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INDIAN ECONOMIC POLICIES

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Abstract: Economic policies are basically the aims and objectives stated to be achieved using various instruments defined by the government towards economic growth. It is also called a structural response to resolve economic inequality and imbalances.

In this article, we will get up-to-date insight to economic policies in India. This study determines the economic growth of India and factors which sustain the same, such as investment and savings, cross-border commerce, and productivity. All in all, we will discuss some major economic policies in detail which are important in the economic growth of the country.

In order to fulfill the above objectives, this study will be based on secondary data collected from various online sources, journals, government reports, and others. It is observed that growing unemployment, individual and regional inequality, budget constraints, and infrastructure limitations are some of the major challenges behind slow economic growth.

Keywords: Economic development, economic policies, economic policies in India, economic growth, unemployment, economic inequality

1. INTRODUCTION

By manipulating social and economic variables, the government plays a vital role in allocation of resources to achieve desired economic growth with social stability and justice. An economic policy is basically associated with all or one of three major questions at macro level – why, how, and for whom to produce. It is generally believed that economic considerations guide economic policymakers supported by economic theories to frame several elements of economic policies. However, decisions related to economic policy (to be specific) and general public policy are taken by representatives who have been elected at various levels.

Basically, these are major political decisions. The "pulls and pressure" are exerted to control the process of formulation of economic policies by legislators, public opinion with mass media, judiciary, bureaucracy, expert panels, trade bodies, and NGOs. Hence, interaction between economics and policies are helpful to gain better insight to important questions related to implementation, making, and failure of economic programs and policies.

1.1 BACKGROUND

Most time-tested and trusted approaches across the world to boost standard of living and curb poverty are sustainable and heightened economic growth. Economic policies of India are often affected by the agenda of political parties due to the functional democracy of the country as they fight for popularity in terms of infant mortality and literacy. Hence, political economy is a major concern in formulation of economic policies. It is important to find out the policies that can be implemented for the potential welfare of people.

From the 15th to 18th centuries, India was very prosperous, during which it generated plenty of industrial and commercial skills (Clydesdale, 2007). The per capita income of Indians started to decline in the 16th century and Indians faced negative economic growth and poor salaries for over 400 years, despite the growth of the country's population. India was economically and socially backward during independence. The Constitution framed some "directive principles" to resolve these issues (Bosworth & Collins, 2008). According to "Directive Principles", states have been responsible to ensure that all the citizens have the right to proper means of livelihood and fair distribution of resources available in the country for common welfare and distribute wealth equally, without making it available only to a few people.

Before Independence, India had 56.4% of the UK's GDP in 1600 and it remained constant until 1947, when the per capita GDP of the UK was 10.3 times higher than the GDP of India. During independence, it declined for a while. In 1757, the per capita GDP of the UK climbed from 2.63 to 5.22 in the year 1857. In 1947, it remained 10.29. The population of India was also reduced for the first time since 1757 due to decline in British population in 1947. However, it significantly increased after independence, which resulted in a decline of India's GDP as compared to Britain, according to the Finance Commission report (1994) by the Government of India. This article is aimed to discuss major economic policies that play a vital role in economic growth of the country and factors boosting economic growth of India.

1.2 RESEARCH QUESTION

- What are the important economic policies in India playing a vital role in economic growth?
- What are the factors improving economic growth of India?

1.3 RESEARCH OBJECTIVES

- To discuss major economic policies vital for economic growth of India
- To explore factors promoting economic growth in India

2. RESEARCH METHODOLOGY

In order to fulfill the research objectives mentioned above, secondary data will be used in this study, which is collected from various research articles, journals, reports from various institutions, and other sources.

