Major Issues in Contemporary Politics (CIA – II Assignment)

Topic : Liberalization in China and in India – A Tale of Two Economies.

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(I) Introduction: "*The economic revolution that Narsimha Rao launched in the middle of 1991 may well be more important than the political revolution that Jawaharlal Nehru initiated in 1947. It is the same in China, where the economic revolution that Deng Xiaoping introduced at the end of 1970s is more important than Mao's revolution of 1949. (Das 2000)*[1]*"* The hidden dragon and the crouching tiger were the sobriquets used to refer to China and India respectively. China, after Mao's revolution, and India, post-independence, had gained the political freedom to act on the global stage. But the economic potential of the two nations was yet to be realized. These two Asian wonders embarked on a journey to gain economic freedom. Freedom from status quo. Freedom from cobwebs of a closed economy. Freedom from economic restrictions. China, the hidden dragon, unlocked its economic potential in 1978. India, the crouching tiger, leaped forward on the account of 1991 economic reforms. Both economies since then have surged forward relentlessly. Chinese economy, in the mean time, is close to secure its position as an economic superpower. Indian economy is rapidly catching up with USA, Japan and China. The seeds of the economic progress were sown in an era of economic reforms. The hidden dragon is visible whereas as the crouching tiger has leapt. This assignment analysis the economic reforms in China (1978) and in India (1991) as well as compares the two scenarios.

(II) The Chinese Great "Economic" Leap Forward

A] Historical Background:

The Chinese Communist Party (CCP) took charge of China in 1949. China was an agrarian society. Ninety percent of its population in the 1950s was engaged in agriculture. A sprawling population has been one of the major attributes of China. Its population was 535 million in 1949 and 840 million in 1970. In 1980 it crossed the one billion mark. Feeding the growing population was a concern. To aggravate the situation consider this: China just has twenty percent of arable land. Rest of China has either mountainous terrain or arid conditions. The plight of the impoverished peasants was miserable. They were constantly exploited by landowners. Thus, the prevailing conditions in Chinese society gave birth to Mao Zedong's Communist revolution of 1949 which was inspired by Marxist theory. Once the communists came to power, they focussed on establishing a sound economic and political structure influenced by socialist objectives. The features of this era:

1) Nationalization of major industries. 2) Abolition of foreign companies.

3) State control of economy. 4) Elimination of private sector.

5) Wholesale land reform. 6) Abolition of "landlord class."

During this time China implemented the First Five Year Plan (1953) inspired by Soviet planning system. China's production of steel, cement and electricity increased considerably.

B] The Great Leap Forward (1958 – 1960):

Mao felt that Chinese revolution would be influenced by the economic drive of five year plans. He feared the high-handedness of bureaucracy which would exploit the common Chinese man. Mao ended the system of five year plans and initiated a phenomenon which he named "The Great Leap Forward." Chinese masses were asked to industrialize and collectivize simultaneously. Agriculture collectives were to be reorganized as communes operating on the Marxist principle – "from each according to his abilities, to each according to his needs. (The Communist Manifesto)[2]"

Rural China was divided into 26,000 communes which were expected to meet specific industrial and agricultural targets. An economic catastrophe followed. "The Great Leap Forward" sent China backwards. The Chinese economy went into a tailspin. Crop failure ensued for three successive years. Hardships of people were aggravated. This was entailed by violence and famine. The Great Leap Forward claimed ten million lives along with crippling the economy.

C] The Great Cultural Revolution (1966 – 1976):

Mao, the great helmsman, had ordered the "Cultural Revolution." "Red Guards" were formed to serve the people. Mao called for cleansing of the bureaucratic system as a means to perpetuate the revolution. Several party leaders found to be inclined towards capitalism were purged. Coercion was sanctioned by Mao as a means to entrench the cultural revolution. The "red guards" rampaged throughout the country causing chaos and mayhem. Property was demolished. Several lives lost – about one million. Violence that erupted was brought under control by People's Liberation Army.

One of the main casualties of the "great cultural revolution" was the economy. The problem of work stoppages came to the fore. Shortages in the production sector and inflation further disrupted the economy. The Great Cultural Revolution retarded China's economic growth for a decade.

D] Politics in between:

It can be inferred that two conflicting strategies existed in Communist China. One was **the radical approach** and the other one was the moderate approach. Radical strategy was adopted during the "The Great Leap Forward" and the "Great Cultural Revolution." Such a strategy relied on propagating the communist ideology to the masses. CCP cadres were fed on a diet of revolutionary zeal. Moreover, a revolutionary, egalitarian society free of exploitation of masses was envisioned. Also known as the "Maoist line" was highly political and emotional.

The other strategy i.e. **the moderate outlook** promoted planning the state economy and stressed on the advancement of China in various fields. The moderate strategy debunked the vitality of ideology and the necessity of revolutionary zeal. Central to the moderate approach was pragmatism i.e. practical decisions; problem solving approach and a rational mindset were encouraged. Bureaucratic management and economic modernization were stressed upon.

Mao Zedong adopted the radical (or Maoist) strategy to run China. The failure of policies pursued by radical strategy ensured political sway in the hands of the moderates. "By 1970s Mao was aged and ill. Leadership passed into the hands of the able Zhou Enlai. Zhou, a moderate and a pragmatic politician, had managed to dodge attacks by the Maoists and now, more than ever, Mao trusted and relied on him. *(McWilliams 2011)*[3]" Mao died in 1976. His wife Jiang Qing along with three co-conspirators (The Gang of Four) conspired to usurp state power. "The Gang of Four" was arrested, expelled and executed.

By 1970s, Deng Xiaoping, a moderate leader had established his control over the Chinese Communist Party (CCP). **It was under Deng's leadership that the Chinese economy was liberalized.** Deng Xiaoping's leadership provided the moderate faction within the CCP to reorganize China's economy as it wished. The era of radical strategy ended. The moderate strategy, in Deng's time, operated through consensus, compromise and persuasion. Deng reformed virtually all aspects of China's social, political and economic life.

