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Review Article

A STUDY OF POORLY DESIGNED ECONOMIC REFORMS IN INDIA

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Abstract:
The economic growth attempted with a closed environment until the 1990s failed to mitigate poverty and raise per capita income to dignified level resulted in a new model of development whereby the environment was expected to be liberalized. In a way, the economy was given a free hand to work in the right direction. The liberalization of trade and investment was the plank of economic growth in 1991. Since the scope to increase investment and trade which was not tried earlier was realized and indeed it resulted in appreciable growth in GDP which mitigated poverty and increases employment. But as the growth rate indeed was appreciable till 2008-09 but the economy could not withstand the wrath of fault in the globalization which remains attached with it and hence no emerging economy had to pull back from the globalization before reaping the full benefits as India has done in the middle of ascending path. The country is once back to the rule of protectionism because it had not cared about the rules and tenets of globalization. Since the globalization is not one-sided, the other side was also needed to be nurtured well. It was in 1997, the rules for capital account convertibility were written down and over the years these have been ignored. In the most simple words, the dual deficit is not good for the overall health of the economy and hence to get rid of them as fast as possible should be nicety of the economy. But over the years the economy has been given lip services which could not prove good for sustainable growth and hence the results are before us. Since 1991 the data of fiscal deficit and current account deficit is presented to analyze as to what has caused the growth rate to shrink which was never the case. The defect lies in the repeated current account deficit which is coming up every year but artificially contained with the capital inflow and in some critical situation, its impact on the exchange rate was also allowed to fall on it. The net result is that currency is still overvalued when seen from the angle of the Real Effective Exchange rate. Despite the inflation difference across the currencies, Indian currency is allowed to be kept overvalued so that import does not become inflationary too much. Otherwise, the country has succeeded in clearing all exports it wished where it was enjoying competitiveness and uniqueness. The broad exportable goods are presented as under.

Keywords: globalization, employment,study.

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INTRODUCTION:

Most of the goods being exported are cost-competitive and hence could go through easily. The adverse exchange rate in difficult times also has not affected the export of these goods. But as the bias in the exchange rate was realized in times when the support to currency at the time when capital outflow was excessive in the aftermath of the global financial crisis was missing, the inflation and fiscal deficit and current account deficit were higher than in the normal period. For some time the value of import and export both were on the downside because of the fall in the prices of the commodities, the current account deficit was not pinching. But by 2018, the concern was to contain the current account deficit as the benefit of the low-interest rates which was available to all the economies should be available to India also, the capital inflow was expected to be dented and hence in the cool global environment the government does not want to go with disturbing current account deficit and hence the import duties going up was the right proposition. Most of the emerging economies had little firepower to temper the exchange rate with the capital inflow and hence maintained a good balance of current account deficit and hence there is no set back to economic growth which was being boasted in India as it was known to be the fastest-growing economy and at present, it has lost that charm also. Being the large economy in terms of the size and also grown faster was due to the size of the investment which can be seen from the table presented below:

The investment has given the advantage of accumulating the foreign exchange reserve and it was possible when the land has been sold away to the foreign investors and infrastructure of high quality is built to keep investment still increasing. The export volume indicates that indigenous exports are limited to a few items where the cost competitiveness could have been made possible with value addition. It needed a different type of environment whereby the MSME had been given the space to work systematically. As it continued to be overlooked for many years the current account deficit was contained and its impact on the exchange rate was minimized, no difficulty was experienced. But keeping the export faster than the import the country must have created human capital to be realized in the honored capital account and hence when the growth rate had slowed down the capital account convertibility had given the Indian investors to make good their earning from the other countries and at the same time lowering of interest rates when these needed the most were also possible. As the interest rates are craving for reduction it is facing the resistance from the saving community and hence held tightly. China has devalued the currency when it was fighting with the odds of exports falling but most of the time exports were cost-competitive and not to be surprised that Yuan has gained the status of the reserve currency. The outbound investment by China and India are indicated as under;

Since globalization has taken downside, the Chinese economy is not losing its internal strength but India has been dented with ever high unemployment and ever low growth rate. The minuscule outbound investment is possible because the difference in the return for capital account invested elsewhere and remittance could not be large to bail out the current account deficit. However, the Chinese have moved out in large numbers to invest where there was an opportunity to get remittance and of course surplus is also invested safely elsewhere.

