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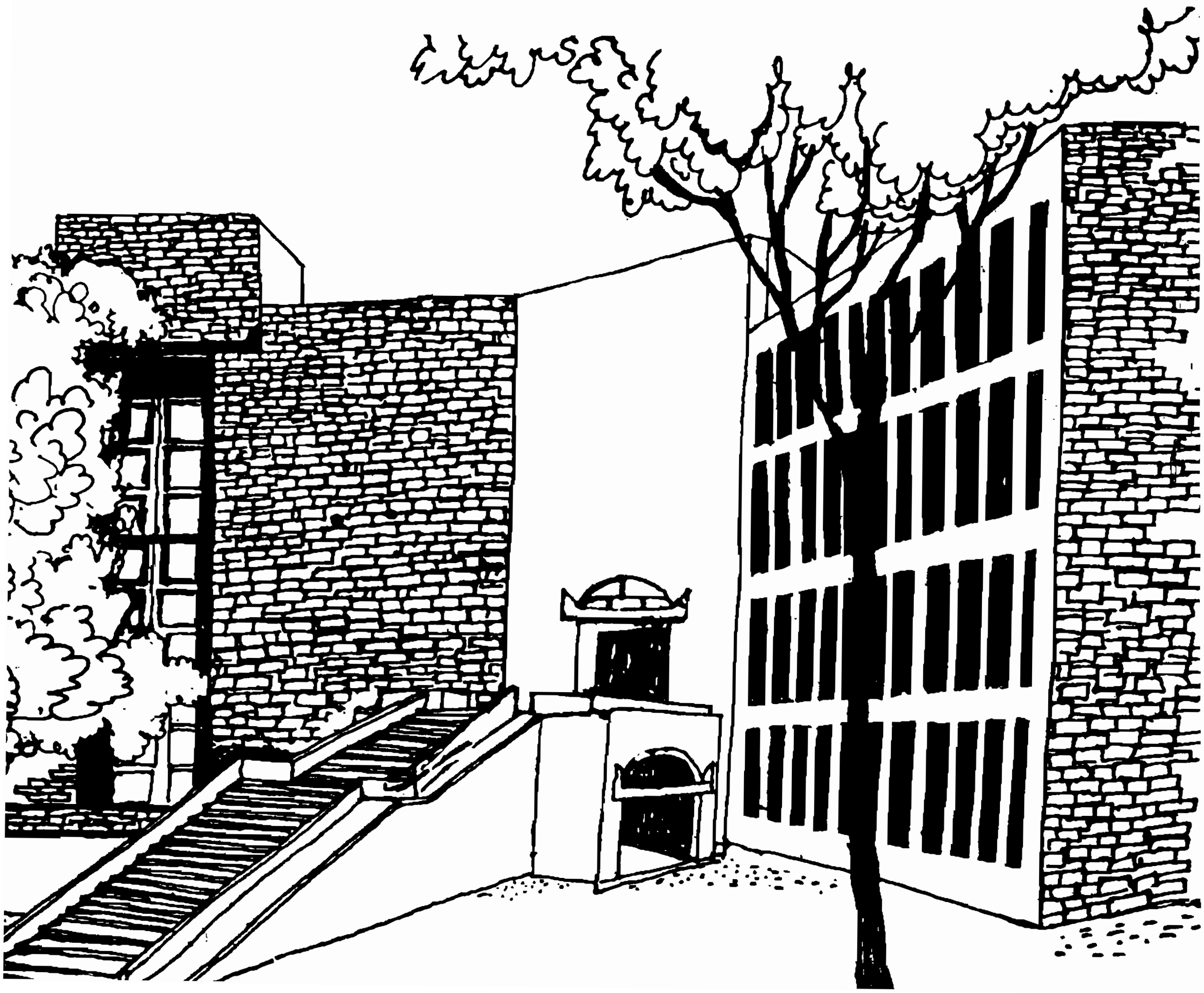

INDUSTRIAL GROWTH DURING THE EIGHTH FIVE YEAR PLAN PERIOD AND BEYOND

By

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INDUSTRIAL GROWTH DURING THE EIGHTH FIVE YEAR PLAN PERIOD (1992/93 - 1996/97) AND BEYOND

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I : OBJECTIVES

An attempt is made in this paper to answer three questions :

(1) The Eighth Plan envisages the rate of growth of 8.2 per cent in industrial production. Is this target likely to be attained?