E] The Great "*Economic*" Leap Forward:

"Engels never flew on aeroplane; Stalin never wore Dacron. *(The Economist 2008)*[4]" Deng spoke 30 years ago in a meeting aimed to initiate economic reforms in China. He simply meant that the Maoist way of restructuring the economy had rusted and rationality combined with prudence was crucial to structure the Chinese economy post 1978. Economic progress of the Chinese economy, under Deng's leadership, scaled new heights. Liberal and moderate outlook adopted by Deng were the main drivers of these reforms. Deng's big bang reforms package included the following policies:

1) Open Door Policy (1978): Economic development was central to this policy. Damage done by the "Cultural Revolution" had to be corrected. ODP aimed at attracting foreign capital and technology. China normalized its trade relations with USA and Japan.

(i) Technology gap in China was to be plugged by inviting foreign techniques of production as well as upgrading domestic technology to match global levels. Scientists, engineers and industrialists were invited from around the world to fix the gap. Several Chinese students were sent abroad to study technology, computer science and business management.

(ii) Free market enterprise with a socialist spirit was promoted. China was hell-bent on maintaining its commitment to socialism. Incentives for production were introduced.

(iii) Greater foreign inflows were attracted by setting up special economic zones (SEZs), peninsula open zones, open coastal cities and the like in areas bordering Hong-Kong, Macau and Taiwan. In Shanghai foreign investments were promoted by proportionate inducements. The decision of setting up SEZs was a golden one. SEZs attracted businessmen, investors and peasants (all alike) like bees lured by honeycomb. SEZs came to be known as "enclaves of liberalization (Mahtaney 2007)[5]" Success of SEZs in Hong-Kong was phenomenal. It had spillover effects on the mainland in the form of greater investments and establishment of new industries.

2) Housing Responsibility System: Deng put in place an agrarian mechanism that ended agricultural collectivization and abolished communes. Under this system, the peasant could enter in a contract with the state. Under this contract, the state would provide for land, seeds and tools to the peasant. The peasant would till the land and grow crops. Once the crop produce is harvested, the peasant can raise money by selling the produce. The revenue raised would allow the peasant to meet his contractual obligation to the state. After disposing off the contractual obligation whatever remains in the hands of the peasant would be his personal income i.e. all they had earned over and above for what they had contracted for. Market forces decided the price of surplus produce. It is interesting to observe what Deng did. **He created an incentive based mechanism.** The peasants under the new agrarian policy had the incentive to earn personal profits – something which was denied under Mao's regime. Thus, an incentive based agrarian system promoted efficient farming which led to increase in overall agricultural production.

Critics lambasted Deng's responsibility system on the criterion that it missed Marxism by light years. This agrarian system was a classic departure from Mao's ideology of communism. It was more capitalism oriented. But it was the only option to push the Chinese economy forward. One of the Soviet leaders on learning about Deng's reforms commented – "If this is Marxism, I must reread Marx (*McWilliams 2012*)[6]" Deng Xiaoping was a practical man. Chinese economic growth was his

sole intention. **According to Deng, "It doesn't matter what colour the cat is, as long as it catches the mice** *(McWilliams 2012)*[7]**"** Basically, he was of the opinion that it doesn't matter what means are adopted to achieve an end. End being economic growth and means being the political substructure (such as capitalism or communism) that strives to achieve a particular end.

3) Town and Village Enterprises (TVEs): It was aimed at perpetuating rural reform. Peasants were encouraged to invest in village enterprises. The object of liberalization was applied to TVEs completely. Administrative restrictions were eased out. TVEs increased at an average rate of 26 percent per year from 1979 – 1992 thus securing rural welfare. The main aspect which ensured the success of TVEs was fiscal decentralization. It enabled governance at provincial level and ensured that administration was carried out at lower levels. State responsibilities of education, health, housing and local infrastructure were decentralized allowing TVEs to play a greater role at the grass roots leading greater rural welfare and ensuring the success of TVEs themselves.

4) State Owned Enterprises (SOEs): It was decided in 1979 that six SOEs in Sichuan province would be granted autonomy. Later on 100 SOEs were granted autonomy. The autonomy clause allowed these firms the right to produce and to sell products to the market. Furthermore, it permitted the firms to appoint middle level managers without any Governmental interference. Icing on the cake was that these SOEs were permitted to retain a portion of the profits they earned. In 1980, the autonomy clause covered sixty percent SOEs in China. By 1985, the Government had a say over twenty percent of SOEs. Degree of autonomy was further extended by allowing for freedom in decision making. Managers of SOEs could decide on important matters such as technology up gradation and investments. **Larger degree of autonomy led to increasing levels of profits.** Thus, SOEs, working through a contract responsibility system, made greater profits and retained a sizeable share of those profits.

5) Openness: It is an interesting story that though opening up the Chinese economy was the main intention of the reformers, in actuality, the word "opening" was not mentioned in the official report that laid the path of openness. Deng's china came to be recognized with capital investment, self-interest, consumerism, encouragement to strive for personal profit, private enterprise and pursuit of private wealth. Thus, the term "openness" encapsulates within itself not only the lifting up of economic barriers but also the **lifting up of mental barriers**. It was during Deng's regime that China dumped its old rusted mindset and adopted a fresh mindset i.e. a fresh attitude to pursue the economic goals of their nation.

F] Outcome of the Reforms:

"Economic liberalization transformed China from a drab proletarian society, in which individual expression was suppressed, into a lively new consumer society in which individuality was expressed much more freely *(McWilliams 2012)*[8]." Deng's moderate approach made the path that China traversed for over a decade to reach its destination.