REVIEW OF LITERATURE:

MukerjeeNeela (1998): He thinks that trade balance and current accounts balance was due to import extensive and hence reducing the export as much as possible is necessary for orderly growth.

VirmaniArvind (2001): He has cited reasons for the crises of 1990-1991 and underpinned several reasons for the crises such as split of USSR, Iraq-Kuwait war, political uncertainty, etc.

Cerra Valerie &SaxenaSweta (2002): In their study, they have stressed that the current account deficit played a significant role in causing external shocks.

MathurArchana and SachdevaArvinder (2002): They are of the view that a fixed exchange rate is being followed in some countries created a risk of capital inflow and hence threat to BOP continued to remain.

Kruger (2008): She is of the view that India has gone through the economic reface. There were significant leverages on trade policy. Secondly, FDI has also been liberalized due to which investment by foreigners and Indians competed.

Objectives:

The main objective of the paper is:

Shifting the capital account convertibility indefinitely resulted in unemployment and a collapse in GDP.

Hypothesis:

H0: There was no impact on capital convertibility on growth.

H1: There was an impact on capital convertibility on growth.

METHODOLOGY:

The dual deficit has delayed the capital account convertibility as observed from the figures of the fiscal and current account deficit. The objectives and hypotheses are studied and analyzed based on the graphs and tables presented below.

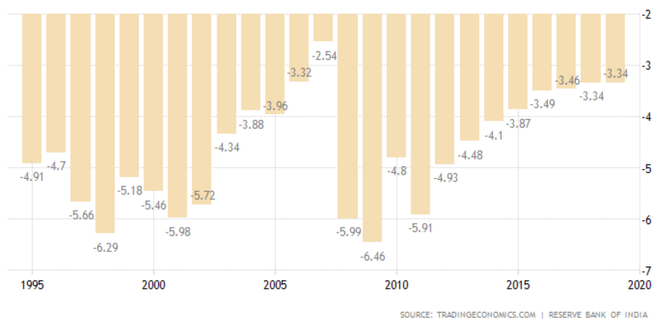
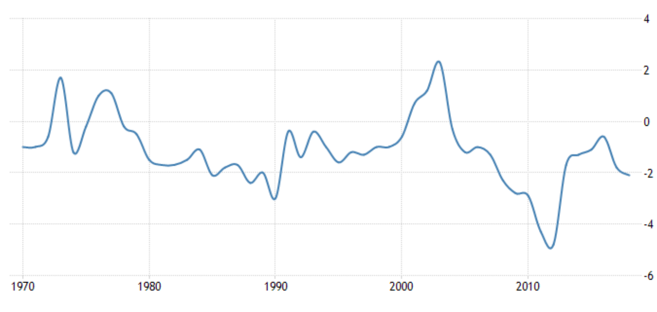