(2) This plan is set in the long-term perspective of the Ninth and the Tenth Five year Plans - 1997/98-2001/02 and 2006/07. The rates of growth of industrial production for these plans are however, not indicated, but in view of the high rates of growth of gross domestic product (GDP) thought of for these plans, 6.05 and 6.5 per cent relative to 5.6 per cent for the Eighth Plan, the growth rate target of industrial production during the Ninth and the Tenth Plan, would only be higher than the rate of 8.2 per cent during the Eighth Plan. Our guess of the rate for these plans is about 10 per cent. What are the prospects of this rate materialising?

(3) Industrial policy and planning has been having a mix of economic and social objectives. This mix continues during the Eighth Plan and is likely to continue later, though the emphasis may change. Industrial growth may be treated as an economic objective, and such other-

protection/promotion of small industry, reduction in regional imbalances, and prevention of concentration of economic power in private hands as social objectives. Although the latter are not the direct concern of this paper, in view of their inter-connection with the economic objective of industrial growth, they cannot be totally ignored in any serious discussion of industrial problems. As a compromise, we, therefore, raise a supplementary question on social objectives, and attempt to answer it briefly. How well will they be served in future?

While answering these questions, this paper draws upon the past experience of our industrial growth, and relies on the logic of our lately adopted liberalisation policies.

India's experience of planned economic development dates back to 1950. It, thus, relates to a period of over four decades. As regards industry, this experience is best examined by dividing this period into four sub-periods of 1950-65, 1966-74(80), 1975(81)-90, and 1991-92 and 1992-93. (In deference to the view that the second period ends in 1980 and the third period begins in 1981, we have put these years in brackets). The following four sections of this paper are devoted to these sub-periods. The sixth section deals with the remaining four years of the Eighth Plan and the period beyond. The last section gives a summary of answers to the three questions posed above.

A couple of clarifications are in order here. First, this paper is in the nature of a bird's eye view. By its very nature, it has, therefore, a broad sweep, and such a paper cannot meet details. It is, however, more than a mere outline, as will be found by the reader. Second, the statistics of rates of growth of industrial production are in terms of per cent per annum. The rates are trend-based averages (Sections II to IV) or average annuals (other sections) and are worked out from the Index of Industrial Production (1980/81 = 100). They are of aggregate production in the large organised sector of mining and quarrying, manufacturing and electricity (which have the weights of 11.46, 77.11 and 11.43 in the index). Reference years are calender years or fiscal years indicated as, for example, 1951 or 1991/92.

II : 1950-65

The fifteen year period, 1950-65 - the first three plan periods - witnessed the rate of growth of 7.3 per cent. Two features underlying this figure may be noted. First, the rates varied greatly - from a low of 1.8 per cent in 1953 to 12.1 per cent in 1960. Second, in nine of the 14 years, the rate exceeded the average of 7.3, of which in seven it did so continuously (1959 to 1965).

This period is described as a period of high growth rates. It compares very favourably with the earlier period (1990-46) during which industrial production is estimated to have grown at the rate of 2 per cent per annum, and also with the latter period - 1965-74, during which the growth rate decelerated to 4.3 per cent per annum.

The high growth of this period is easily explained, and there is a broad measure of agreement on that explanation. In that include : emphasis on investment on industry and industry-related infrastructural sectors, the complementary character of public and private sector investments, and the creation and nursing of captive home markets needed for import-substituting industrial production.

At a more general level, we had inward looking policies in trade, state-regulated or guided policies in respect of interest, foreign exchange and a number of other key prices, and socialist policies in respect of controls on private ownership/management and expansion of the public sector through starting of new enterprises and nationalisation of private sector enterprises.

III : 1966-74(80)

These policies continued during this period and in some cases they were strengthened. For example, nationalisation of commercial banks, passing of the MRTP Act, specification of targets of lending and/or lending at concessional rates for priority sectors and backward areas took place during this period. But these policies appear to have lost their steam during this period, as is seen from the fact that the growth came down to 4.3 per cent.

Here also, the rates varied. For the first time since planning, industrial production declined - by -0.4 and -1.3 per cent in 1966 and 1967. And for the other years during the period ending 1974, the growth rate varied from 0.5 per cent in 1973 to 7.1 per cent in 1969.

The situation looks a little better when the terminal year is put at 1980, but not really very much.