In order to gauge whether the 1978 economic reforms had a positive impact it is imperative to consider the magnitude of change in per capita income in China. Per capita income in China in 1990 was fourteen times higher than per capita income in 1978. Apart from this standard of living of people has improved. Deng's "*numero uno"* aim – to boost the economic growth of the Chinese economic – has been achieved.

1) Prior to 1978, the Chinese economy progressed at an average annual growth rate of about 6%. However, post 1978, the Chinese economy paced at an average annual growth rate of 9%. In the post reforms era the growth rate sometimes even climbed to unbelievable 14%. Apart from the growth rate, what is intriguing is that Chinese economy faced several ups and downs prior to 1978 i.e. its economy wasn't quite stable. However, after the reforms, the economy has been more consistent and stable. **It was able to cushion shocks to the system.**

2) In 1987, Deng Xiaoping remarked, "The greatest achievement that was totally unexpected is that rural enterprises have developed.(*Mahtaney 2007*)[9]" **From 1979 to 1983, total rural industrial output doubled.** Rural reform allowed China to reap unmatched benefits in agriculture sector. **Rural collective enterprises** were allowed to keep profits; as a result, efficiency of production was on the rise. Additionally, China was able to put its rural workforce (engaged in agriculture) into industrial work. The transition was so smooth migration of people from rural pockets of China to urban localities didn't spur any urban crisis. Prior 1978, eight ought of ten workers in china were engaged in agriculture. **Post 1978 only one in two did agricultural work.**

3) **Poverty reduction in China** since 1978 has been tremendous. Rural poverty reduced by a mind boggling figure of 89%. 250 million poor in 1978 were reduced to 28 million in 2001. According to World Bank estimates China's rural poor numbers have decreased from 280 million to 124 million. China's poor population accounted for 29% of world's poor. However post economic reforms the figure has come down to 15%.

4) China's open door policy has **enhanced FDI inflows in China.** FDI in China was insignificant prior to 1978. However, in 1994, FDI reached $100 billion – a baffling figure. Greater FDI has led to greater jobs. Thus, the unemployment rates in China have reduced over time. Moreover, greater FDI has ensured that China is interlinked to global markets.

5) Privately held enterprises increased and so did the rate of production efficiency. **Private ownership of production was permitted.** This led to quest for profits which was translated into effective production strategies and increase in employment rates. Reforms inculcated in people the need for property rights. **Thus, property rights gained recognition.**

6) Lastly, one major outcome of 1978 reforms was that it converted China into "factory of the world." Cheap labour, low cost of production, great productivity levels and relaxed state controls (all a result of 1978 economic reforms) assisted China to achieve the **"factory of the world"** sobriquet.

G] Recent developments:

In 2009, China's GDP overtook that of Germany's. Its GDP had crossed $3.4 trillion making China the third largest economy on the planet following US and Japan. Its social and economic indicators have improved too. The 11th Five Year Plan (2006-2010) suggested "building a socialist harmonious society through more balanced wealth distribution and improved education, healthcare and social security.[10]" It is clear that China is poised to assume the mantle of world superpower in years to come. Economic power allows a nation to play significant geopolitical role on the global stage. IMF and World Bank are seen as the leading financial institutions in the world. China has already set out to construct a countercheck to the two.

The Asian Infrastructure Investment Bank (AIIB) has been founded by China. Prominent economies such as UK, Germany, India etc have agreed to be the members of this international financial institution. New Development Bank (NDB), a BRICS initiative, has headquarters in Shanghai. Apart from this, China is leading international forums such as Shanghai Co-operation Organization (SCO).

Though China may be enjoying an envious position in the international arena all's not well with its domestic economy. China's economy in 2015 is facing a slowdown. It is growing at a sluggish rate of 7% which is unlike China. **The Economist paints the picture** – "Structurally, China's economy faces headwinds. In the long run, growth is a function of changes in labour, capital and productivity. When all three increase, as they did in China for many years, growth rates are superlative. But they are all slowing now. China's working-age population peaked in 2012. Investment also looks to have topped out (at 49% of GDP, a level few countries have ever seen). Finally, China's technological gap with rich countries is narrower than in the past, implying that productivity growth will be lower, too.[11]" What the future has in store for China remains to be seen.

(III) The Golden Summer of 1991

A] Historical Background:

India followed **Import Substitution Industrialization policy** up to 1991. The major highlights of this policy included significant restrictions on imports (ensured by high tariffs and import control), limited incentives to private sector, a large public sector (with focus on heavy industries) and an overvalued exchange rate. Furthermore, there were restrictions on consumer goods too. Quantitative restrictions such as import licensing and exchange control existed too. All of these policy measures were part and parcel of what is known as **"barriers to an economy."** The quantitative restrictions prevented the opening up of the Indian economy. Thus, integration of India with the 'global village' was to wait till 1991.

The period from 1976 to 1991 is known as **"ad hoc liberalization."** It is during this period that businesses in India began lobbying for removal of trade restrictions. Quantitative restrictions remained but **trade policy was liberalized partially**. Main features of this era were:

(i) In 1976 an Open General Licenses list was released by the Government. Items placed under this list did not require licenses to be produced or to be traded. The number of items placed in the list gradually increased.

(ii) Anti-labour stance was adopted by the Government during this period. The aroma of capitalism was in the air. Pro-business policies were being formulated though not implemented. It can be said that the Government made a departure from socialist policies.

Politically speaking, in 1978 Janata Party formed the Government. The Janata Pary Government had thought of modifying India's economic policy in order to attract foreign investment and to encourage participation of private sector. However, "ad hoc liberalization" began during Rajiv Gandhi's tenure as the P.M. in 1980s. The Rajiv Gandhi Government introduced **partial economic reforms** to relax restrictions on industrial license and on import export prices.

It should be understood that the 1991 economic reforms were **not wholly** a knee jerk reaction to the economic crisis that shook India in the same year.

