Liberalization and Unification of World Economics

Liberalization

Liberalization (or liberalization) is any method of how a state raises limitations on some private individual ventures. Liberalization befalls when something which was forbidden is no longer forbidden or when government laws are loosened.

Liberalization in India

Since the adoption of the new economic strategy in 1991, there has been a drastic change in the Indian economy. With the arrival of liberalization, the government has regulated the private sector organizations to conduct business transactions with fewer restrictions.

For developing countries, liberalization has opened economic borders to foreign companies and investments. Earlier, Investors has to encounter difficulties to enter countries with many barriers.

These barriers included tax laws, foreign investment restrictions, accounting regulations, and legal issues. The economic liberalization reduced all these obstacles and waived few restrictions over the control of the economy to the private sector.

Objectives

- To boost competition between domestic businesses
- To promote foreign trade and regulate imports and exports
- Improvement of technology and foreign capital
- To develop a global market of a country
- To reduce the debt burden of a country
- To unlock the economic potential of the country by encouraging the private sector and multinational corporations to invest and expand.
- To encourage the private sector to take an active part in the development process.

- To reduce the role of the public sector in future industrial development.
- To introduce more competition into the economy with the aim of increasing efficiency.

Positive impacts of liberalization in India

1. Free flow of capital: Liberalization has improved flow of capital into the country which makes it inexpensive for the companies to access capital from investors. Lower cost of capital enables to undertake lucrative projects which they may not have been possible with a higher cost of capital pre-liberalization, leading to higher growth rates.

2. Stock Market Performance: Generally, when a country relaxes its laws, taxes, the stock market values also rise. Stock Markets are platforms on which Corporate Securities can be traded in real time.

3. Political Risks Reduced: Liberalization policies in the country lessens political risks to investors. The government can attract more foreign investment through liberalization of economic policies. These are the areas that support and foster a readiness to do business in the country such as a strong legal foundation to settle disputes, fair and enforceable laws.

4. Diversification for Investors: In a liberalized economy, Investors gets benefit by being able to invest a portion of their portfolio into a diversifying asset class.

5. Impact on Agriculture: In the area of agriculture, the cropping patterns has undergone a huge modification, but the impact of liberalization cannot be properly measured. It is observed that there are still all-pervasive government controls and interventions starting from production to distribution for the produce.

Negative impacts of liberalization in India

1. Destabilization of the economy: Tremendous redistribution of economic power and political power leads to Destabilizing effects on the entire Indian economy.

2. Impact of FDI in banking sector: Foreign direct investment allowed in the banking and insurance sectors resulted in decline of government's stake in banks and insurance firms.

3. Threat from Multinationals: Prior to 1991 MNC's did not play much role in the Indian economy. In the pre-reform period, there was domination of public enterprises in the economy. On account of liberalization, competition has increased for the Indian firms. Multinationals are quite big and operate in several countries which has turned out a threat to local Indian Firms.

4. Technological Impact: Rapid increase in technology forces many enterprises and small scale industries in India to either adapt to changes or close their businesses.

5. Mergers and Acquisitions: Acquisitions and mergers are increasing day-by-day. In cases where small companies are being merged by big companies, the employees of the small companies may require exhaustive re-skilling. Re-skilling duration will lead to non-productivity and would cast a burden on the capital of the company.

Effects of Liberalization on Indian Economy

1. GDP growth rate:

India's annual average growth rate from 1990 - 2010 has been 6.6 % which is almost double than pre reforms era. GDP growth rate surpassed 5% mark in early 1980's. This made impact of 1990's reforms on growth unclear. Some believe that 1980's reforms were precursor to LPG reforms. Other things apart, it is clear that 1980 reforms led to crash of economy in 1991, which was remedied by LPG reforms which were quite more comprehensive. It was IMF loan which gave government to adjust its economy. It was largest ever loan given by IMF. Initially there were global doubts on India's credibility for loan, but India has been so far a disciplined borrower.

2. Agricultural Sector:

Agricultural Sector is the mainstay of the rural Indian economy around which socio-economic privileges and deprivations revolve and any change in its structure is likely to have a corresponding impact on the existing pattern of Social equity. The liberalization of India's economy was adopted by India in 1991. Facing a severe economic crisis, India approached the IMF for a loan, and the IMF granted what is called a 'structural adjustment' loan, which is a loan with certain conditions attached which relate to a structural change in the economy. Essentially, the reforms sought to gradually phase out government control of the market (liberalization), privatize public sector organizations (privatization), and reduce export subsidies and import barriers to enable free trade (globalization). Globalization has helped in:

- Raising living standards,
- Alleviating poverty,
- Assuring food security,
- Generating buoyant market for expansion of industry and services, and
- Making substantial contribution to the national economic growth.