Fig: 01 Government' s fiscal deficit



Fig, 02 India's current account deficit

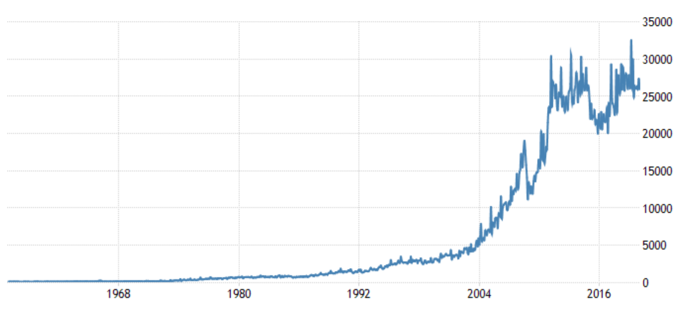


Fig. 03 Exports from India

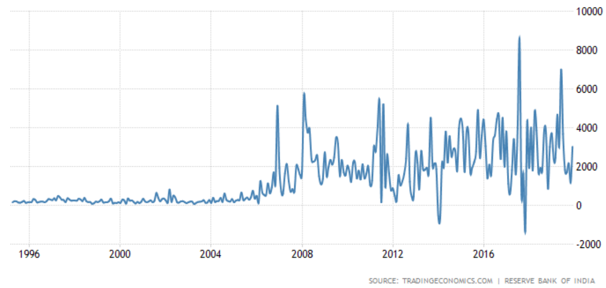


Fig. 04 Foreign Direct Investment in India

Table 01: Chronology of Chinese Investments into Indian Unicorns

Year		**Investor**	**In which unicorn**	**Funding Amount (in $)**	**Further participating Investors**
2014	Jun 01	Tencent, DidiChuxing	Ola	Undisclosed	.
	Feb 05	Alibaba Group	Paytm	213M	SAIF Partners
	Aug 02	Alibaba Group	Snapdeal	500M	Foxconn Electronics, SoftBank Group, Temasek, BlackRock, Myriad Group, Premji Invest
	Sep 29	Alibaba Group	Paytm	472M	.
2015	Nov 18	DidiChuxing	Ola	$500M	Tiger Global Management, DST Global, Baillie Gifford, Steadview Capital, ABG Capital, JSCapital, Falcon Edge Capital, GIC, SoftBank Group, Daniel E Neary
2016	Aug 16	Tencent	Hike	175M	. Foxconn Electronics
	Mar 03	Alibaba Group	Paytm Mall	200M	. SAIF Partners
	May 22	Forum	Delhivery	30M	.
	Jul 25	Tencent	Byju's	40M	CZI, Lightspeed Venture Partners, IFC, Sofina, Brand Capital
	Sep 07	China Lodging Group	OYO Rooms	260M	Hero MotoCorp, SoftBank Vision Fund, Sequoia Capital, Greenoaks, Lightspeed Venture Partners
	Sep 13	China Lodging Group	OYO Rooms	10.2M	
	Oct 11	Tencent	Ola	1.1B	SoftBank Group
2017	Oct 25	Alibaba Group	BigBasket	5M	Helion Venture Partners, Trifecta Capital, Ascent Capital, Bessemer Venture Partners, Brand Capital, Paytm Mall, The Abraaj Group
	Jan29	Alibaba Group	BigBasket	300M	The Abraaj Group, IFC, Sands Capital, Bessemer Venture Partners, Trifecta Capital
	Feb 01	Ant Financial	Zomato	152M	
	Feb 07	Meituan	Swiggy	100M	Naspers
	April 02	Alibaba Group	Paytm Mall	453M	SoftBank Group
	Jun 20	Meituan	Swiggy	210M	DST Global, Naspers, Coatue
2018	Sep 06	Tencent	Dream11	100M	Kalaari Capital, Multiples Equity, Think Investments

	Sep 18	China Eurasia Economic Cooperation Fund	Ola	50.2M	Sailing Capital
	Oct 13	Ant Financial	Zomato	210M	.
	Dec 20	Hillhouse Capital Group, Meituan, Tencent	Swiggy	$1B	Naspers, DST Global, Wellington Management, Meituan, Coatue
	Dec 31	DidiChuxing	OYO Rooms	100M	SoftBank Vision Fund, Grab, Lightspeed India Partners, Sequoia Capital, Greenoaks
2019	Feb 28	Shunwei Capital	Zomato	61.9	Delivery Hero, Naspers, Saturn Shine
	Mar 06	Fosun	Delhivery	413M	SoftBank Vision Fund, The Carlyle Group
	Mar 11	Tencent	Byju's	35.4M	General Atlantic
	Mar 28	Alibaba Group	BigBasket	150M	Mirae Asset, CDC Group
	Aug 30	Hillhouse Capital Group	Udaan	$374	Altimeter Capital, GGV Capital, DST Global, Lightspeed Venture Partners

Source: Traxn (as of September 2019)

Table 02: Real Gross Value added growth of labor-intensive industries (in percent)