The process of liberalization had already begun though at a snail's pace. The crisis of 1991 provided India with an opportunity to do away with the traditional mindset of 'license raj.' It provided an opportunity to sell the big bang reforms to the masses. It provided an opportunity to adopt an industrial policy that broke away from the Hindu growth rate (3.5 % per annum from 1950 -1975) and ensured a much higher sustainable economic growth rate. Lastly, it provided an opportunity to **liberalize, globalize, privatize and modernize India** i.e. to complete India's integration with the global village.

B] Economic Crisis of 1991:

In the late 1980s, fiscal deficit was rising at a rapid rate due to rise in Government expenditures. Fiscal deficit had climbed to the 8% mark. **Inflation was on the rise.** In 1990 credit rating agencies such as Moody's and S&P downgraded India's credit rating. In 1991, inflation had reached 14 %. **On the global stage, Iraq invaded Kuwait.** Consequently, oil prices rose. India faced huge oil import bills. Apart from that, India's exports to Kuwait and Iraq declined. This had a negative impact on India's export earnings as well. External debt to export ratio and external debt to services ratio, both were high. External debt of India had reached $ 72 Billion.

India's foreign exchange reserves dwindled to a dangerous level. India's forex reserves in 1991 rested at a meagre 250 million. To put things in perspective, India's foreign exchange today stands at $ 330 billion. The reserves could hardly buy India oil for two weeks. India had no money to meet essential overseas payments.

Non resident Indians (NRIs) began pulling out money from the Indian economy. **India was facing a liquidity crisis.** To quell the crisis, the Government resorted to high cost finance methods such as External Commercial Borrowings. Government imported FOREX from Union Bank of Switzerland and Bank of England by mortgaging sixty-seven tonnes of gold reserves. "*The financial crisis was long brewing. Its main cause was the profligate and the short term external commercial borrowings (ECBs) the Government resorted to.* (*Das 2000*)[12]"

Astonishingly, by each passing day, the crisis tightened its noose on the Indian economy. State Bank of India till now had a clean record when it came to meeting international financial obligations. However, **SBI was about to default** mostly due to a fertilizer import deal made by the Government. Additionally, the entire international currency market viewed the Indian Rupee to be officially overvalued. **Indian had entered into talks with the International Monetary Fund (IMF) for a prospective bailout package.** It seemed that trade reforms were on the way.

C] Structural Adjustment Programme:

"**Structural Adjustment Programmes (SAPs)**" by nature aim at establishing and entrenching free market economic policies in developing countries. International Monetary Fund (IMF) may advance loans/ bailout amount to debt strapped, broke developing nations on the condition that these countries introduce free market economic policies in their respective regions. This particular arrangement is known as "structural adjustment programme." ***Why structural adjustment?*** SAP's primary objective is to alter or to modify or to change the economic structure of a loan seeking developing economy. The economic structure is altered/ modified/ changed to adjust to the global trade practice. Structural adjustment of the economy is achieved by relaxing Government-set barriers to the economy, by inviting foreign investment in the domestic economy, encouraging

globalization and liberal economic policies and promoting privatization. **SAPs may be imposed by the IMF on poor developing economies. SAPs may even be accepted voluntarily by cash-strapped, debt-ridden economies out of desperation to make ends meet.** The recent Greek bailout package in July (2015) was nothing but a structural adjustment programme. Rather than using the term "structural adjustment" the use of term "(greater) austerity measures" was employed to crack **the Greek conundrum**. Both the term have similar meanings and similar implications.

IMF was hell-bent on making India relax its rigid trade policies. "For the international lending agency, the crucial issue was the Government's borrowings, which it wanted to be cut. It was the key condition for IMF loans to countries facing balance of payment crisis. IMF calculated that elimination of export subsidies could assist India in improving its GDP. IMF also saw the value of Rupee, which had been artificially pegged high, as a disincentive for exports and was of the view that devaluation would boost exports (Financial Chronicle) [13]." SAPs reduce Government deficits through cut in deficits, secure a conducive foreign investment climate and replenish foreign exchange reserves of a country by promoting exports. The Government of India accepted the structural adjustment programme or the so called "financial assistance" provided by IMF to bail its crisis hit economy.

It must be borne in mind that the economic reforms of 1991 were a manifestation of multiple factors. Firstly, IMF did dictate terms vouching for reforms. Secondly, the economic crisis of 1991 made India desperate to seek financial assistance. Lastly, to some extent it can be concluded that the Government made a conscious decision to usher the Indian economy into the modern era. Thus, the restructuring of the Indian economy had begun.

D] How India Tackled the Economic Crisis and Politics in Between:

Rajiv Gandhi was assassinated in May, 1991. Fresh elections were held. Sympathy votes bought Congress back to power. P. Narsimha Rao, coming out of semi-retirement, headed the Government. Narsimha Rao was a learned man. He understood the gravity of the situation as well as the fact that India was bankrupt. His first move was to instate a good finance minister i.e. not a politician but a professional. Rao went for a reticent and soft spoken economist called Manmohan Singh.

The new cabinet took oath on 21st Jun, 1991. The next day the P.M. announced that an economic crisis had hit India. His intention was clear – "to sweep the cobwebs of the past and usher in change. (*Das 2000*)[14]" Action was underway. Finance Minister – Manmohan Singh assured M. Camdessus, the Managing Director of IMF (in 1991) of major reforms in trade and industrial policy. **Early measures included:**

(i) Currency Management: India's overvalued currency's realistic value was reinstated by resorting to **currency devaluation** in two phases. Over a period of three days the currency was devalued by 20% to encourage exports.

(ii) Soon, Manmohan Singh met P. Chidambaram (then Commerce Minister) and Montek Singh Ahluwalia (then commerce secretary) to abolish an export subsidy – **cash compensatory support (CCS).** It was held that elimination of CCS would reduce the fiscal deficit by 0.4%.

