AN ANALYSIS OF THE NEW INDUSTRIAL POLICY OF 1991

Ruchira Baruah,*

Abstract

Industrial Policy is a formal declaration by the Government whereby it outlines its general policies for industries. The primary objective of an industrial policy is to augment the industrial productivity of the nation. India's first industrial policy was formulated in the year 1948. Subsequent to this policy, a number of industrial policies came up in the form of resolutions. Amongst all such policies, the Industrial Policy of 1991 is of extreme importance as it brought about far reaching structural reforms in order to initiate the removal of stringent direct control by the Government on the regulation of industries in India. It aimed at saving India from the major economic crisis that threatened to demolish the Indian economy. The researcher in this project work has aimed at understanding the need for the 1991 industrial policy, thereby highlighting the impact and changes brought about by this policy.

Introduction

The Industrial Policy of 1991 was termed as the "New Industrial Policy". It comes at the centre of all economic reforms in India because it could successfully bring about substantial changes in the economic regulations of the country. A dedicated reform policy for the public sector was launched under this policy.[1]With the onset of gradual liberalisation of regulations in regards to industries, that was brought about by the Industrial Policy of 1956, the industrial development of India gained momentum. However, due to the severe restrictions and control imposed by the Government, it became difficult to maintain the pace of development. As such, India was faced with an economic crisis in the later part of 1980s. For a faster growth of the industries and to lift the economy from such crisis, the government led by Shri Narasimha Rao, which took office in June 1991, announced a "package of liberation measures under its Industrial Policy on July 24, 1991."[2]Through this policy, structural reforms were initiated by the government in the field of trade, industry and the public sector. Private sector investments were made possible in the industrial front through this policy. Foreign investments were also welcomed. One of the significant measures undertaken by this new policy was that industrial licensing was made limited in the country. The thrust of the policy of 1991 was to accelerate the growth process of the Indian Economy and

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* V Semester, 3rd Year, National Law University, Assam

[1] "What are the features of New Industrial Policy of 1991?", http://www.indianeconomy.net/splclassroom/291/what-are-the-features-of-new-industrial-policy-of-1991/

[2] "Major Articles of India's New Industrial Policy 1991", http://www.yourarticlelibrary.com/policies/major-objectives-of-indias-new-industrial-policy-1991/23441/

facilitate the forging of dynamic relationship with foreign investors and suppliers of technology. As result of the reforms brought about by this policy, the Indian economy has been able to achieve significant growth on varied fronts. As such the researcher under this project work has studied the reforms under the New Industrial policy of 1991and analysed its impact on the economy by also focusing on the economy after twenty five years of such reforms.

Aim and Objective

The researcher aims at studying the economic reforms that were brought about through the adoption of the Industrial Policy of 1991. While doing so, the aim of the researcher would be to highlight the important changes brought about by the policy and the impact that it had on the Indian economy.

The objectives of the researcher are:

- To understand the need for industrial policies in an economy
- To understand the evolution of industrial policies in the Indian economy
- To study the New Industrial Policy of 1991
- To analyse the impact of the reforms sought to be achieved through the policy of 1991
- To study its impact 25 years after it was implemented

Scope and Limitations

The scope of this project work has been limited to understanding the Industrial Policy of 1991 and the influence that it had on the Indian economy. The researcher has tried to limit it to understanding the LPG effect of the policy, thereby highlighting its influence after 25 years of its implementation.

Research Questions

While carrying out the project work, the researcher has faced the following research questions:

- What is an industrial policy?
- What were the industrial policies adopted by India?
- How is the Industrial Policy of 1991 significant?
- What were the implications of the policy of 1991 on the Indian Economy?
- Have the targets been achieved that were sought for through this policy?

Research Method Used

IJESLS

The research methodology adopted is a doctrinal method of research. The researcher has also utilised explanatory and analytical methods of research in order to explain and analyse the implications of the Industrial Policy of 1991 on the Indian Economy. Secondary sources of data have been used as the researcher has used books from the library and various articles from journals available in the library as well as online sources.

Mode of Citation Used

The researcher has adopted the OSCOLA mode of citation throughout the article.