Industry code	1990-91 to 1995-96	1996-97 to 1999-2000	2000-01 to 2003-04	1990-91 to 2003-04
1600	3.04	17.56	1.67	7.09
1912	48.08	-1.16	11.23	21.46
1810	27.30	8.52	-5.55	11.42
1544+1549	2.08	0.91	-4.89	-0.42
3693	39.24	11.54	6.75	20.72
2010	-14.67	3.62	6.79	-2.44
2023	4.84	12.17	-1.37	5.18
1730	17.67	21.77	8.78	16.20
3691	87.45	37.76	5.90	47.07
3592	8.20	5.72	6.85	7.02
2692+ 2693	8.18	8.26	2.85	6.56
1541	4.42	6.02	2.43	4.30
2022	-2.48	56.73	40.84	29.07
2811	10.43	-2.55	8.27	5.77
1820	50.17	-15.86	91.51	42.57
3694+ 3699	21.98	34.77	3.28	20.16
2222	19.91	8.44	-3.55	9.16
1920	-0.42	10.25	1.79	3.54
1723	3.85	17.23	-3.33	5.76
1721	18.78	33.42	9.54	20.44
2919+2923+2927+2929	14.84	3.19	-2.01	6.07
2899	15.54	71.78	8.23	30.60
2021	11.65	-5.99	10.82	5.97
2211+2219	6.55	-26.83	-3.94	-6.95
2696	18.53	8.68	17.79	15.27
2102	1.60	15.93	25.40	13.33
1533	18.25	12.13	88.06	37.84
3610	24.42	15.29	8.58	16.73
1712	11.66	36.25	-1.60	15.15
2109	25.72	28.18	-3.65	17.44
2519	9.86	12.06	-2.39	6.77
Weighted Average	10.22	12.88	2.36	8.94

Source:
https://www.researchgate.net/publication/46435408_The_Employment_Potential_of_Labor_Intensive_Industries_in_India%27s_Organized_Manufacturing/figures?lo=1
Industry codes are according to NIC 1998(http://mospi.nic.in/classification/national-industrial-classification/national-industrial-classification-1998).

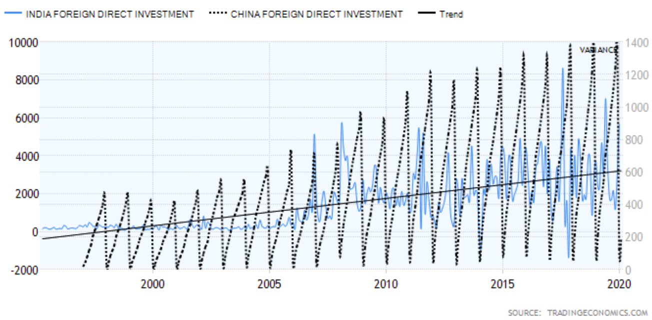


Fig. 05 Comparison of FDI in-between China and India

Source: https://tradingeconomics.com/india/foreign-direct-investment

Table 03 Consumer Price Index (year wise)

Year	CPI(in percent)
1999-2000	3.4
2000-01	3.7
2001-02	4.3
2002-03	4.1
2003-04	3.8
2004-05	3.9
2005-06	4.2
2006-07	6.8
2007-08	6.2
2008-09	9.1
2009-10	13
2010-11	9.5
2011-12	9
2012-13	8