(iii) Main aim of Chidambaram was to kill import licensing. Chidambaram decided to substitute import licensing with a marketable incentive called **Exim scrips** which would permit exporters to

earn forex for part of the value of their export. Exim scrips could then be sold in the market or used to import goods. Domestic producers who intend to import raw materials could use exim scrips instead of applying for import license.

Now, Rao sought to dismantle the industrial side of the license Raj. Rao had retained the industry portfolio. On Rao's insistence the New Industrial/ Economic Policy was formulated.

Extract from India Unbound: "Rao thought, "If we are going to open up, why not go the whole hog? Why don't we delicense cars and whole lot of other things as well?" M.Singh concurred "In that case, let us open everything except for a small negative list related to security and the environment." In a matter of minutes, Narsimha Rao and Manmohan Singh seemed to be destroying the License Raj. However there was plenty of dissent within the Congress itself. Arjun Singh said that he found no continuity with past policies. Fotedar thought the policy anti-Nehru and anti-Indira. Shankaranand did not find a mention of cooperatives. The policy was in trouble.[15]"

Regardless of the political opposition, Rao and his ministers succeeded in selling the New industrial Policy (NIP) to their peers in the Congress. The international lender of the last resort i.e. the IMF too was happy with NIP. India had accepted IMF's diktats to secure the conditional loan. Thus, on 24th July, 1991 NIP was adopted by India.

E] New Industrial Policy (NIP), 1991:

NIP marked Indian economy's transition from Nehruvian socialism to free market economic model. Restrictions set by the Government on the Indian economy were lifted. The central idea was that Government should refrain from intervening in the economic sphere and it should encourage private players. NIP had four main aims:

(i) To sustain consistent growth and productivity. (ii) Attaining international competitiveness. (iii) To encourage entrepreneurship. (iv) Use of modern technology in production processes.

Specifics of the NIP are as follows:

1) Licensing Policy – Industrial licensing was abolished. The rationale was that too much licensing affected productivity and the efficiency of firms. Only 18 industries were subject to licensing. included industries dealing with coal, white goods (includes air conditioners, refrigerators) etc.

2) Replacement of "License Permit Quota (LPQ) Raj" with "Liberalization, Privatization and Globalization (LPG) system. **Deregulation of tariffs and custom duties** was undertaken to promote international trade and commerce. Restrictions on imports and exports were lifted. Import and export duties in unnecessary areas were done away with.

3) Foreign Investment – It was recognized that domestic investment should be complemented by foreign investment. Foreign Direct Investment (FDI) upto 51% of foreign equity was allowed in high priority industries (such as metallurgical industries and the like). Collaboration with foreign companies for technical support was encouraged. It was believed that involvement of foreign firms in Indian markets through foreign investments would bring in managerial efficiency and expertise.

4) Public Sector – The public sector was large and inefficient. Public Sector Utilities (PSUs) were facing several problems such as excessive manpower, low productivity etc.

PSUs needed restructuring. Public sector restructuring was carried out in the following manner:

a) De-reservation: According to this, industries reserved for public sector were thrown open to private sector. Earlier 17 industries (such as railways, chemical etc) were reserved for public sector. In 1991, 16 industries were reserved for the public sector. Today, only 2 industries (railways and atomic energy) are reserved for public sector. Rest have been de-reserved.

b) Disinvestment Policy (D.P.): According to this policy, Government decided to withdraw its control in industrial and financial sectors. The Government disinvested its share in public sector to encourage the participation of private sector. By disinvestment policy Government decided to reduce its shareholding in non-strategic public sector while it has decided to retain its majority share up to 51% in strategic public sector enterprises. A "Committee of Disinvestment" (headed by the P.M. of India) was set up to recommend the Government on its disinvestment programmes. Subsequently, Government reduced its share in VSNL, MTNL etc.

Objectives of D.P: (i) To raise resources (ii) Encourage wider public participation.

At macro level, disinvestment can be used to raised resources and fill the gap between public expenditure and public revenue. At the micro level, change in ownership can increase efficiency. Fiscal impact of D.P can be through growth in G.D.P. and tax revenues.

Disinvestment Methods: Includes "strategic sale" i.e. transfer of management control to strategic partner and "public offer" i.e. sale of PSU shares to financial institutions and general public.

c) Board for Industrial and Financial Reconstruction (BIFR) was set up to recognize and revive sick industrial units. Chronically sick units were referred to BIFR for reconstruction and rehabilitation.

d) National Renewal Fund (NRF) was set up to finance Voluntary Retirement Schemes (VRS) for PSU employees i.e. NRF assisted in the implementation of VRS which aimed at offloading excessive manpower. Moreover, NRF was a social security mechanism for the rehabilitation of affected PSU workers.

e) Memorandum of Understanding (MoU) was signed between the PSUs and the operating ministry to increase accountability. Tasks are specified in the MoU and greater autonomy is granted to PSUs to achieve those goals.

4) Monopoly Restrictive and Trade Practices (MRTP) applies to large industrial houses. MRTP was put on paper to prevent unfair trade practices. However MRTP became an annoying tool in the hand of the Government. Government (through MRTP) interfered in decision making process of firms. Mergers and acquisitions by firms became difficult. NIP amended MRTP. Later on MRTP was converted into Competition Commission of India (CCI).

Thus, **the essence of NIP was to promote liberalization, globalization and privatization** in Indian economy. **Liberalization** ensured removal of unnecessary restrictions/ barriers imposed on an economy. Once liberalized, the economy became competitive. **Globalization** ensured free flow of goods and services, capital, personnel and technology across borders. It ensured integration of domestic economy with global economy. Lastly, **privatization** ensures that the Government is no longer a "provider" but a "facilitator." Role of Government in the market reduces and private

players are invited to own or operate public sector thereby improving the efficiency and profitability of the public sector.