Industrial Policy

According to some economists, Industrial Policy is the only method to bring about real economic growth and transformation for a nation. An industrial policy of a nation is the country's strategic effort to encourage the development and growth of part or the entire manufacturing sector of the economy. It is defined as "government efforts to alter industrial structure to promote productivity-based growth."[3]According to economist Dani Rodrik, "Development is fundamentally about the structural changes and involves producing new goods with new technologies and transferring resources from the traditional activities to the new ones."[4]Industrial policies bring about structural change in the economy of a nation in order to foster better and new strategies with a view to achieve a sustainable growth for the industrial sector. It can also be used to promote and motivate a particular sector or specific industry for achieving a focused target. The concept of industrial policy is comprehensive and it covers all those procedures, principles, rules and regulations that control the industries of a nation. The undertakings of a nation in regards to the industries which control and shape the pattern of industrialisation of the nation form the industrial policy of the country.[5]

The main objective of any industrial policy is to augment the industrial production[6]and it is for enhancing the growth of the economy by making optimum use of the resources through the application of various methods. The first and foremost need for an industrial policy is to achieve a balanced industrial development for a country. If implemented effectively, it can facilitate maximum output at minimum cost of production.

Many types of industrial policies contain other policies within them, such as trade policy and fiscal policy. The trade policy of a nation is related to its inflow of international trade and particularly aim at

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[3] "Industrial Policy", http://www.enterprise-development.org/implementing-psd/industrial-policy/#Debates
[4] Ibid
[5] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.206
[6] http://www.gktoday.in/blog/industrial-policy-meaning-need-and-importance/

restricting its import. On the other hand, the fiscal policy of a nation is in relation to the utilisation of the revenue collected by the government so as to influence the economy. There has been an ensuing debate over the merits of industrial policies. The most important debate is in the domain of "how to" formulate the industrial policy of the country. One aspect of the debate is whether governments should use industrial policies to make the most of their country's current comparative advantage, or instead invest in higher-productivity industries that are not competitive in the short term.[7]Some economists also argue that the governments should not favour particular manufacturing sectors while giving importance to manufacturing through the policies. Therefore the debate continues on which type of industrial policies are most effective and productive. Moreover the political aspirations and ideology of governments in power influence the industrial policy of the nation. For developing countries, the industrial policies are aimed at contributing towards poverty reduction thereby focusing on specific industries for the promotion of linkage between larger companies and smaller local enterprises.

Evolution of Industrial Policies in India

Prior to independence, India was not an industrially developed country. Its productivity was primarily focused on the agrarian sector and the modes of production were traditional. The tariff policy pursued by the British in India was based on the principle of one way trade and Indian interest for industrialisation remained neglected. The industrial policies were framed by the British keeping in view the British interests. The British Government had established the Department of Commerce and Industry in the year 1905 but was mostly for favouring the industrial activities of England. Subsequently, the Government also established the Board of Scientific and Industrial Research in the year 1940.[8]In 1938, the Indian National Congress under the leadership of Jawaharlal Nehru set up the National Planning Committee. The committee proposed a series of studies on the subjects concerned with economic development and growth. It laid down that the State should control the key industries and the large-scale industries were to become monopolistic in nature.[9]Apart from this Committee, eight leading industrialists of India prepared and put forward "A Plan of Economic Development" which was popularly known as the Bombay Plan. A Gandhian Plan was also prepared by Shriman Narayan.[10]A "People's Plan" was also formulated by M.N Roy. Therefore, simultaneously a number of plans were prepared for the economic development of India under the British but none were significantly implemented. After gaining independence, for Jawaharlal Nehru, the Prime Minister of Independent India the development

[7] "Industrial Policy", http://www.enterprise-development.org/implementing-psd/industrial-policy/#Debates
[8] "India – Industrial Policy, Liberalisation and Its Impact", http://www.insightsonindia.com/2014/12/09/india-industrial-policy-liberalization-impact/
[9] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.186
[10] Ibid

of heavy industries was synonymous to industrialisation which was a basic condition for attaining rapid economic growth for the nation.[11]As such the first industrial policy of independent India was formulated in 1948.