3. Industrial Sector:

Effects of Globalization on Indian Industry started when the government opened the country's markets to foreign investments in the early 1990s. Globalization of the Indian Industry took place in its various sectors such as steel, pharmaceutical, petroleum, chemical, textile, cement, retail, and BPO.

Globalization means the dismantling of trade barriers between nations and the integration of the nations' economies through financial flow, trade in goods and services, and corporate investments between nations. Globalization has increased across the world in recent years due to the fast progress that has been made in the field of technology especially in communications and transport. The government of India made changes in its economic policy in 1991 by which it allowed direct foreign investments in the country. The benefits of the effects of globalization in the Indian Industry are that many foreign companies set up industries in India, especially in the pharmaceutical, BPO, petroleum, manufacturing, and chemical sectors and this helped to provide employment to many people in the country. This helped reduce the level of unemployment and poverty in the country. Also the benefit of the Effects of Globalization on Indian Industry are that the foreign companies brought in highly advanced technology with them and this helped to make the Indian Industry more technologically advanced.

The negative Effects of Globalization on Indian Industry are that with the coming of technology the number of labor required decreased and this resulted in many people being removed from their jobs. This happened mainly in the pharmaceutical, chemical, manufacturing, and cement industries.

4. Financial Sector:

Reforms of the financial sector constitute the most important component of India's programme towards economic liberalization. The recent economic liberalization measures have opened the door to foreign competitors to enter into our domestic market. Innovation has become a must for survival. Financial intermediaries have come out of their traditional approach and they are ready to assume more credit risks. As a consequence, many innovations have taken place in the global financial sectors which have its own impact on the domestic sector also. The emergences of various financial institutions and regulatory bodies have transformed the financial services sector from being a conservative industry to a very dynamic one. In this process this sector is facing a number of challenges. In this changed context, the financial services industry in India has to play a very positive and dynamic role in the years to come by offering many innovative products to suit the varied requirements of the millions of prospective investors spread throughout the country. Reforms of the financial sector constitute the most important component of India's programme towards economic liberalization.

Growth in financial services (comprising banking, insurance, real estate and business services), after dipping to 5.6% in 2003-04 bounced back to 8.7% in 2004-05 and 10.9% in 2005-06. The momentum has been maintained with a growth of 11.1% in 2006-07. Because of Globalization, the financial services industry is in a period of transition. Market shifts, competition, and technological developments are ushering in unprecedented changes in the global financial services industry.

5. Export and Import:

India's Export and Import in the year 2001-02 was to the extent of 32,572 and 38,362 million respectively. Many Indian companies have started becoming respectable players in the International scene. Agriculture exports account for about 13 to 18% of total annual of annual export of the country. In 2000-01 Agricultural products valued at more than US $ 6million were exported from the country 23% of which was contributed by the marine products alone. Marine products in recent years have emerged as the single largest contributor to the total agricultural export from the country accounting for over one fifth of the total agricultural exports. Cereals (mostly basmati rice and non-basmati rice), oil seeds, tea and coffee are the other prominent products each of which accounts from nearly 5 to 10% of the country's total agricultural exports.

6. Stock Markets:

Another major development is one of Stock Markets. Stock Markets are platforms on which Corporate Securities can be traded real time. It provides mechanisms for constant price discovery, options for investors to exit from or enter into investment any time. These are back bone of free markets these days and there is robust trade going all over the world on stock exchanges. Their Importance can be estimated from the fact that, behavior of stock markets of a country is strongest indicator of health and future prospects of an economy.

These markets has thrown open wide array of associated services such as Investment Banking, Asset Management, Underwriting services, Hedging advice etc. These collectively employ lakhs of people all over India.

Similarly there are commodities market which provides avenues for investment and sale of various eligible commodities.

7. Telecom Sector:

Conventionally, Telecom sector was a government owned monopoly and consequently service was quite substandard. After reforms, private telecom sector reached pinnacle of success. And Indian telecom companies went global. However, corruption and rent seeking marred growth and outlook of this sector.

Entry of modern Direct to Home services saw improvements in quality of Television services on one hand and loss of livelihood for numerous local cable operators.

