Indian Economy 1950-1990

Indian Economic System

Mixed Economy (with best features of both Socialist and Capitalist Economy) was adopted by the Indian Economy. In this view, India would be a socialist society, with a strong public sector, but also with private property and democracy.

Economic Planning

"Economic planning can be defined as making major economic decisions (what, how and for whom to produce) by the conscious decision of a determinate authority, on the basis of a comprehensive survey of the economy as a whole."
'P. C. Mahalanobis' is known as the Architect of Indian Economic Planning.

- To make economic planning effective, the Government of India set up Planning Commission in 1950, under the chairmanship of the then Prime Minister Pandit Jawaharlal Nehru.
- The purpose of the Commission was to carefully assess the human and physical resources of the country and to prepare the Plans for the effective use of resources.
- The Planning Commission fixed the planning period at five years, which began the era of 'Five Year Plans'.

Goals of Five years Plan

- The five year plans have been concerned with the removal of economic backwardness of the country and to make India a developed economy.
- The five year plans have also taken care to ensure that the weaker sections of the population benefit from the economic progress of the country.
- Each five year plan listed the basic Goals of India's development. These basic Goals are:

(i) Growth
(ii) Modernisation
(iii) Self-reliance
(iv) Equity

Growth

- Growth refers to increase in the country's capacity to produce the output of goods and services within the country.
- Growth implies:
  - Either a larger stock of productive capital;
  - Or a larger size of supporting services like transport and banking;
  - Or an increase in the efficiency of productive capital and services.
- A good indicator of economic growth, in the language of economics, is steady increase in the Gross Domestic Product (GDP).
- GDP refers to market value of all the final goods and services produced in the country during a period of one year. Increase in GDP or availability of goods and services enables people to enjoy a more rich and varied life.
- The GDP of a country is derived from the different sectors (Agricultural sector, Industrial sector and Service sector) of the economy.
- The contribution of each economic sector to the GDP makes up the structural composition of the economy.

Modernisation

Indian planners have always recognised the need for modernisation of society to raise the standard of living of people.
Modernisation includes:

1. **Adoption of New Technology:** Modernisation aims to increase the production of goods and services through use of new technology.

2. **Change in social outlook:** Modernisation also requires change in social outlook, such as gender empowerment or providing equal rights to women. A society will be more civilised and prosperous if it makes use of the talents of women in the workplace.

Self-reliance

- Self-reliance under Indian conditions means overcoming the need of external assistance.
- The policy of self-reliance was considered a necessity because of two reasons:

1. To reduce foreign dependence: As India was recently freed from foreign control, it is necessary to reduce our dependence on foreign countries, especially for food. So, stress should be give to attain self-reliance.

2. To avoid Foreign Interference: It was feared that dependence on imported food supplies, foreign technology and foreign capital may increase foreign interference in the policies of our country.

Equity

The objectives of growth, modernisation and self-reliance, by themselves, may not improve the kind of life, which people are living. So, it is important to ensure that benefits of economic prosperity are availed by all sections (rich as well as poor) of the economy.
• In addition to the objectives of growth, modernisation and self-reliance, equity is also important.
• According to Equity, every Indian should be able to meet his or her basic needs (food, house, education and health care) and inequality in the distribution of wealth should be reduced.

Agriculture

Policies for Growth of Agriculture

1. **Land Reforms**
2. **Land Ceiling**

Land Reforms

Land Reforms primarily refer to change in the ownership of landholdings.
Land reforms is achieved by abolition of intermediaries.

- **Aim behind "Land to the Tiller':** The idea behind this step was that ownership of land would give incentives to the actual tillers to make improvements and to increase output (provided sufficient capital was made available to them). Tenants do not have any incentive to make improvements on land since it is the owner of the land who benefits more from higher output. Ownership of land will enable the tiller to make profit from the increased output.
- The abolition of intermediaries brought 200 lakh tenants into direct contact with the government.
- The ownership rights granted to tenants gave them the incentive to increase output and this contributed to growth in agriculture.
- However, the goal of equity was not fully served by abolition of intermediaries because of following reasons:

  (i) In some areas, the former zamindars continued to own large areas of land by making use of some loopholes in the legislation;
  (ii) In some cases, tenants were evicted and zamindars claimed to be self-cultivators;
  (iii) Even after getting the ownership of land, the poorest of the agricultural labourers did not benefit from land reforms.