Industrial Policy of 1948

The policy of 1948 involved both the public and private sectors for industrial development. It contemplated a mixed economy for India. Although the public sector was conceived to be the senior partner in the process of economic development in India, the private sector was to be permitted to exist and supplement the efforts of the public sector within the overall framework of the economy.[12]The industries were to be divided into four categories:

a) Exclusive Government Monopoly[13] - The industries under this category were to be exclusively controlled by the Central Government. Even the State Governments could not interfere here. The manufacture of arms and ammunition, production and control of atomic energy, ownership and management of railway transport[14] were to be included in this category.
b) Government Monopoly for New Units[15]- This category included the coal, iron, steel , aircraft manufacture, ship building, telegraphs and wireless apparatus etc., were to be brought under the State Governments.
c) The third category was of the industries where the Central Government felt necessary to plan and regulate them.[16] It included industries like chemicals, fertilizers, non-ferrous metals etc.
d) Unregulated Private Enterprises[17]- it included industries that were left open for the private investors, individual as well as co-operatives. The provision of mandatory licensing of the private industries was to be kept intact.

The Industrial Policy of 1948 was formulated to achieve economic growth by accelerating the pace of industrial development. For this, both the private and public sectors were to contribute. To implement this policy, the Industries (Development and Regulation) Act, 1951 was passed.

Industrial Policy of 1956

This policy was framed simultaneously with the Second Five-Year Plan of Mahalanobis. Prior to the 1991 Plan, this policy is regarded to be the most important. It projected a clear-cut classification of the industries in India. The industrial sector was divided into three schedules.

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[11] Ibid, p.195

[12] Ibid, p.193

[13] "India – Industrial Policy, Liberalisation and Its Impact", http://www.insightsonindia.com/2014/12/09/india-industrial-policy-liberalization-impact/

[14] Note-9, p.206

[15] Note-13

[16] Note-14

[17] "India – Industrial Policy, Liberalisation and Its Impact", http://www.insightsonindia.com/2014/12/09/india-industrial-policy-liberalization-impact/

a) Schedule A: 17 industries were brought in this category.[18] These were to be the exclusive responsibility of the State. Arms and ammunition, atomic energy, iron, steel, mineral oils etc., were included in this list.

b) Schedule B: A total of 12 industries were to be brought under this category. These were progressively state-owned and the private sectors were to supplement the state efforts.[19] However, new enterprises were to be set up by the state governments.

c) Schedule C: The remaining industries were to be left for the private sector. These industries had to fit into the framework of social and economic policy of the state and were to be subject to control in terms of the legislations in regard to the regulation of industries in India.

The provision for the compulsory licensing of the industries was cemented through this policy. It established the so-called "licence-quota-permit raj" in India. The policy of 1956 laid significance on the establishment of small industries in India. The state was to support the cottage and village industries by restricting the volume of production in the large-scale industries by the provisions of differential taxation or by direct subsidies. Moreover, the basic objective was to strengthen India as a mixed economy. For this, the private sector was to be aided by the state and in cases where there were both public and private units of the same industry; the policy of the state was to give full and non-discriminatory treatment to both. The policy of 1956 was also aimed at removing regional disparity. The upcoming Public Sector Undertakings were to be set up in the comparatively backward economic areas. The Government recognised the need for foreign capital but at the same time insisted upon the progressive Indianisation of foreign concerns.[20] This policy is however, criticised for completely neglecting the agricultural sector of the economy. The focused remained diverted towards the setting up of heavy industries and regulating the private sector. As such, the contribution of the primary sector significantly declined.

Industrial Policy of 1969

As the private sector was allowed to flourish without many restrictions through the Industrial Policy of 1956, the monopoly of the private investors led to unfair and scrupulous means being adopted by the private sector investors. Therefore, the policy of 1969 focused on creating legislations in order to regulate the behaviour of the private investors. With this view, the Monopoly and Restrictive Trade Practices Act 1969 was passed. Through this act, it was intended to regulate the trading capacity and commercial practices of firms checking monopoly and concentration of economic power. The

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[18] Ibid

[19] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.207

[20] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.207

companies/firms with the assets above 25 crores were put under the obligation of taking the permission of the Government before expansion and takeover of other companies/firms. These were known as the MRTP Companies. This Act became effective in June 1970 but as it was found to be incompatible with the new economic policy of 1991, it was repealed in 2009.[21]

Industrial Policy of 1973

The policy of 1973 brought a new classificatory term i.e. 'core industries' with it. These industries were also to be known as basic industries. It included the industries of iron and steel, cement, coal, crude oil, oil refinery and electricity. Originally it had 6 industries as the core industries but now, 8 industries are identified as the core industries. Out of these core industries, the private sector could apply for licences for industries that were not part of Schedule A of the Industrial Policy, 1956. A Reserved List was also created which had certain industrial areas under it that were open only for small and medium industries. For the first time, under this policy, a joint sector was initiated where partnership amongst the centre, state and private investors was allowed while setting up of an industry. The Multinational Companies were also given permission to open their market in India but could not sustain due to the stringent regulations. Companies like Coca-cola and Pepsi entered India during this time but had to return due to rigid regulatory norms. One of the most significant outcomes of this policy was the passing of the Foreign Exchange Regulation Act, 1973. Under this Act strict exchange control was sought to be achieved and it aimed at minimising dealings in foreign exchange and foreign securities. This Act was replaced by the Foreign Exchange Management Act, 1989.

