in June-August 1990, petroleum products imports rose sharply to \$ 671 million in 6 months). This accounted for the rise in the trade deficit from an average of \$ 356 million per month in June-August 1990 to \$ 677 million per month in the following 6 months.*"

Domestically, as India saw greater imports and public expenditure, it was found struggling with the Twin Deficit Problem. Twin Deficit theory correlates with the fiscal deficit and the current account deficit which means when the fiscal deficit rises, the current account deficit also widens. Nevertheless, the Indian government was already in huge debt, both domestically and internationally. There was a shortage of foreign exchange reserves and India was left with limited import cover. According to the Economic Survey (1991-92): "*Throughout the eighties, all the important indicators of fiscal imbalances were on the rise. These were the conventional budgetary deficit, the revenue deficit, the monetized deficit and gross fiscal deficit. Moreover, the concept of fiscal deficit is a more complete measure of macroeconomic imbalance as it reflects the indebtedness of the Government. This gross fiscal deficit of the Central Government has been more than 8% of GDP since 1985 – 86, as compared with 6% in the beginning of 1980s and 4% in the mid – 1970s.*"

What is a Structural Adjustment Programme (SAP)?

In 1992, Indian Prime Minister P.V Narasimha Rao along with Finance Minister Dr. Manmohan Singh negotiated with the International Monetary Fund (IMF) and the World Bank to launch suitable SAPs in India. SAP refers to policies prescribed by the IMF and the World Bank to developing countries for receiving financial assistance or loans. SAPs were initially designed as short-term strategies to stabilize indebted economies, and then provide long-term Economic Recovery Programs (ERPs) to restructure the economies through extensive liberalization, privatization, and globalization. The objectives of the reforms were based on the clear recognition of the need to integrate the global economy through trade, investment, and technology flow and to create conditions that would give domestic entrepreneurs an environment comparable to those in other developing countries. Overall, the three main objectives of SAPs include boosting economic growth, addressing balance of payments of deficits and reducing poverty.

A Brief Review of India's SAP

The objectives of the reforms, as per the discussion paper brought out by the Ministry of Finance in July 1993 were: *"...to bring about rapid and sustained improvement in the quality of the people of India. Central to this goal is the rapid growth in incomes and productive employment... The only durable solution to the curse of poverty is sustained growth of incomes and employment... Such growth requires investment: in farms, in roads, in irrigation, in industry, in power and, above all, in people. And this investment must be productive. Successful and sustained development depends on continuing increases in the productivity of our capital, our land and our labor. Within a generation, the countries of East Asia have transformed themselves. China, Indonesia, Korea, Thailand and Malaysia today have living standards much above ours... What they have achieved, we must strive for."* Hence, the New Economic Policy launched formally by finance minister Dr Manmohan Singh under the leadership of P.V. Narsimha Rao, the Prime Minister of India is by far considered one of India's most successful policies due to the following reforms: -

(A) Financial Sector Reforms - The financial sector in India is regulated by the Reserve Bank of India (RBI) which gives various norms and regulations to be compulsorily followed by other Indian Financial Institutions. Earlier, the RBI used relevant statistics to decide the amount of money that the banks could keep with themselves, interest rates, nature of lending to various sectors, etc. Hence, reducing the role of RBI from regulator to facilitator of the financial sector was a key reform as now the financial sector may be allowed to take decisions on many of these matters without consulting the RBI.

(B) Tax Reforms - The reforms in a government's taxation and public expenditure policies combine to make the fiscal policy, concerned with tax forms. There were majorly two types of taxes - Direct taxes which were levied on individual income or business profits and Indirect Taxes which were levied on consumption commodities. The highest marginal rate of personal income tax was 56% in 1991 which was reduced to 40% in 1992-93. Therefore, the following years saw a continuous reduction in the taxes on individual incomes as high rates of income tax were found to be an important reason for tax evasion. Also, the average amount of customs duty drastically decreased from 200% in the 1960's to only 65% in 1990's. In 2016, Goods and Service Tax (GST) was further introduced as an indirect destination-based tax to bring together all multiple indirect taxes, including VAT, Central Excise Tax, Entertainment Tax, Luxury Tax, Entry Tax and Service Tax Act.