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3. ANALYSIS OF STUDY

3.1. What are the important economic policies in India playing a vital role in economic growth?

Reason behind the formation of economic policies by the government seems to be naïve but still an important concern. It is because the answer starts the most ceaseless and interesting debate on Economics. Here are some of the most important economic policies followed in India and play a vital role in country's growth (Shruti, n.d.) –

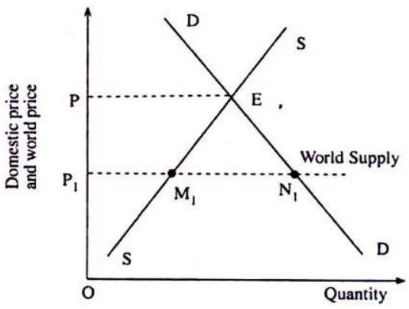
3.1.1. INDUSTRIAL POLICY

On the basis of the principle of "mixed economy", the first Industrial Policy was declared in the year 1948 which clearly earmarked the operation areas in private and public sectors. In 1956, the Industrial Policy was revised which focused highly on expanding the role of the public sector under the "Mahalanobis strategy of Industrialization" as part of "Second Five Year Plan (1956-61)". In 1991, the unexpected changes in policies were required due to the sudden economic crisis and the nation reached the crossroads. The liberalized Industrial Policy was introduced by the Government of India on July 24, 1991, making a steep departure from Industrial Policy 1956. This policy was a bold move by the government for deregulating the economy to make Indian industry more internationally and domestically competitive. This policy made a significant leap for liberalization and privatization. It focuses on disinvestment of equity and has been a welcome change for FDI or "foreign direct investment". It was aligned with existing economic strategy to liberalize the traditional commercial and industrial policies in order to gain competitive edge, improve efficiency, and achieve modernization of economy.

3.1.2. TRADE POLICY

Each country has its own production capability as part of free trade. Each country can benefit from trade which gives a comparative advantage. Commercial policy has been through a great change when protectionism was removed across the world after World War II (1939-45). Some trade was better than no trade at all at that time. It goes without saying that free trade was supposed to be the best. Figure 1 suggests the Demand Curve (DD) and Supply Curve (SS) of consumers and producers in India, respectively. E is the intersection of these curves. This way, OP is the pre-trade price in India. The price in the global market is lower than domestic OP when a commodity is exported from the country.

Figure 1 – Flow of Free Trade Process



Source – Economics Discussion

Suppose OP is the world price. The OP in India is equivalent to OP of the world price with opening of trade and without tariff. But why a foreign country deal with a market where the price is higher than the international price when trade is free? It is when the competition would fall to OP between the countries' prices in the Indian market. The supply would be reduced from PE to P_1M_1 by the Indian producers at a lower price, while there would be a hike in demand by M_1N_1. The supply curve is shown in the horizontal line for import (Figure 1). The supply curve is very elastic and the gap between demand and supply when trade opens to M_1N_1 should be filled by foreign imports. The volume of trade relies on the demand and supply under free trade.

3.1.3. MONETARY POLICY

Also known as "credit policy", the monetary policy is based on the rate of interest and credit availability to affect the overall monetary supply. In the 1950s, RBI had the hallmark of "controlled monetary expansion" in its monetary policy. To support the process of structural adjustment and macro-stabilization programs introduced in the mid of 1991, monetary policy was revamped. Market-based reforms like entry of foreign and Indian banks, liberalization of interest rate, and development of alternative monetary controls are being made regularly with constant measures of monetary policy.

3.1.4. AGRICULTURAL POLICY

There are two major issues India faced just after independence – lack of raw materials in industries and food crisis. Fixing the imbalances in food grain and commercial crops supply and infrastructure development were the main goals after partition and to meet the goals of the First 5 Year Plan. Irrigational power and agriculture were, hence, accorded with top priority. Backwardness and low productivity are some of the characteristics of Indian agriculture. Agriculture reforms were badly needed. Technological and institutional improvements are needed in agricultural productivity.