Industrial Policy of 1980

The policy of 1980 was to strengthen the policy of 1956. It endorsed the policy of 1956 and tried to adopt a pragmatic approach. The primary thrust of this policy was to regularise the excess capacity installed over the allowed capacity. The policy was guided by the considerations of growth.[22]It made a sea-change in terms of liberalisation of licensing policy in favour of large-scale businesses. Automatic increase was granted to units wanting to achieve economies of scale and a 49% rise in capacity due to modernisation was allowed.[23]One of the major changes brought about was that the asset requirement under the MRTP Act was raised to Rs.100 crores.[24]The number of industries requiring compulsory licensing was reduced from 56 to 26. The earlier bias against the private sector was greatly moderated,

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[21] "India – Industrial Policy, Liberalisation and Its Impact", http://www.insightsonindia.com/2014/12/09/india-industrial-policy-liberalization-impact/

[22] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.210

[23] Ibid, p.212

[24] Ibid

and it was recognised that Indian industry needed to modernise and upgrade technology. Industrial licences were granted for capacities that were closer to economic scale.[25]

Following these policies, the most important industrial policy was formulated in 1991 as a result of the crisis faced in the later period of 1980s. The government took a series of initiatives in respect of industrial licensing, foreign investment, foreign technology policy and MRTP Act.

Industrial Policy of 1991

By the end of the later part of 1980s, India was faced with a grave economic crisis. This was triggered by the rise in oil prices after the Gulf war. Industries were struggling but the government was unable to provide funds for investment in industrial activities. It fulfilled the long-felt demand of the corporate sector for declaring the abolition of licensing.[26] It also proposed to remove the limit of assets fixed by the MRTP Act and dominate the undertakings. There was an overall relief in the dismantling of industrial licensing and regime of controls.[27]To understand the reforms brought about by the policy of 1991, it is important to understand the background that led to the formulation of this policy.

Background

Economic Crisis of late 1980s

In mid-1991, the exchange rate of India was subjected to severe adjustment. This began with a slide in the value of Indian rupee. In 1990, the value of petroleum imports increased by $2 billion to $5.7 billion as a result of the Middle east crisis and a surge in the oil import volumes. The Gulf crisis resulted in the decline in workers' remittances as well as an additional burden on repatriating and rehabilitation of the NRIs from the affected zones.[28]The export markets were weak in the period leading up to India's crisis as world growth declined steadily from 4.5% in 1988 to 2.5% in 1991.[29]By 1985 India started having a balance of payment problem. The government was nearing to the line of the default and the country's central bank was refusing to give any credit or loan and foreign exchange reserves had been reduced to such a point that India could barely finance itself for even 20 days and the worth of imports which led the Indian government to basically take away the national gold reserves as a pledge to the International Monetary Fund (IMF) to get a loan or credit in order to overcome this balance of payment crisis.[30] The rising of the fiscal deficit and gradually increasing overvaluation has all resulted and contributed to the

[25] Montek Singh Ahluwalia, "The 1991 Reforms – How Home-grown Were They", Economic & Political Weekly, Vol. 51, No. 29 (2016), p.39

[26] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.210

[27] Ibid

[28] Valerie Cera, Sweta Chaman Saxena, "What Caused the 1991 Currency Crisis in India", International Monetary Fund, 2000, p.5