(C) Industrial Sector Reforms - The New Industrial Policy established in 1991 sought substantially to deregulate industry to promote growth of a more efficient and competitive industrial economy. Industrial licensing, an authority issued by the government organization to permit the institution or organization for starting an industry or to start a certain function, was therefore abolished for all projects except in 18 industries which included defense, energy, and production of necessities. With this, 80% of the industry was taken out of the licensing framework. Moreover, The Monopolies & Restrictive Trade Practices (MRTP) Act was repealed to eliminate the need for prior approval by large companies for capacity expansion or diversification. The policy also encouraged disinvestment of government holdings of equity share capital of public sector enterprises.

(D) Trade Reforms - Prior to 1991, Imports in India were regulated by a positive list of freely importable items. However, from 1992, imports were regulated by a limited negative list and the Trade Policy of 1 April 1992, freed imports of almost all intermediate and capital goods. India was also following a regime of quantitative restrictions on imports to protect domestic industries. This was encouraged through tight control over imports and by keeping the tariffs very high. Another measure taken was to reduce export duties to increase the competitiveness of Indian goods in international markets.

(E) Foreign Exchange Reforms - In 1991, the rupee was devalued against foreign currencies as an immediate measure to resolve the balance of payments crisis. This led to an increase in the inflow of foreign exchange leading to free the determination of rupee value in the foreign exchange market from government control.

Criticism of Structural Adjustment Policies

While economic reforms may be justified on the basis that they have helped to improve the growth rate of GDP, they cannot be justified in reducing unemployment and poverty to the desired extent. Another major drawback of economic reforms is neglect of agriculture, more especially in terms of reducing investment in irrigation by the public sector. Economic reforms have also not been fruitful in facilitating industrial growth, majorly in electricity generation and mining. The failure was also manifest in an ineffective tax and disinvestment policy.

(A) Neglect of Agriculture - Public investment in the agricultural sector, including irrigation, roads, market linkages, power and research and extension has been narrowed down in the reform period. The number of policy changes did not provide any major advantage to agriculture and included reduction of import duties on agricultural products, removal of minimum support price and lifting of quantitative restrictions on agricultural products which adversely affected the Indian farmers who faced International Competition.

(B) Low Level of Industrial Growth - Due to globalization, there was a greater flow of goods and capital from developed countries and as a result, domestic industries were exposed to imported goods. The infrastructure facilities, including power supply, remained inadequate due to lack of investment. As cheaper imports replaced the demand for domestic goods, domestic manufacturers started facing competition. For example - Chinese goods posed a big threat for Indian manufacturers.

(C) Ineffective Tax and Disinvestment Policy - The government decided to always fix a target for disinvestment of Public Sector Units (PSU'S). For instance, in 2014-15, the target was Rs. 56000 crore, whereas achievement was about Rs. 34500 crore. The reason for this is the undervaluation of PSUs assets and them being sold to the private sector. Some disinvestments of the Public Sector were used to compensate for shortage of government revenues rather than using it for development of PSEs and building social infrastructure in the country. Furthermore, tax reduction was done to generate larger revenue and to curb evasion of tax which nevertheless did not result in an increase in the tax revenue for the government. The scope for raising revenue through customs duties was decreased by Tariff Reduction and tax incentives were provided to attract foreign investment which in turn further reduced the scope of raising tax revenues.

Conclusion

India's decision to adopt the Structural Adjustment Policies and the economic reforms in 1991 seems justified to improve the crisis-ridden economy of the 1980-1990's. The most important theories for explaining India's policy choice are those focused on interest groups and international financial and political institutions. The policies covered a wide range of sectors including incentives for both the private and public sector. Several concessions were given to

certain groups, including the labor and rural sector, but hardships and discontentment among many groups of farmers and industrial workers was unavoidable. Even though the policies focused on Liberalization, Privatization and Globalization mechanisms for the country, it was not able to fully cover the previously existing loopholes in the economy. In conclusion, the Indian government showed that it could meet both the demands of the Indian population and the International Financial Institutions by introducing vast economic reforms and making efforts in implementing them to their full capacity. Therefore, even with some discontentment among the nation, the policies were not withdrawn and kept for the Indian nation to work on their lines.

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