F] Outcome of 1991 Reforms:

Expansion of industrial houses became easy with the amendment of MRTP. Large industrial houses were freed from the clutches of the draconian MRTP act. Public sector monopoly was reduced. Banking, airlines, cellular telephones etc was open to the private sector. Abolishment of licenses ensured that raw materials and capital goods could flow freely to and from India.

- Custom duties were reduced from 200% (in 1991) to 40% (in 1995).
- The rupee transformed its nature from being a fixed overvalued exchange rate to an unified market-determining floating rate.
- Inflation came down to 6% from 14% in 1991.
- Fiscal deficit was reduced from 8.4% (in 1991) to 5.7% (in 1993).
- Exchange reserves shot up to $20 billion from $ 250 million (in 1991).
- Market forces determined the interest rates of Government securities.

Most importantly, the 1991 reforms ensured that India's growth trajectory was upward sloping. Since 1991, India enjoyed a steady growth rate of 6.5% per annum. India even managed to stay away from the "Asian flu" (East Asian Financial Crisis of 1997) due to its headstrong economy which was restructured in 1991.

However, the outcomes were not all positive. Gurcharan Das, a prominent economist's words beautifully portray what was yet to be achieved – "The Government had not introduced labour reforms – it is impossible to lay off a single worker even if there is no production. It is impossible to close a private company even if it is bankrupt. Agriculture and insurance sectors were yet to be opened. It had not tackled the vast subsidies that were slowly eating away the financial health of the country. The Government had abolished the License Raj but it had done nothing about the 'Inspector Raj' – or the army of inspectors who make life hell for the Indian entrepreneur.[16]"

G] Recent Developments (Initiatives since 1991):

The 1991 economic reforms had a great impact on the Indian economy. It initiated an era of economic freedom in India. One cannot assess whether this freedom has assisted the growth of India without taking into account the recent happenings in Indian economy.

1) **Navratna Scheme:** Implemented in 1997, this scheme categorizes PSUs on the basis of its performance. High profit-making and well performin PSU can be granted the "navratna" status. Navratna Central Public Sector Enterprises (CPSEs) are granted autonomy in decision making, raising capital and in restructuring their own companies. Eg Bharart Electronics Limited, Hindustan Aeronautics Limited (HAL) etc. Recently, in 2014 there were 17 Navratnas operational.

2) **Miniratna Scheme:** Implemented in 1997, this scheme recognizes those CPSEs as "miniratnas or mini gems" that have secured profits consecutively for three years. Miniratnas are only guaranteed financial, operational and managerial autonomy. Full autonomy is granted when they are no longer credit defaulters of the Government. Eg Airports Authority of India (AAI), Antrix Corporation etc. Currently, in 2014 there were 73 Miniratnas operational.

3) **Maharatna Scheme:** The Maharatna scheme for CPSEs was introduced in 2010. The goal of this scheme is to inspire mega CPSEs into transforming themselves as global giants. Maharatnas are delegated enhanced powers to facilitate their domination in domestic and international markets. One of the criteria of being recognized as Maharatna is to be listed on the Indian stock exchange. In 2014 there were 7 Maharatnas including Coal India Ltd, SAIL etc.

In 2010, total number of CPSEs was 277. Together they contributed to 5.67% of the GDP and employed 1.76 lakh personnel.

4) Earlier in 1991, 17 sectors were reserved for the public sector. **Today only 2 sectors (Railways and Atomic energy) are reserved for the public.** Moreover, debate is going on to allow private players to run railway trains in India. Bibek Debroy, Niti Aayog member, has even proposed proper commercial accounting of railway budget and expenditure to ensure efficiency and transparency. In the atomic energy field, a French Company called Areva is assisting Nuclear Power Corporation of India Ltd (NPCIL) in installing the Jaitapur Nuclear Power Plant (JNPP).

5) **Foreign Direct Investment (FDI):** In sectors such as single brand retail and construction 100% FDI is allowed. In Multi-brand retail 51% FDI is allowed provided 30% domestic servicing clause is followed. 74% FDI in private banks and 20% FDI in public sector banks is permitted. In insurance sector 26% FDI is permitted. FDI in several sectors ensures foreign participation in Indian economy. Foreign companies may bring with themselves much needed funds, technology, and expertise. FDI-spurred-competition may improve the quality of domestic firms.

6) **Disinvestment** has become one of the major tools in the hands of the Government to raise revenue in a particular fiscal year. For instance in the fiscal year of 2014-2015, Government's target was to raise around 58,000 crore through disinvestment much higher than what it was in 2013-2014 (15,900 crore). Recently in January 2015, 10% stakes of Coal India Limited (CIL) were up for public offer. The sale of 10 % stakes fetched the Government about 23,000 crore, highest divestment revenue ever to be collected. To quote Rediff news "The successful divestment in Coal India, where the government would now hold about 80 per cent stake, will help the government close the gap on its target of Rs 43,425 crore (Rs 434.25 billion) for the current fiscal ending March 31, 2014, while helping it shore up finances to meet fiscal deficit challenges.[17]"

In India, there was an economic boom from **2003 to 2008**. Despite the world sinking into the Global Financial Crisis (2008) India stood firm. It enjoyed consistent growth rates of 8% or more during this period. However, in **2012-2013** the Indian economic growth took a backseat. It was reduced to 6%. Manufacturing sector was badly hit. Rupee plunged at new lows. Policy paralysis during the UPA-II regime was one of the factors of this sluggish growth. Corruption increased at unprecedented rates. Graft and red tapism too doubled India's economic woes. Moreover, draconian labour laws scared foreign firms from entering into India. Prices of commodities increased and so did the inflation rates. Economic gloom had descended upon India.