8. Education and Health Sector:

It should be noted that food (Agriculture), Health and education (and to lesser extent banking) are among basic necessities, which every human being deserves and can't do without. Unfortunately, in developing countries there is market failure in all these sectors and majority of people can't afford beyond a certain limit (or can't afford at all). Concept of free markets, globalization, liberalization etc. fails here miserably. Free markets provide goods and services to people who can afford paying for them, not to those who deserve and need these.

Now if we consider these sectors from angle of our inclination towards free markets, certainly there has been lot of progress. There has been world class education available in India and Deregulation has resulted in Mushrooming of private engineering and Medical Colleges. But in reality, this had far reaching devastating effect on society.

These new colleges accommodate only a miniscule proportion of aspirants at very high costs. Recently, an Independent organization 'Transparency International' came out with report claiming that India's medical system is most corrupt in the world. This was no surprise, we all know from where it starts. High fees of education forces many aspirants to take educational loans from banks. After qualifying job market is unable to absorb majority of them. Practice turns out to be option of last resort. Now to make a decent living and to pay back the loans person is lured by corruption. Consequently, when many similar cases are put together, we get a corrupt system, economy and society.

Reality is that after deregulation and liberalization, government along with other sectors, pulled its hand from social sectors too. Now there is Mediocre to high quality options are available in private sector which can be availed as per one's budget. In public Sector Less than Mediocre to Mediocre options are available. This leaves huge proportion of aspiring students and expecting patients.

Unification of World economies

- A process whereby countries cooperate with one another to reduce or eliminate barriers to the international flow of products, people or capital.
- Basically there are two approaches to international trade liberalization and economic integration: the international approach and the regional approach.
- The international approach involves international conferences under WTO. The purpose of these international conferences is to reduce barriers to international trade and investment.

- The regional approach involves agreements among a small number of nations whose purpose is to establish free trade among themselves while maintaining barriers to trade with the rest of the world.

Advantages of Economic Integration

1. Trade Creation: Member countries have (a) wider selection of goods and services not previously available; (b) acquire goods and services at a lower cost after trade barriers due to lowered tariffs or removal of tariffs (c) encourage more trade between member countries the balance of money spend from cheaper goods and services, can be used to buy more products and services

2. Greater Consensus: Unlike WTO with hugh membership (147 countries), easier to gain consensus amongst small memberships in regional integration

3. Political Cooperation: A group of nation can have significantly greater political influence than each nation would have individually. This integration is an essential strategy to address the effects of conflicts and political instability that may affect the region. Useful tool to handle the social and economic challenges associated with globalization

4. Employment Opportunities: As economic integration encourage trade liberation and lead to market expansion, more investment into the country and greater diffusion of technology, it create more employment opportunities for people to move from one country to another to find jobs or to earn higher pay. For example, industries requiring mostly unskilled labor tends to shift production to low wage countries within a regional cooperation.