[29] Ibid

[30] "1991 Reforms", https://www.iaspaper.net/1991-crisis-indian-economy-new-industrial-policy-upsc/

rising imbalance in the balance of payment of the country. The balance of payments of a country is a systematic account in the form of summarized record of all the economic transactions between residents of a country and non-residents over a given period. Current account and Capital account form the components of the BOP account. Access to the external commercial credit market was completely denied and the international trade ratings were degrading. India could borrow only against the security of gold reserves by physically exporting the gold. India's BOP also suffered from capital account problems due to a loss of investor confidence.[31]There also existed political uncertainties and outflows began to take place on short term external debt as the creditors became reluctant to roll over maturing loans. When the V.P. Singh government came to power in December 1989, he wanted to differentiate himself from the Congress. During his time as finance minister to Rajiv Gandhi, Singh had acquired a reputation for being a liberal reformer.[32]When V.P. Singh came back to power, there was a renewed focus on industrial reforms. Amar Nath Verma and Rakesh Mohan submitted a set of policy recommendations that were the basis for the New Industrial Policy of 1991. The annual World Economic Forum summit at Davos served as a platform for developing countries eager to attract global attention and capital even then. In January 1990, V.P. Singh was keen to promote a reformist image of India and nominated Ajit Singh to lead the Indian contingent.[33] For Davos, a presentation of what had to be done was prepared, including a pitch for liberalization of FDI. But at the last moment, he was replaced by the Arif Mohammad Khan, the minister for civil aviation and energy. But the preparations had been made and the team in the ministry kept on working on a blueprint for industrial reforms. However, V.P.Singh's government fell as it was caught in caste and religious disputes. A number of political forces—from Devi Lal's farmer agitation, to BJP's Rath Yatra as a counter to the Mandal Commission, and Chandra Shekhar's rebellion (ostensibly) over the industrial policy—combined to bring down the V.P. Singh government. A caretaker government was formed until next elections. The new Congress government was formed under P.V. Narasimha Rao who retained the industry portfolio.[34] Within a few days of his appointment as finance minister, Manmohan Singh called a meeting of all the major secretaries and the chief economic adviser and he knew that a framework on industrial reforms had already been prepared. Under A.N. Verma, a steering committee for economic reforms was created. It was decided that the industrial policy would be presented along with the budget on 24 July 1991.[35] The new industrial policy almost did not happen. It was rejected by the Cabinet when it

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[31] Ibid, p.6
[32] "India's Industrial Reforms of 1991 – The Inside Story", http://www.livemint.com/Sundayapp/GEflSNMjdRctaEbPAzxg9M/Indias-industrial-reforms-of-1991-The-inside-story.html
[33] Ibid
[34] Ibid
[35] Ibid

was first taken up on July 19. Many ministers objected to the sweeping changes being proposed, saying that it was a wholesale and unwarranted condemnation of over four decades of planned development.[36] It is only after consultations in a Group of Ministers, and some political repackaging and repositioning, that the Cabinet had approved the proposals on 23rd July.

M Document of 1990

In June 1990, Montek Singh Ahluwalia, the special secretary to the PM prepared a note on "Restructuring India's Industrial and Trade Policies."It was published by Finacial Express and was popularly named as the "M Document". The M Document argued that the process of

Liberalisation that had been underway needed to be taken further.[37] It also pointed out a weakness in India's approach, arising from the fact that the government's liberalisation initiatives consisted of ad hoc steps in a particular direction. The note explicitly excluded two important sectors—agriculture and infrastructure—which needed to be considered separately.[38] The M Document emphasised the need to bring the fiscal deficit under control over a three-year period.[39] The measures suggested were conventional measures to restrain defence expenditure, subsidies, etc. The note said the economy had become too complex to continue with the system of licensing control as it had operated in the past. The M Document recommended steps to increase the scope of delicensing.[40] The M Document also proposed that the prevailing restrictive approach to FDI needed to be liberalised.[41] It suggested a positive list of industries where foreign investment up to 40% should be welcomed and there should be another high priority list where investment up to 51% would be allowed. It also proposed a proactive approach towards good quality foreign investors by encouraging some of the large public sector organisations and private corporations to seek out foreign investors as partners.[42] The M document recognised that there may be hesitation in embarking on import liberalisation for fear of the consequences for the balance of payments. It, therefore, suggested a transitional mechanism of keeping import licensing in place, but linking import liberalisation to tradable replenishment licences given to exporters.