Government change in 2014, it can be said, has once again raised hopes of India to reach the desired economic growth and to fulfil its population's aspirations. The NDA Government has introduced several programmes such as the Make in India and Skill India programmes which might once again spur domestic industrial growth. P.M.'s several foreign tours have succeeded in bringing in much needed foreign capital.

Insurance coverage schemes (Atal Pension Scheme, Pradhan Mantri Jivan Jyoti Bima etc) aim at protecting the future of the downtrodden. The Good and Services Tax (GST) bill if implemented will go very ahead in raising revenues and distributing the same among the states. However, parliament logjam and petty politics must be avoided to realize the same. Thus, it remains to see whether India of 1991 is able to carry on its **"India Story"** in 2015.

IV) Leadership Roles

Economics is crux of world politics today. In today's day and age economic clout (structural power) of a nation is far more superior to its military power (hard power) or cultural power (soft power). But economics by itself cannot redefine a nation. Economics is facilitated by politics. It is politics that ensures establishment of a particular economic way of life in a country. In such a scenario, leadership roles played by a few political leaders in both the countries become crucial. Thus, it is important to give credit to Deng Xiaoping in leading the Chinese Great "Economic" leap forward and to P.V. Narsimha Rao in guiding the 1991 economic reforms in India.

A] Deng Xiaoping :

China, after the 1978 economic revolution, freed 620 million people from the clutches of poverty. The living standards enjoyed by the Chinese improved. During Deng's rule, 22% of world's population resided in China. By improving their life standards Deng catapulted himself into a group of few handful people who have had the fortune to shape and inspire human history. It is well known fact that **Deng was the best political leader the world had seen in the 20th century.**

His political and economic achievements aside, it is imperative to concentrate on his personality which would help us know him better. One of his younger daughters gives a sneak peek into Deng's personality –"In the eyes of his children, Father **is a man of introverted character and few words.** Only with old colleagues and old friends does he like to talk and carries on in a loud voice.[18]" Besides that it is crucial to consider his personal characteristics – "There is a well-known list of his personal characteristics: he played bridge; liked bread, cheese and coffee; smoked; drank and used spittoons. He was unswervingly self-disciplined.[19]" Deng felt that pragmatism was the answer to several problems that his country faced. Deng **was a political wizard, always calm and composed,** similar to some "Zen master." Xiaoping, several times, in his career had been banned or criticised for taking the "capitalist road." But such criticisms didn't affect him. As mentioned earlier, Deng maintained - **"It doesn't matter what colour the cat is, as long as it catches the mice.[20]"**

It is intriguing to learn that Deng became the **"paramount leader"** of China at the age of 74. But the political longevity he enjoyed is unrivalled to this day. It was only during his rule that Chinese had access to consumer goods. A Chinese person could watch a T.V. set or make use of the washing machine due to unbridled efforts of Deng Xiaoping. Deng made China the third largest economy just after U.S. and Japan. To many in China he is a fairy tale character and due to his magical actions, lives of many Chinese people could be described in the traditional line – "and they lived happily ever after."

The following lines best describe the life and times of Deng Xiaoping – "**He was emperor-like** in a century in which the Chinese overthrew their last emperor after three millenniums of imperial rule. Mr. Deng was first among equals in the small circle of revolutionary elders who survived Mao. The

posts and titles Mr. Deng held in the Communist Party hierarchy never quite equalled or conveyed his stature as paramount leader, a term that seemed invented for Mr. Deng, who was still arguably the most powerful citizen of China when he died.[21]"

B] Pamulaparti Venkata Narsimha Rao:

Life has its own twists and turns. Rao's life was no different. During the late 1980s, Rao had begun to quit several of his political responsibilities and was prepared to leave for his native place in Andhra Pradesh. Little did he know that life had other plans. After the assassination of Rajiv Gandhi, Rao was selected as the Prime Minister of India. **No one thought that this accidental prime minister would be the architect of new India.** Often, Manmohan Singh is seen as the face of 1991 reforms. But only few know that the Industries portfolio, which sourced the New Industrial Policy (1991), was with P.V. Narsimha Rao.

Firm and tactful in decision making, Rao left no stone unturned to usher India into a new era. "Fluent in more than 13 languages, well versed with subjects related to economics, law, history, politics & arts, he was rightly called the scholar among politicians. **He was deeply respected among his intellectual circles** and these qualities helped him rise.[22]" Rao understood the nitty-gritties of the negotiations his Government had with international financial institutions. He quickly grasped the situation at hand and made necessary adjustments. He was the one to appoint Manmohan Singh to assume the Finance Minister's role. Manmohan Singh, a quiet and recluse man, enjoyed his job under the leadership of Rao. Rao ensured that Singh was given a free hand to steer the sinking ship of India. If Manmohan Singh was the steward of that Indian ship in 1991 then **P.V. Narsimha Rao was a lighthouse who ensured that this ship was safely manoeuvred to escape choppy seas.**

"The man who led India's transformation was an unlikely pragmatist. **He was 70** and had undergone triple-bypass surgery when he assumed office. A career politician, he had no political constituency of his own. There was hardly a voice that did not lament his elevation to the premiership. And yet if Jawaharlal Nehru "discovered" India, it can reasonably be said that PV Narasimha Rao reinvented it.[23]" He was a flagstaff of a man. It is sad that he remains a forgotten legend. Moreover we fail to realize that he was the only prime minister from a southern state who had a substantive tenure. Its time P.V. Narsimha Rao, the rescuer of Indian economy, is given his due.

V) A Comparison between Indian and Chinese Economies

1900s was referred to as the American century. The 21st century is going to be the century of China and India. It is going to be an era of a dragon's dance and an elephant's march.