Among the more specific explanations for this slow down, there has been considerable controversy. The issues which figured in the controversy were (1) worsened income distribution operating principally through shrinkage of demand, especially of mass goods, (2) poor performance of agriculture, (3) slow-down in import-substituion, (4) slow-down in public investment, especially in infrastructure, and (5) regulatory and restrictive policies in respect of private enterprise. The emphasis on these points is not merely at the primary level, but it is carried forward by bringing into account, in some cases, the weakening of backward and forward linkages therefrom.

A detailed examination of some of these points. in the light of the more and detailed empirical evidence, seems to lend support, by and large, to the last three factors.

IV : 1975(81)-1990

The decade and a half, and the decade in particular, ending 1990 marks a spectacular turnaround to high growth rates; with the rates of 6.5 and 8.3 per cent respectively. The rates during 1975-90 varied from 0.8 per cent in 1980 to 12.1 per cent in 1976, and during 1981-90 from 4.2 per cent in 1982 to 10.9 per cent in 1985. Of the fifteen years, in 10 the rate exceeded the average of the period (6.5) of which in seven (1984 to 1990) it did so continuously. And of the ten years, in 7 the rate exceeded the average of the period (8.3), of which in three each (1984 to 1986 and 1988 to 1990) it did so continuously.

It appears that the government seems to have been convinced of the plausibility of, among others, slow-down of investment, especially in public sector infrastructure and poor productivity thereon, and of regulatory and restrictive policies for private enterprise together with poor performance of public sector as villains of the slow-growth period. Consider, for example, what it did later.

First, investment in infrastructure increased and capacity utilisation also improved during this period ending 1990. Thus, for example, the allocation to the infrastructure sector (energy, transport and communication) which was of the order of 36 to 39 per cent of the total public sector outlay from the Third to the Fifth Plans, was stepped up to 46 per cent in the Sixth Plan, and was fixed at 47 per cent in the Seventh Plan.

The other development relates to changes in policy which permitted a greater role to the private sector in development than in the past, and to the easing of restrictions and controls. Thus, for example, of the total investment in the Fourth and Fifth Plans, the share of the private sector was around 40 per cent. The share in the Sixth Plan went up to 47 and it had a majority share of 52 per cent in the Seventh Plan.

As to the specific policies, references are invited to raising the limit of investment for licensing, delicensing a number of industries, broad-banding, streamlining of licenses, raising investment limits of MRTP companies and exemption to such companies from some provisions of the MRTP Act, increased participation by private sector in areas earmarked for public sector, etc. Attention must also be drawn to liberalisations in the fiscal, trade and financial areas.

The turn in favour of these policies seems to have commenced around mid-seventies, beginning with a measure of skepticism on the capacity of old policies to deliver respectable growth. Later, positive steps to liberalise the economy were initiated, beginning with minor changes and moving towards major ones. But the more substantive, more significant, and more pervasive changes took place around mid-1991 and after a brief spell of lull they continued in that direction with a measure of conviction not shown before by the Government. But as these changes occurred in 1991 and later, they are taken up in detail in the next two sections.

To put it more generally, this period marks, so to say, a U-turn in Indian economic policies. In respect of ownership/management of means of production, government was moving away from the socialist to the capitalist path, in respect of trade policy, from the inward-looking to the outward looking path, in respect of foreign investment/technology from the non-dependent to the dependent path and in prices of goods and services, foreign exchange, interest, etc. from the administered (distortionary) to the free (non-distortionary) path of growth, of industrial growth in particular.

V : 1991/92 and 1992/93

Among the major and significant economic reforms of 1991/92 include : depreciation of the rupee by 20 per cent, introduction of exim script and its replacement by partial convertibility of rupee on trade account and other liberalisations in regard to trade, industrial licensing, foreign investment and technology, MRTP company investments, opening up of a number of areas for private sector, lending rates by financial institutions and banks and reduction in statutory liquidity ratio. And although after that there was lull in reforms for some time, thanks partly to non-economic factors, there was some movement in that direction later during 1992/93. Thus, for example, capital market was freed from government control and the office of the Controller of Capital Issues was abolished. Investment restrictions on foreign investment were further liberalised. Private investment in exploration of oil and refining was allowed and the National Renewal Fund was operationalised.

And yet, industrial production during 1991-92 declined slightly by 0.1 per cent. During April-October 1992-93, its growth rate was 3.8 per cent, and for the year as a whole, it could, hopefully, increase to 4 per cent.