3.1.5. FISCAL POLICY

It is another important arm of economic policy focused on expenditure, taxation, and borrowing. It has evolved over time and led to great dependence on indirect taxes in a tax structure. It couldn't control unplanned expenditures and generated re-investible surpluses. Then, the government ended up with public borrowing and deficit financing. All these led to more fiscal deficits. In

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the early 1990s, the situation got even worse when there was a significant rise in fiscal imbalances. Initially in the mid of 1991, major fiscal measures were introduced. Since then, fiscal policies were aimed to promote development of the economy led by the market. For example, the government is constantly making efforts to simplify both tax laws and tax structures even today.

3.1.6. INDUSTRIAL POLICIES

Industrial policy should be announced by the government in a mixed economy by indicating what should be in the domain of private enterprise and of state government clearly. Co-existence of public and private sectors refers to a mixed economy. On April 30, 1948, the Government of India made a policy resolution named "Industrial Policy Resolution" or "First Industrial Policy Resolution". It had the following guidelines –

- State must have a complete monopoly on strategic and basic industries like atomic energy, railways, and arms and ammunition.
- The second group covered major industries like iron and steel, coal, manufacturing of telephone, telegraph, mineral oils, wireless devices, ship-building, etc. The State became solely responsible for all developments in future and existing industries could work for over 10 years. Thereafter, the State will oversee the situation and review the needs for nationalization.
- The third group consisted of 18 industries, such as tractors, automobiles, tools, etc. to be added in the private sector, under government supervision and regulation.
- Private sector could handle all other industries not mentioned above. However, when needed, the State may intervene and/or participate in such activities.

3.1.7. NATIONAL AGRICULTURAL POLICY

Considering the challenges in the 1990s related to the agricultural industry, the government had introduced the "National Agricultural Policy (NAP)" in 2000. Here are some of the objectives described in the policy document –

- Over 4 p.c. of annual growth;
- Efficient use and conservation of resources like water, soil, and biodiversity;
- Demand-based growth to meet domestic market demands and enhance benefits from agricultural products' export;
- Widespread growth across farming regions; and
- Sustainable economic, environmental and technological growth.

The NAP-2000 introduced measures in different areas to achieve the above objectives, such as nutritional and food security, sustainable agricultural growth, transfer and generation of technology, investment and incentives for farming, risk management, and institutional structures.

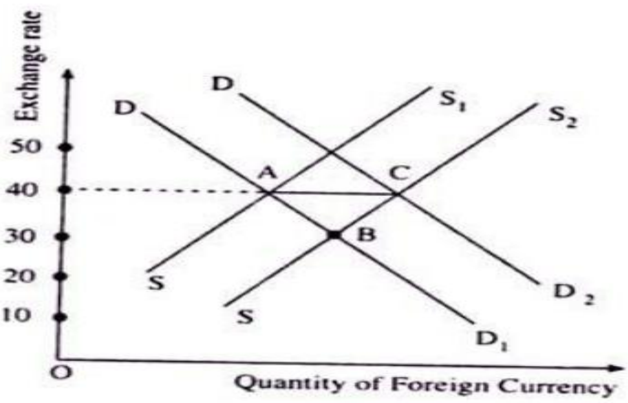
3.1.8. INTERNATIONAL TRADE POLICY

Whether external trade must be regulated or allowed to grow significantly is a controversial matter. The position of the country in this matter is widely known as trade policy or commercial policy. Hence, the trade policy of the country is based on free trade over protection. Free trade refers to no trade restrictions. It includes absence of quotas, tariffs, subsidies and taxes on production, exchange limitations, consumption, and factor use. On the other side, protection refers to trade with restrictions. Protective trade imposes duty and tariff while free trade removes tariff. Government can intervene in trading in case of protective trade. Almost all countries adopted free trade policy in the world in the mid-19th century. Great Britain was the leader in this policy at that time. But this tide no longer flourished in the beginning of the 20th century. The protective or restrictive trade policy was followed in India till June 1991 when liberalization was ushered in.