The assumption of capital account convertibility is borrowed from China which dared its currency Yuan to take the place of the reserve currency among the already operating 6 currencies. It is no mean task. There are clear reasons that how capital account convertibility provides lift-off in the matters of foreign investment, keeping inflation under control and also giving monetary and fiscal space to handle the economy sensibly in difficult times. In the great recession of 2008, all the emerging economies had taken shock of the reversal of the capital flow to the haven unless the capital inflow was resumed with the heavy quantitative easing. There is a difference in creating a capital account with the earning from the exports and reducing the incidence of imports as far as possible. But in the case of India, the import has to be contained either with the foreign investment or giving required freedom under current account convertibility. Only essential imports were allowed under the multilateral trade regime rules by WTO. The value-added production in China could keep the inflation under control whereas, in India core inflation and food inflation remained abnormally high when the economic growth was picking up the momentum. The limited value addition in the manufacturing sector indicates that rural poverty was much higher and hence the government was using liberal subsidies or also used the fiscal stimulus to create employment or increase subsidy amount or cutting down the taxes to keep the economy on trend growth. The spurt in inflation most of the time is correlated with the high fiscal deficit. No doubt international prices when these ruled at the peak also created pressure on the inflation. The combined effect of the inflation due to any reason and also the current account deficit was found to be giving severe jolts to the exchange rate and in an extreme situation, the real effective exchange rate was not properly justified. The above graphs provide sufficient reason for explaining that since exports were elastic to exports to some extent but most of the time these were demand-based and hence inelastic to exchange rate. Over the years the hope was always fixed on FDI and FII but no doubt earning was repatriated from the adjustment in foreign exchange reserve with the fresh investment. Secondly, repatriation was not even 6% of the total investment made by the FDI which is a continuous process. The flow of FDI was excellent till 2008 but as the global economy was hit by the global financial crisis and India could not remain unscathed the collapse in demand of the industrial and capital goods is slumping and hence there was no reason that foreign investment had continued to the rising level. As the inflation in the peak growth period was also high as is shown in the graph above the interest rates continued to tread at a higher level and hence the impact on the exchange rate could not be lessened. Therefore looking to the Chinese economy which could afford the low inflation and hence controlling the cost of production with proper fiscal and monetary management has given the fillip to the range and variety of exports and hence the foreign exchange reserve not only as the buffer in extreme conditions but also to be used for outbound investment proved good. While the thought of capital account convertibility which according to the Tarapore Committee was expected to be related to controlling the inflation, CAD and Fiscal Deficit was not considered as important for the particular benefit the economy was managed with the environment available at that time. For example, offshore, derivatives are treated in terms of the rupee. The government securities buying is capped. The NRI and foreign bonds are raised on the interest rate decision based on the rupee. It indicates that since fluctuation in the exchange rate is due to high CAD and fiscal deficit and even though interest rates in domestic conditions are different from the interest rates paid on foreign bonds but the precaution had to be taken that depreciation in the exchange rate due to internal reasons and hence swings could be pricey at times but the interest paid was less pricey and therefore automatic adjustment had to be sacrificed. It is beyond doubt that functioning of the Indian economy was not carried on with the systematic principles and the least was applicable when both sided investment was the case, at the later stage the economy had come to struggle with structural deficiency due to which structural unemployment has increased and also the poverty could not be tackled efficiently. The graph above indicates that in terms of foreign investment also India is way behind China and even now when the foreign investors are vacating their ground in China there was a good opportunity to enjoy the benefit of the companies to come here. The reason is very clear and it is attributed to two facts one the agricultural productivity is far below the normal and very limited benefit of the VGC products could be taken by India. At the end of the peak growth, the Indian rupee is not convertible despite the foreign exchange reserve going high as much as $500 billion. There is one point which has not been absorbed in the analysis, at the time of high-interest rates prevailing in the country, there is one respite to blue-chip companies and these are forced to bear hedging cost while they are resorting to external commercial borrowing. Therefore controlling the interest rates by controlling inflation is of paramount importance. But before it is done the current account deficit must be controlled by increasing export far more than the imports so that fiscal deficit resulting from low-level employment and less paid employment need to be rectified.

CONCLUSION:

In terms of geography and demography, India compares well with China but in terms of treating the financial sector vis-à-vis the real economy, the financial sector remained under stress particularly in difficult times. This has happened because of the tools being adopted to contain the effect of the adverse changes in the economic sector on the financial sector. No doubt the economy has delivered positive results for some time but it had failed bitterly when the global economy had gone through a recession. Therefore one of the lessons that capital account convertibility could not have been postponed too inordinately and real economy could have been dealt better as gradually the stress was reduced on the inflation and fiscal deficit. It is the reluctance on the capital account convertibility which resulted in the imbalances and hence profound impact on the corporate and exporters was obvious.

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