Manmohan Singh's Address at the Convocation of IIM Bangalore

[36] "Manmohan Singh's 1991 Budget – Twenty Five Years Ago On This Day", http://www.thehindu.com/opinion/lead/manmohan-singhs-1991-budget-twenty-five-years-ago-this-day/article8891562.ece

[37] Montek Singh Ahluwalia, "The 1991 Reforms – How Home-grown Were They", Economic & Political Weekly, Vol. 51, No. 29 (2016), p.42

[38] Ibid

[39] Ibid

[40] Ibid, p.43

[41] Ibid,p.44

[42] Ibid

In April 1991, Manmohan Singh delivered the convocation address at the IIM Bangalore. He knew at the time that the country was facing a crisis, and his remarks were, therefore, made in the context of a crisis. The address called for action on both the fiscal deficit and on structural reforms. On the fiscal deficit, the address was conventional, focusing on the need to contain current expenditure and reduce subsidies.[43] The address also dealt with tax reforms to generate the revenue needed for rural infrastructure.

Reforms under the Policy of 1991

The reforms that were introduced through this policy were structural in nature. It made India a totally open economic system as compared to the earlier mixed system. As per the statement published by the Government, the objectives of the policy were:

- to maintain a sustained growth in productivity;
- to enhance gainful employment;
- to achieve optimal utilisation of human resources;
- to attain international competitiveness and
- to transform India into a major partner and player in the global arena.[44]

The primary features that introduced the reforms were as follows:

- Industrial Licensing was abolished – The compulsory licensing provision for the industries was removed except for a short number of industries. These excluded industries were related to the security and strategic reasons, hazardous chemicals etc. The projects where the imported capital goods were required, automatic clearance would be given in cases where the foreign exchange availability is ensured through foreign equity.[45]In locations other than cities having a population of more than 1 million populations, there was no requirement for approval of the Government except for industries subject to compulsory licensing.[46] A total of 18 industries only were to be under the control of the Government and required compulsory licensing. However, of these 18 industries, 13 categories have been removed from the list gradually and currently only 5 category of health, strategic and security considerations industries needs license viz. alcohol, cigarettes, hazardous chemicals, electronic, aerospace and all types of defence equipment.

[43] Montek Singh Ahluwalia, "The 1991 Reforms – How Home-grown Were They", Economic & Political Weekly, Vol. 51, No. 29 (2016), p. 44

[44] "Industrial Policy Statement", Ministry of Commerce

[45] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.212

[46] Ibid

- Foreign Investments - The rules regarding foreign investment were liberalised in several ways. In order to invite investments in high priority industries, requiring larger volumes of investments, the policy provided for direct approval of the foreign investments. The direct foreign investment was allowed up to 51%[47], thereby opening Indian markets to foreign investors. The Reserve Bank of India was to monitor the payment of dividends so as to ensure that outflow on accounts of dividend payment are balanced by export earnings over a period of time.[48]Foreign investments take two forms – Foreign Direct Investment (FDI) and Foreign Portfolio Investment (FPI). The FDI helps to increase the productive capacity of the economy. FPI is more speculative in nature. During the period of 1990-1991 and 1994-1995 the share of FDI in total investment flow was only 24.2% and that of FPI was 75.8%.[49] FDI had a gradual upward growth from $129 million in 1991-92 to $1,314 million in 1994-95.[50]With the inflow of foreign investments, the requirement for foreign technologies also increased. As such, there were liberal allowances for the use of foreign technologies. Government was to allow direct approval for the use of foreign technologies within the specified parameters in high-priority industries.[51]
- Restriction of the MRTP Act – The growing complexities of the industrial sector and the opening up of the market for foreign investors alongwith the private players, the need for loosening of the restrictions imposed by the MRTP Act was called for. Accordingly vide this new policy, certain changes were brought about –
    - The MRTP Act required the MRTP Companies to take pre-entry scrutiny of investments. This was no-longer required. Focus would now be on the controlling and regulating the monopolistic trade practices and not on company functioning and takeovers.
    - The interference of the Government was to be restricted and the thrust was to be on controlling the unfair means of business practices.
- Public Sector Policy – Public enterprises should minimal returns on the capital invested. Many of the public sectors had become burdens for the Government. The government while keeping at least 51% of equity, directed such undertakings to privatise their remaining equity and go for fresh funds from the public. The budgetary support to the public undertakings was to be

[47] Ibid, p.213
[48] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.213
[49] Ibid, p.280
[50] Ibid
[51] Ibid, p.213

reduced thereby forcing these undertakings to improve their performances.[52]The government would provide aid only to those sectors that were in the reserved areas of operation. There were a large number of industries in the public sector that were incurring heavy losses, operating in a competitive market, yet serving no public purpose. As such certain steps were to be taken up by the government.