3.1.9. EXCHANGE RATE MANAGEMENT

Fixed Exchange Rate and Flexible Exchange Rate are two tried and tested exchange rates in India. The IMF tried the fixed exchange rate when it was banned during 1947 to 1971. The global exchange rate after 1971 became floating and flexible. The IMF is currently following the "managed floating system". As the name suggests, fixed exchange rate doesn't change or fluctuate at regular intervals in a given exchange rate.

Figure 2 – Fixed Exchange Rate



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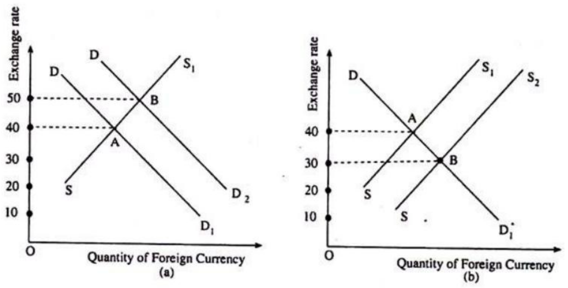
To keep exchange rates stable and fixed, central authority or government intervenes in the foreign market. Par value is the rate to fix the currency. This par value can move in "band" or narrow range of $\pm$1%. If there is a negative sum of capital or current account, it refers to excess domestic currency in global markets. The government uses official foreign exchange reserves to acquire domestic currency. Suppose demand for goods from the US rises in India. The increased import demand leads to a rise in supply of INR in the exchange market to attain USD. In Figure 2, Demand curve is DD_1 and supply curve is SS_1, intersecting at A when exchange rate for US$1 is Rs. 40. At the same time, the DD_1 is intersecting at B when SS_1 is moving to SS_2.

It shows the exchange rate falling. RBI will call for more domestic currency (INR) in exchange for USD to avoid this fall further. It will lead to upside pressure in the exchange rate and inhibit the excess supply of INR. This way, DD_1 will move towards DD_2 and the old exchange rate will be restored at C. Hence, foreign exchange reserves must be abundantly available to maintain a fixed exchange rate. A country cannot acquire sufficient domestic currency with inadequate reserves of foreign currency and domestic currency will be devalued.

On the other hand, the exchange rate may vary due to the influence of foreign exchange market under a floating or flexible exchange rate and the government has no intervention in it. The exchange rate is controlled by the market forces.

Figure 3 - Flexible Exchange Rate



In Figure 3, the demand and supply curves are DD_1 and SS_1. The supply of USD rises when US goods are bought by Indians. On the other hand, demand for INR rises when Indian goods are bought by US customers. The intersection of SS_1 and DD_1 in both Figures 3(a) and 3(b) determine the exchange rate ($1 = Rs. 40). Demand for INR rises with the rise in demand for Indian goods. On the other hand, the value of USD increases when demand moves to DD_2, i.e., $1 = Rs. 50 (Figure 3(a)). In Figure 3(b), the exchange rate is $1 = Rs. 40 initially. Due to the rise in demand for goods from the US, the supply curve moves to SS_2. The value of INR declines to $1 = Rs. 30 at point B. This way, when INR increases its value, the value of USD depreciates.

3.2. WHAT ARE THE FACTORS IMPROVING ECONOMIC GROWTH OF INDIA?

The existing economic growth may keep escalating because of deeper and wider financial markets, globalization and fiscal sector reforms (Kelkar, 2004). For example, the effect of those changes may be visible in metrics like transparency in transactions and market capitalization, number of exchanges, and accessibility of economy to FDI. The legal structure of the country has enabled tie-ups in high-tech industries for both international and local markets. Here are some of the causes behind the growth in economy –