Land Ceiling

Land Ceiling refers to fixing the specified limit of land, which could be owned by an individual. Beyond the specified limit, all lands belonging to a particular person would be taken over by the Government and will be allotted to the landless cultivators and small farmers.

- The purpose of land ceiling was to reduce the concentration of land ownership in few hands.
- Land ceiling helped to promote equity in the agricultural sector.
- However, the land ceiling legislation was challenged by the big landlords. They delayed its implementation. This delay time was used by them to get the land registered in the name of close relatives, thereby escaping from the legislation.

New Agricultural Strategy

The new agricultural strategy was adopted in India during the Third Plan, ie, during 1960s. The traditional agricultural practices followed in India were gradually being replaced by modern technology and agricultural practices. The aim of this strategy was to raise agricultural production and productivity in selected regions of the country through the introduction of modern inputs like fertilizers, credit, marketing facilities, etc.

Green Revolution

Green Revolution refers to the large increase in production of food grains due to use of high yielding variety (HYV) or miracle seeds especially for wheat and rice.

HYV Seeds: Main Reason for Agricultural Revolution

Agricultural revolution occurred primarily due to the miracle of new wonder seeds (high yielding varieties (HYV) of seeds), which raised agricultural yield per acre to incredible heights.
• These seeds can be used in those places where there are adequate facilities for drainage and water supply.
• As compared to other ordinary seeds, these seeds need heavy doses of chemical fertilizers (4 to 10 times more fertilizers) to get the largest possible production.

- So, to derive benefit from HYV seeds, Indian farmers need to have:
    - Reliable irrigation facilities; and
    - Financial resources (to purchase fertilizers and pesticides).

Indian Economy experienced the success of Green Revolution in 2 phases:

1. In the first phase (Mid 60s to Mid 70s), the use of HYV seeds was restricted to more affluent states (like Punjab, Andhra Pradesh, Tamil Nadu, etc.). Further, the use of HYV seeds primarily benefited the wheat growing regions only.
2. In the second phase (Mid 70s to Mid 80s), the HYV technology spread to a larger number of states and benefited more variety of crops.

Important Effects of Green Revolution (or Merits of Green Revolution)

1. Attaining Marketable Surplus: Green Revolution resulted in 'Marketable Surplus. Marketable or Marketed surplus refers to that part of agricultural produce which is sold in the market by the farmers after meeting their own consumption requirement.
2. Buffer Stock of Food Grains: The green revolution enabled the government to procure sufficient amount of food grains to build a stock which could be used in times of food shortage.
3. Benefit to low-income groups: As large proportion of food grains was sold by the farmers in the market, their prices declined relative to other items of consumption. The low-income groups, who spend a large percentage of their income on food, benefited from this decline in relative prices.

Risks involved Under Green Revolution (or Demerits of Green Revolution)

(i) Risk of Pest Attack: The HYV crops were more prone to attack by pests. So, there was a risk that small farmers who adopted this technology could lose everything in a pest attack. However, this risk was considerably reduced by the services rendered by research institutes established by the government.
(ii) Risk of Increase in Income Inequalities: There was a risk that costly inputs (HYV seeds, fertilizers, etc.) required under green revolution will increase the disparities between small and big farmers since only the big farmers could afford the required inputs.
However, due to favourable steps taken by the government, these fears did not come true. The government provided loans at a low interest rate to small farmers so that they could also have access to the needed inputs.

Debate over Subsidies to Agriculture

Subsidy is the financial assistance provided by the government to producers to fulfil its social welfare objectives.

Economists in Favour of Subsidies

1. The government should continue with agricultural subsidies as farming in India continues to be a risky business.
2. Majority of the farmers are very poor and they will not be able to afford the required inputs without the subsidies.
3. Eliminating subsidies will increase the income inequality between rich and poor farmers and will violate the ultimate goal of equity.

Economists Against the Subsidies

1. Benefit to fertilizer industries and prosperous farmers: Subsidies do not benefit the poor and small farmers (target group) as benefits of substantial amount of subsidy go to fertilizer industries and prosperous farmers.
2. Fiscal Burden: Economists argue that subsidies are a huge burden on government's finances.