- Portfolio of the public sector investments were to be reviewed with a view to focus on the strategic, high-tech and essential infrastructure.[53]
- Public sector enterprises that were chronically sick and which were unlikely to be turned around would be referred to the Board for Industrial and Financial Resolution (BIFR).[54]This was an institution created for the purpose, in order to protect the interests of workers likely to be affected by such rehabilitation package.[55]A social security mechanism was to be created through such institutions.
- Board of public sector enterprises were to be made more powerful and professional.
- There would be a greater thrust on the performance improvement of the enterprises and the managements would be granted greater autonomy throught the Memorandum of Understandings.[56]

➢ Fiscal Policy – The Chelliah Committee set up in June 1991 recommended simplification of the taxation system. Accordingly, the government reduced the maximum marginal personal income tax from 56% in 1991 to 40% in 1994. The Corporate Tax was brought down to 46% in 1994 from 57.5%.[57]New private sector banks were licensed so as to make the public sector banks more effective. The government deregulated the interest rates and reduced the mandatory reserve requirements.

➢ Privatisation and disinvestment – Privatisation is a way of altering the relationship between the public and private sector. Through the policy of 1991, the industrial sector was opened up to the private sector. Government announced its intention to offer a part of government shareholding in the public sector enterprises to mutual funds, financial institutions, the general public and the workers. A beginning in this direction was made in 1991-92 themselves by

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[52] V.R. Rajan, "GLOBALISING INDIAN INDUSTRIES: STRATEGIES AND MANAGEMENT", Deep & Deep Publication, 1998, p. 8
[53] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.214
[54] Ibid
[55]"India: Industrial Policy Liberalisation Impact", www.insightsonindia.com/2014/12/09/india-industrial-policy-liberalization-impact/
[56] Note-53
[57] V.R. Rajan, "GLOBALISING INDIAN INDUSTRIES: STRATEGIES AND MANAGEMENT", Deep & Deep Publication, 1998, p. 8

diverting part of the equities of selected public sector enterprises. The government would divest parts of its holdings in selected enterprises but did not place any restrictions on the extent of disinvestment.

- Convertability of Rupee – The exchange rate of rupee was devalued by 24% in June 1991 and the export subsidies were simultaneously withdrawn. There was a brief experiment with the exchange rate system in 1992 but in March 1993 the exchange rate was unified and effective floated to be a market determined rate. This total convertibility of the currency on trade account[58] was a major step undertaken through this policy.

Evaluation of the Policy

The 1991 reforms were generally well received by the press as signalling a resolve to deal firmly and innovatively with the crisis. Numerous cases of bottleneck restrictions created by the bureaucracy were struck down by the policy. It ended the license-permit raj[59]and relieved various business practices. The lifting of restrictions from the MRTP companies enabled the establishment of new industries and effective expansion of the industrial sector. The new industrial policy electrified the atmosphere leading up to the presentation of the Budget.[60]Manmohan Singh delivered a hugely moving speech. Its contents, of course, marked a huge paradigm shift in economic thinking and charted out a course that has remained steady for a quarter of a century — a course that has been embraced by all political parties when they have been in power. Devaluation of the rupee had taken place on July 1 and 3. Almost 47 tonnes of gold had been transported to the Bank of England between July 4 and 18 enabling the country to borrow about $400 million at a time when the country's foreign exchange reserves had dwindled to a measly $900 million.[61] It also articulated a new fiscal policy and led to scrutiny of the system under two committees – one on the financial sector reform, headed by P.V. Narasimha and another to prepare a road map for reducing import duties, led by Raja Chelliah.

There were certain reservations regarding the effectiveness of the policy. The left were profoundly suspicious of the scaling down of the role of the public sector, the weakening of control over large houses, greater reliance upon market forces, and especially external liberalisation.[62]Critics have argued

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[58] V.R. Rajan, "GLOBALISING INDIAN INDUSTRIES: STRATEGIES AND MANAGEMENT", Deep & Deep Publication, 1998, p. 10

[59] Gaurav Datt and Ashwani Mahajan, DATT & SUNDHARAM'S INDIAN ECONOMY, 71st edition, S. Chand & Company Pvt. Ltd., 2015, p.215

[60] The Hindu, "Manmohan Singh's 1991 Budget – Twenty Five Years Ago On This Day", http://www.thehindu.com/opinion/lead/manmohan-singhs-1991-budget-twenty-five-years-ago-this-day/article8891562.ece