3.2.1. RISE IN PRODUCTIVITY

There has been a significant rise in overall "factor productivity" which helped in the growth of GDP since the 1980s. A lot of theories have been made to justify this growth in productivity. According to Rodrik & Subramanian (2004), Keynesian-style growth led by demand, the potential domestic and foreign liberalization, and the Green Revolution are some of the important factors. On the other hand, the regimes of Rajiv Gandhi and Indira Gandhi shifted attitudes. In these regimes, authorities are supposed to have started preferring more moderate changes by the beginning to perceive private businesses and investments more positively. It has brought a welcome change in productivity in industries and knock-on circumstances. The growth of the economy was accelerated as a consequence. Delicensing and deregulation was started in the beginning of 1990s, enabling positive changes. Some researchers have also focused on the effect of changes after 1991 and downplayed policy efforts in the 1980s. In 1993, the reform of the financial sector was started but is yet to be finished. (Jha, 2004).

3.2.2. IMPROVEMENTS IN WORKFORCE

Structural changes in the economy of the country have spurred economic growth in supply of workforce. Around 60.9% of the population of India was aged 15 to 64 years old in 2000. According to the Population Division of the UN, this ratio would exceed the Japanese population in this age range within the next 30 years, and it rose to over 66 percent by 2012. It is all set to cross China in this age bracket. The Nutritional status of India is also improving with a decline in calories and other micro and macro deficiencies of nutrients. In 2001, the literacy rate rose up to 65.38%, from 51.54% in 1991. In the 2001 Census, the literacy rate of women was 54.16% and men was 75.85%.

3.2.3. SAVINGS

From 23.4% in 2000-01, savings were also increased to GDP of 32.4% in the year 2005-06 and investment was also raised up to 33.8% from 24.4% over the same period. The implementation of "Fiscal Reforms and Budget Management Legislation (FRBMA)" was favorable for savings in the public sector in 2003-04. The GDP of India grew at 9% and capital productivity also improved over China. Hence, India should improve investment rates and savings by controlling its financial deficits in order to further improve growth rate and eradicate hunger. India has to raise tax collection and streamline subsidies for economic growth.

4. RESULTS

It is also important to have sustainable growth for India and it should be inclusive in terms of factors like color, caste, gender, areas, etc. Despite having significant growth in closing the gap between political participation and gender wage, a lot of things should be done to ensure women safety. More social protection measures are needed for equitable growth in the country. It is vital to learn from cases like "Amma's canteen" launched in Tamil Nadu to serve healthy meals to poor children to deal with malnutrition issues in India.

There are more than 200 million people in India who are aged 15 to 24 years old. Hence, India is well-versed with a huge population of people in the workforce. On the other hand, balancing the demand and supply of skills and workforce strategically is the need of the hour to make the most of the growing population. Government has made efforts to increase education opportunities but it has to do more to improve the quality of education, examination process, teaching standards, vocational training, and skill development. It is also important to deal with the issue of underprivileged children with right-to-education policies, so that they can learn with privileged children and befriend and respect each other. Social entrepreneurship and public-private partnership should also be improved for the youth of India.

Inflation has also been another serious concern for common public and policymakers over the years. On average, prices have been increased to 10% year on year over the past five years and they may climb up to 13% in upcoming years. The Research Bank of India has increased interest rates to deal with inflation. It is also important to manage the national and international frameworks.

5. CONCLUSION

There has been a significant influence of the government on governance, economic growth, and policymaking over the years. States are investing significantly to promote the local economy and generate models across the nation. There is also a need to make states more proactive to exchange best practices with one another and the central government should work harder to develop cooperation between states. Additionally, the federal government should work harder to even out the rates of growth across the states. Though India is looking forward to promoting the population of its youth, it should also prepare to spend more on social and health programmes for the elderly. The fertility rates are also being affected by the rise of life expectancy, which will increase the population to over 300 million in the age bracket of 60 years by 2050. Even after over 2 decades of economic growth, India has reached the crossroads. Significant modernization and consistent growth of the economy can be possible with reforms. Economy of the country is poised for better expansion in recent years.

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