Critical Appraisal of Agricultural Development (1950-1990)

- The 'Land Reform' measures and 'Green Revolution' were the greatest achievements of the Indian Government, in enhancing the agricultural production and productivity.
- Between 1950 and 1990, there had been substantial increase in the agricultural productivity. Agricultural Productivity refers to output per hectare of land. As a result of Green revolution, India became self-sufficient in food production. Land Reforms resulted in abolition of zamindari system.
- The Proportion of GDP between 1950 and 1990 contributed by agriculture declined significantly, but not the population depending on it (67.5% in 1950 to 64.9% by 1990).
- Around 65% of the country's population continued to be employed in agriculture, even till 1990. Agricultural output could have been grown with much less people working in the sector, but industrial and service sectors were unable to absorb the extra workforce involved in agriculture. The involvement of such a large proportion of the population in agriculture was regarded as the important failure of policies followed during 1950-1990.

Industrial Development

The developing countries (like India) can progress only if they have a good industrial sector. Industry provides employment, which is more stable than the employment in agriculture. Industrialisation promotes modernisation and overall prosperity. Due to this reason, Five Year Plans stressed a lot on the industrial development.

At the time of independence, the variety of industries was very limited. The cotton textile and jute industries were mostly developed in India. There were only two well-managed iron and steel firms: one in Jamshedpur and the other in Kolkata. So, there was a strong need to expand the industrial base with a variety of industries.

Role of Public Sector in Industrial Development

At the time of independence, the big question facing the policy makers was to decide the role of government (public sector) and the private sector in industrial development.

There was a need for a leading role of the Public Sector due to the following reasons:

1. Shortage of Capital with Private Sector: Private entrepreneurs did not have the capital to undertake investment in industrial ventures, required for the development of Indian economy. At the time of independence, Tatas and Birlas were the only well known Private entrepreneurs. As a result, Government had to make industrial investment through Public Sector Undertakings (PSU's).

2. Lack of Incentive for Private Sector: The Indian market was not big enough to encourage private industrialists to undertake major projects, even if they had capital to do so. Due to limited size of the market, there was low level of demand for the industrial goods.

3. Objective of Social Welfare: The objective of equity and social welfare of the Government could be achieved only through direct participation of the state in the process of industrialisation.

As a result, state had complete control over those industries, that were vital for the economy. The policies of the private sector had to be complementary to those of the public sector, with public sector leading the way.

Industrial Policy Resolution 1956

Industrial Policy is a comprehensive package of policy measures which covers various issues connected with different industrial enterprises of the country.

• Industrial Policy is essential for devising various procedures, principles, rules and regulations for controlling industrial enterprise of the country.

• After the Industrial Policy, 1948, Indian economy had to face a series of economic and political changes, which necessitated the need for a fresh industrial policy for the country. So, on 30th April, 1956, a second Industrial Policy Resolution was adopted in India, which also formed the basis of Second Five Year Plan. The 1956 Policy emphasised the need to expand the Public Sector.

Classification of Industries

According to Industrial Policy Resolution 1956, the industries were reclassified into three categories, viz., Schedule A, Schedule B and Schedule C.

1. Schedule A: This first category comprised industries which would be exclusively owned by the state. In this schedule, 17 industries were included, like arms and ammunitions; atomic energy; heavy and core industries; aircraft; oil; railways; shipping, etc.

2. Schedule B: In this schedule, 12 industries were placed, which would be progressively state-owned. The state would take the initiative of setting up industries and private sector will supplement efforts of the state. This schedule includes industries like aluminium, other mining industries, machine tools, fertilizers, etc.

3. Schedule C: This schedule consisted of the remaining industries which were to be in the private sector. The state would facilitate and encourage the development of all these industries These industries were controlled by the state through a system of licences", enforced under Industries (Development and Regulation) Act, 1951.

Industrial Licensing

An industrial licence is a written permission from the government, to an industrial unit to manufacture goods. The Industries (Development and Regulation) Act, 1951, empowered the government, to issue licences for:

• Setting up of new industries;
• Expansion of existing ones; and
• Diversification of products.

According to Industrial Licensing

1. No new industry was allowed unless a licence is obtained from the government.
2. It was easier to obtain a licence if the industrial unit was established in an economically backward area. In addition, such units were given certain concessions, such as tax benefits and electricity at a lower tariff. The purpose of this policy was to promote regional equality.
3. Licence was needed even if an existing industry wants to expand output or diversify production. Licence to expand production was given only if the government was convinced that there is a need for larger quantity of goods in the economy.

Small-Scale Industry (SSI)

A 'small-scale industry is defined with reference to the maximum investment allowed on the assets of a unit. This limit has changed from rupees five lakh in 1950 to present limit of rupees one crore.