1) Ideology: China follows the communist ideology whereas India democracy. The political atmosphere in both the countries is quite different. Historically, China has always been ruled by a single ruler. Existence of a single political authority has been its main feature. Its clean record of monarchy had been disrupted by invasions, but as compared to India, China had to deal with fewer foreign invasions. India on the other hand, has had a melange of kingdoms. Even during the British rule (which had succeeded to establish centralized administration in India) there had been more than 500 princely states. **After 1949, China followed Mao's path. Post 1947, India adopted democracy.**

India (post independence) adopted a multi-party system and China is adapted to one party system. Post 1978, centralized administrative set up in China remained. In India, economic freedom was followed by decentralization of political power. India concentrated on decentralization of power since 1993-94. The 73rd and the 74th constitutional amendment ensured the participation of Panchayati Raj and local municipal institutions in decision making process.

Isn't it baffling that despite the differences in ideology and in political structures, India and China enjoyed similar economic growth rates for three decades from 1950s to mid 1980s. The human development indices for the two countries during this period have been quite similar. Thus, two nations with divergent political set ups and stark ideological differences have had economic outcomes that have been quite identical. After 1978, the economic outcomes also began diverging.

2) Both the countries had an agrarian economy. The **economic agenda** of both the nations had been quite similar in 1950s: to attain self-sufficiency and self reliance in production of basic goods. Heavy industrialization followed. "State controlled industrialization, with an emphasis on production of steel and cement, was the central characteristic of modernization programmes in both the countries. In India it proceeded within a democratic context and in china it was propelled by totalitarian dictate.[24]"

3) The **transitional periods** in both countries differed. In China reforms were underway in 1978, whereas in India reforms came late in 1991. It is crucial to point out the **prevalent conditions** in the two countries, when these reforms were enacted, were quite different. Initial conditions in India were crisis-induced whereas in China, the reform policy was definitely a conscious decision of the state. It can be said that reforms were a compulsion for India and a conscious choice for China. When such is the case, it is easy to decipher that the state which chooses reform is better placed to perform better than the state that is compelled to resort to reforms. The rational is simple – choosing something involves taking heart in that particular thing before pursuing it. A person who loves his job is likely to perform better than a person who is forced to complete his work.

3) **Economic liberalization** in China was confined to special economic zones. In India, liberalization had a profound impact on a plethora of spheres in the framework of service sector such as banking services, financial consultancy, I.T and communication etc. However, liberalization in China was characterized by trade led expansion in manufacturing sector.

4) India followed mixed economy with shades of socialism. China followed communism. Theoretically, it is believed that liberalization as a process is incompatible with communism and socialism because both these ideologies are concerned highly centralized system. However, **liberalization in the two countries changed this perception.** It could be concluded that the utopian political economy where free market enterprise co-exists with state control in certain areas seemed achievable.

It was believed that democratic set up acts as a catalyst for capitalism to execute its effectiveness. But in China, liberalization succeeded in achieving more than it ended up achieving in India. Thus, democracy isn't always the pre-requisite for liberalization to play itself out. India's tryst with liberalization proved that a democratic Government cannot always ensure quick pace of economic reforms. Thus, traditional myths were busted.

5) **China has enjoyed export driven growth. India over time has built a vibrant private sector.** Business houses such as the Tatas, Birlas etc bear testimony to this fact. India has had an edge over China when it came to presence of institutional framework for building up the basics of financial sector. Moreover, India was more likely to modernize at a quick pace than China because it had certain required ingredients of modernism in place. For instance, post independence, India, unlike China, had a vast railway network, a well established bureaucracy and world class textile industry.

6) According to a Boston Consulting Group study (2006), "China has two-thirds state controlled enterprises, some have a mixed ownership structure and only four are privately owned. In India most leading companies have private owners and shareholders and only one company is state owned.[25]" Both China and India are surging ahead at a phenomenal pace. Thus, China's commercial success points out that higher **economic growth is possible even if companies are state owned** whereas the Indian story holds that higher **economic growth is achievable even when private sector has an integral part to play in production.**

7) The ratio between China's per capita GDP (PPP) and India's per capita GDP is 1.6:1. That implies that every dollar that India makes China makes 1.6 dollars. Moreover, India has a greater fraction of people living below the poverty line (poverty line, here is fixed at $1 per day.) than China i.e. In India, the number of people whose cost of living per day is less than $1 is 26% higher than that of China.

8) Lastly, availability of cheap labour and low cost of production has made **China the "factory of the world."** On the other hand, a sound financial sector base and developed I.T. and communication sector has made **India the "office of the world."** Both the economies are marching forward to accomplish their economic goals. The journey of these two Asian economies is yet incomplete.

(VI) Conclusion

The 21st century is the Asian century. **China and India in this century will regain their past**. In the 17th century the Chinese and the Indian civilizations were rich, magnanimous and well-respected. What followed in the years to come was deterioration and despair. All hope was lost. But pragmatists such as Deng Xiaoping and P.V. Narsimha Rao had different plans. They set the course of economic development in their respective countries. They corrected the wrongs of their predecessors and worked tirelessly to regain the lost glory of their respective countries. In 2015, in GDP terms China is ranked second whereas India seventh. In Purchasing Power Parity (PPP) terms China is ranked one and India third. In the historical trajectory of the two countries it was one common factor that is responsible for their enhanced economic status today. That factor being – **liberalization of the economy**. Liberalization has catapulted the two countries to the pinnacle of global economic pecking order. Economic freedom has ensured that China and India are surging relentlessly to register greater growth rates and higher productivity levels. It is best to conclude by quoting Piya Mahtaney "**The India-China story is epoch making**. First, it is the story about two of the world's most populous countries, which have notched up higher growth rates. Second, it embodies for the developing world, the possibilities of consistent economic advancement by counties that found themselves enmeshed in host of constraints and periods of adversity.[26]" To pick up a winner of the two is childish because **the world is large enough to accommodate the two neighbours** together. **What is certain is that India and China will shake the world.**

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