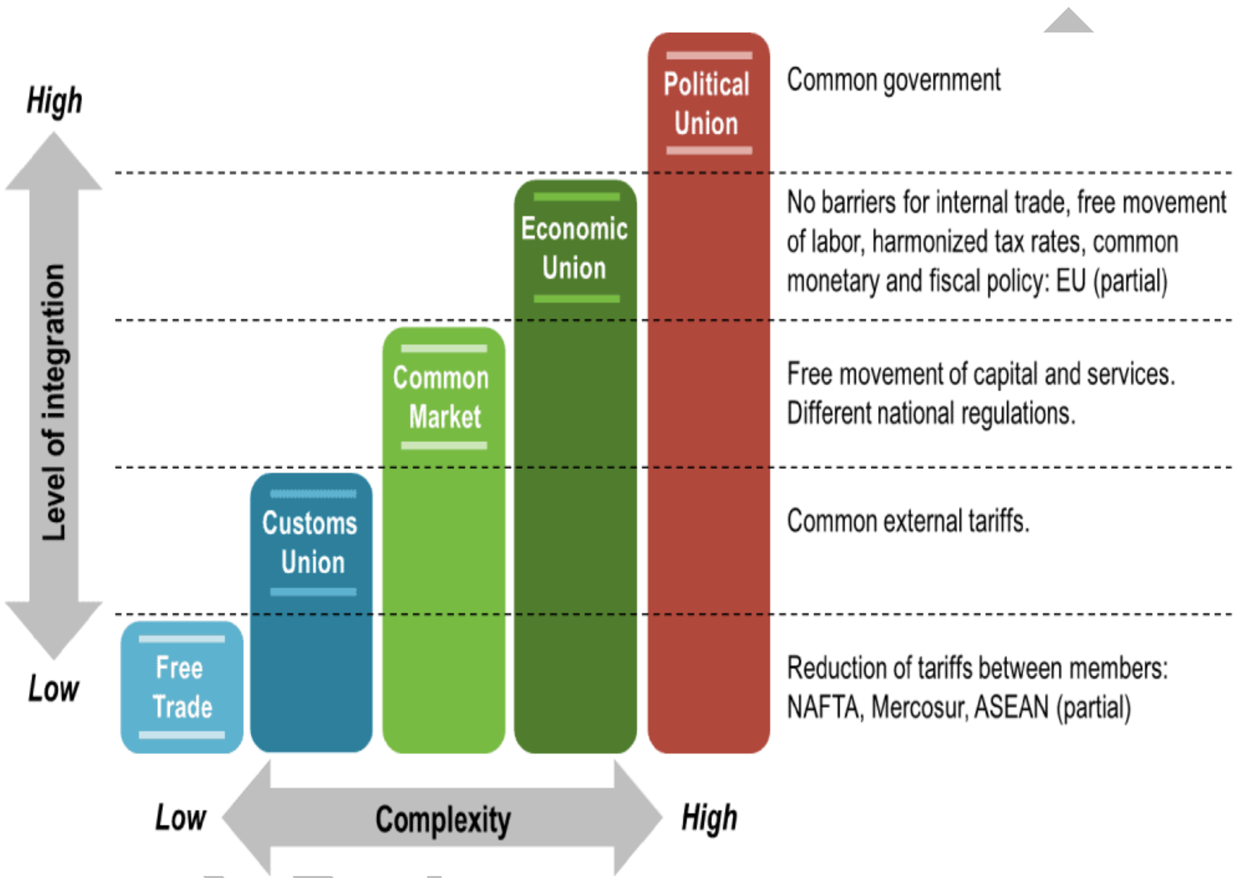
Disadvantages of Economic Integration

1. Creation of Trading Blocs: It can also increase trade barriers against non-member countries.

2. Trade Diversion: Because of trade barriers, trade is diverted from a non-member country to a member country despite the inefficiency in cost. For example, a country has to stop trading with a low cost manufacture in a non-member country and trade with a manufacturer in a member country which has a higher cost.

3. National Sovereignty: Requires member countries to give up some degree of control over key policies like trade, monetary and fiscal policies. The higher the level of integration, the greater the degree of controls that needs to be given up particularly in the case of a political union economic integration which requires nations to give up a high degree of sovereignty.

Levels of Economic Integration



Economic integration can be classified into five additive levels, each present in the global landscape:

- **Free trade**. Tariffs (a tax imposed on imported goods) between member countries are significantly reduced, some abolished altogether. Each member country keeps its own tariffs in regard to third countries. The general goal of free trade agreements is to develop economies of scale and comparative advantages, which promotes economic efficiency.
- **Custom union**. Sets common external tariffs among member countries, implying that the same tariffs are applied to third countries; a common trade regime is achieved. Custom

unions are particularly useful to level the competitive playing field and address the problem of re-exports (using preferential tariffs in one country to enter another country).

- **Common market**. Services and capital are free to move within member countries, expanding scale economies and comparative advantages. However, each national market has its own regulations such as product standards.
- **Economic union (single market)**. All tariffs are removed for trade between member countries, creating a uniform (single) market. There are also free movements of labor, enabling workers in a member country is able to move and work in another member country. Monetary and fiscal policies between member countries are harmonized, which implies a level of political integration. A further step concerns a monetary union where a common currency is used, such as with the European Union (Euro).
- **Political union**. Represents the potentially most advanced form of integration with a common government and were the sovereignty of a member country is significantly reduced. Only found within nation-states, such as federations where there are a central government and regions (provinces, states, etc.) having a level of autonomy.

As the level of economic integration increases, so does the complexity. This involves a set of numerous regulations, enforcement, and arbitration mechanisms. The complexity comes at a cost that may undermine the competitiveness of the areas under economic integration since it allows for less flexibility for national policies. The devolution of economic integration could occur if the complexity and restrictions it creates, including the loss of sovereignty, are no longer judged to be acceptable by its members.