[61] Ibid

[62] Montek Singh Ahluwalia, "The 1991 Reforms – How Home-grown Were They", Economic & Political Weekly, Vol. 51, No. 29 (2016), p. 45

that the over-enthusiasm of welcoming the foreign capital might sell the sovereignty of the country to multi-nationals. They have also questioned the government for assuring majority foreign equity holding up to 51% even for trading companies engaged in exports because they can effectively explore the foreign markets without foreign participation. The policy also lagged in the social security policy. The government would only refer the rehabilitation cases to the BIFR, which created fear in the minds of the workers. They feared that the government was not sincere in protecting their interests. A group of industrialists, described by the press as the Bombay Club, argued that Indian industry needed time before they could make themselves ready to face competition.[63]The policy however, worked towards controlling inflation. The first four years of the 1990s registered double-digit inflation based on the wholesale price index, (WPI) with a 13.6 percent peak reached in 1992-93.[64] The developments in the economy since 1996 have been conducive to a decline in the inflation rate. Importantly, on the demand side, there has been a noteworthy change in the source of reserve money creation.[65]

A major criticism of the economic reforms of 1991 is the complete neglect of the agricultural sector. Agricultural sector has stagnated around 2%. It is estimated to be only 2.3% during 2002-2007. The lack of development is contributed to the withdrawing of the public sector investment and hoping that the private sector investment would expand irrigation, did not materialise.

After 25 Years of the Policy

2016 marks the 25th year of bringing about such landmark reforms in the economy of India. The industrialists feared initially that India would not receive adequate time before competing in the world market. But after 25 years of the opening up of markets it is seen that Indian industry did get a lot of time. Large parts of the industrial sector, such as the entire consumer
goods range, were not opened to imports until 2002, 11 years after the reforms began. FDI also did not flow in very quickly, although many foreign companies began to express interest.[66] The post-reforms performance certainly belied the fears of those who had warned of a negative impact on growth, but it is also true that the growth rate in the first 10 years or so after the reforms was not markedly higher than the growth rate in the 1980s.[67]

The post-reform period has been characterised by a "globalisation paradigm", which subsumes the liberalisation of markets (both product and factor) and is expected to lead to a

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[63] Ibid

[64] Nirupam Bajpai, "A Decade of Economic Reforms in India – The Unfinished Agenda" Economic & Political Weekly, Vol. 20, No. 4 (1998), p. 50

[65] Ibid

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[67] Montek Singh Ahluwalia, "The 1991 Reforms – How Home-grown Were They", Economic & Political Weekly, Vol. 51, No. 29 (2016), p. 45

diminution, if not withering away, of industrial conflict for various reasons.[68] Evidence also shows that innovative activities in the industrial sector have shown some significant increases during the post-reform process. Hi-tech industries now contribute over 5% of India's GDP. The innovative activity is, of course, restricted to a few hi-tech industries.[69] This rise in innovative activity is largely contributed by the domestic private sector if one takes into account all the indicators. Within the domestic private sector innovative performance is largely confined to the pharmaceutical industry.[70]Nevertheless, these reforms marked the beginning of a different economic era. It could successfully attract foreign investments and gave a boost to the domestic investments, thereby uplifting India from a grave economic crisis.

Conclusion

At the time of independence, India had an extremely underdeveloped and unbalanced industrial structure. Industries contributed less than one sixth part of national income. Thus after independence, the government had to undertake effective measures to increase industrial development. Therefore, a number of industrial policies came up which tried to project India as a mixed economy. However, the strict government regulations and interference made it difficult for the industries to sustain. Therefore, the Indian economy had to face a major economic crisis in the later parts of 1980s. The political scenario and the world events also triggered the crisis period. As such the P.V. Narasimha Rao government, under Manmohan Singh as the finance minister, brought about reforms that made sea-changes in the Indian economy. The policy of 1991 unshackled many hindrances to the growth of the economy by allowing privatisation and liberalisation. The business circles welcomed the changes. However innocuous those reforms might seem today, they were revolutionary in 1991.

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[68] K R Shyam Sundar, "Industrial Conflict in India in the Post-Reform Period Who Said All Is Quiet on the Industrial Front?"Economic & Political Weekly, January, (2015) Vol l No 3, p.43

[69] Sunil Mani, "Is India Becoming More Innovative since 1991? Some Disquieting Features", Economic & Political Weekly, November (2009) Vol XLIV No 46, p.41

[70] Ibid

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