Important Points about Small-scale Industries

1. Employment Generation: Small-scale industries are more labour intensive, i.e., they use more labour than the large-scale industries and, therefore, they generate more employment.

2. Need for Protection from Big Firms: Small-scale industries cannot compete with the big industrial firms. They can flourish only when they are protected from the large firms. So, various steps were taken by the government for their growth.

- **Reservation of Products:** Government reserved production of a number of products for the small-scale industry. The criterion for reserving the products depended on the ability of these units to manufacture the goods.
- **Various Concessions:** Small-scale industries were also given concessions, such as lower excise duty and bank loans at lower interest rates.

Foreign Trade

Foreign trade in India includes all imports and exports to and from India. India entered into planned development era in 1950's and at that time 'Import Substitution' was a major element of India's Trade and Industrial Policy. In 1950, India's share in the total world trade was 1.78%.

Trade Policy: Import Substitution

In order to be self-reliant in vital sectors, India has followed the strategy of replacing many imports by domestic production.

• Import Substitution refers to a policy of replacement or substitution of imports by domestic production.

• The basic aim of the policy was to protect domestic industries from foreign competition.

• The policy of Import Substitution can serve 2 definite objectives:

(i) Savings of precious foreign exchange; and

(ii) Achieving self-reliance.

Protection from Imports through 'Tariffs' and 'Quotas'

Government made use of two ways to protect goods produced in India from imports:

1. Tariffs: Tariffs refer to taxes levied on imported goods. The basic aim for imposing heavy duty on imported goods was to make them more expensive and discourage their use.

2. Quotas: Quota refers to non-tariff barriers imposed on the quantity of imports and exports. It is fixing the maximum limit on the imports of a commodity by a domestic producer.

The tariff on imported goods and fixation of quotas helped in restricting the level of imports. As a result, the domestic firms could expand without fear of competition from the foreign market.

Reason for Import Substitution

1. The policy of protection (in the form of Import Substitution) is based on the notion that industries of developing countries, like India, are not in a position to compete against the goods produced by more developed economies. With protection, they will be able to compete in the due course of time.
2. Restriction on imports was necessary as there was a risk of drain of foreign exchange reserves on the import of luxury goods.

Arguments against Import Substitution

1. The policy of import substitution encourages production of goods for domestic consumption only and prohibits sale to other countries. It can cause loss of money due to absence of world trade.
2. Some domestically manufactured products can be more costly (due to scarcity of some resources) in the country, while at the same time, they can be imported at a cheaper rate from other countries. Moreover, due to the lack of competition, the inefficiency in the domestic industries might decrease.
3. The economy can be less productive if it tries to manufacture everything domestically.

Critical Appraisal of Industrial Development

1. The proportion of GDP contributed by the industrial sector increased in the period from 11.8% in 1950-51 to 24.6% in 1990-91. The 6% annual growth rate of the industrial sector during the period is also admirable.
2. Indian industry was no longer restricted to cotton textiles and jute. It also included engineering goods and a wide range of consumer goods. The industrial sector became well diversified by 1990, largely due to the public sector.
3. The promotion of small-scale industries gave opportunities to people with small capital to get into business. New investment opportunities helped in generating more employment. It promoted growth with equity.

4. Protection from foreign competition (through Import Substitution) enabled the development of indigenous industries in the areas of electronics and automobile sectors, which otherwise could not have developed. However, this protection had two drawbacks:

(i) Inward Looking Trade Strategy: Our policies were 'inward oriented' and so we failed to develop a strong export sector.

(ii) Lack of Competition: Due to restrictions on imports, some domestic producers made no sincere efforts to improve the quality of their goods and it forced the Indian consumers to purchase, whatever is produced by them. The domestic industry failed to achieve international standards of product quality.

5. Licensing Policy helped the government to monitor and control the industrial production. However, excessive regulation by the government created two difficulties:

(i) Misuse: It was misused by industrial houses. Some big industrialists would get a licence, not for starting a new firm, but to prevent competitors from starting new firms.

(ii) Time Consuming: The cumbersome and complex procedure for obtaining licence was very time consuming. A lot of time was spent by industrialists in trying to obtain a licence.

6. Public sector made a remarkable contribution by creating a strong industrial base, developing infrastructure and promoting development of backward areas.

However, the public sector continued to monopolise (that too ineffectively) in certain non-essential areas, which could be well handled by the private sector.