Why did the growth rates during these two years slide down, inspite of the acceleration in liberalisation? Have these policies which had given high growth rates during the eighties lost their force, as was the case of the previous policies of 1966-1975(80)? Or does the explanation lie elsewhere?

The explanation, it seems to us, is elsewhere. First, it must be remembered that the high growth rates of the eighties led to a major macro-economic imbalance with its inevitable adverse consequences in the long run for industrial growth itself. And when the government began attacking this macro-problem, it produced an adverse impact on industrial growth.

To elaborate, the problem referred to above is the problem of mounting fiscal deficit relative to GDP. The high industrial growth rates of the eighties along with several other factors, led to the growing fiscal deficit (excess of total expenditure including loans net of lending over revenue receipts, grants and non-debt capital receipts) relative to GDP increasing from about 5-6 per cent during the early eighties, to the average of about 8.2 per cent during the later half of the eighties (1985/86-1990) and to 8.4 per cent during 1990/91.

This has had two inevitable consequences. It fueled heavy inflation and created a severe balance of payments crisis. Thus, for example, the wholesale price index (1980/81 = 100) which was moving up at the rate of 5 to 7 per cent per annum during the early eighties, was moving up at 11-12 per cent during the later part of that decade and in 1990/91, and reached a high of 14 per cent during 1991/92. Similarly, foreign exchange reserves (Rs. 5100 crores) which stood equivalent at under about 4 months' imports during the early eighties were sliding down gradually, standing at Rs. 2500 crores — equivalent of 2 weeks' imports during April-June 1991, driving India to the verge of default.

Government's policies during 1991/92 and 1992/93 have, therefore, been dictated to bring about corrections at the macro-level, by cutting fiscal deficit, reducing inflation and improving foreign exchange reserves. So government has applied a number of breaks which along with other factors have produced a near stagnancy and a poor rate of industrial growth in 1991/92 and 1992/93.

To elaborate, the fiscal deficit in 1991/92 was reduced to 6.2 per cent of GDP (revised estimate), and to 5 per cent (budget estimate) in 1992/93. This alongwith a number of complementary measures have brought some control over inflation and improved our foreign exchange position. Thus, for example, inflation rate during 1992/93 is estimated to be about 7 per cent, and foreign exchange reserves have also gone up considerably, thanks largely to the in-flow of foreign loans, Rs. 14,000 crores — equivalent of 3 1/2 months' imports

These policies affected adversely industrial production both from the supply as well as demand side. To take the latter first, reduction in fiscal deficits led to a shrinkage of demand from government and government companies/corporations, and this has had a chain effect. The recessionary conditions which had begun to manifest themselves towards the end of the eighties became more acute now. Exports also, particularly rupee exports, declined. The strain on industrial production from supply side came largely from import compression and increased import prices and cuts in the availability and high cost of credit. Once the fiscal deficit, inflation and foreign exchange reserves started moving in the directions expected, government relaxed its hold, and that along with other measures adopted in 1992/93 led to a bit of revival in that year.

Yet another point has to be kept in view, while understanding the industrial growth of these two years. It must be remembered that the kind of policies which we have initiated, especially since mid-1991, represent major changes, marking a clear and definite turn in a different, if not an opposite direction. Such a period is naturally a period of turbulence, even when changes are designed to produce effects in the same direction. This is especially so when such changes come simultaneously or follow one another in close sequence. Recent changes in industrial, trade, exchange rate, financial and fiscal policies are all of this genus.

It is common knowledge that there is a time-lag between such changes and their percolation in production which is what we are examining with reference to industry. Policies have to be followed by measures, and both have to be appreciated in the right spirit and followed up by investment decisions, capacity installation and production by the economic agents, to seize the opportunities thrown up by the changes. Moreover, in a federal system, changes initiated at one level of government have to be followed at other levels of government, and have to be mutually supporting. In view of this, during this period of adjustment, production may not only not respond positively to these changes, but it may even slow down. And the slow down period may be short or medium - two to five years - depending upon the spread, speed and sequencing of these changes, and the response of the economic agents to these changes. This may account partly for the slow down of these two years examined here.

But after this period of transition, on the logic of liberalisation, industrial production may be expected to accelerate in a sustained manner. For this optimism we entertain for the medium and long periods, we rely upon that logic which is elaborated in the context of growth prospects in the next section.

VI : 1993/94 AND BEYOND

Industrial growth for 1992/93 - the first year of the Eighth Plan - is estimated to grow at the rate of 4 per cent. In a recent interview, the Finance Minister has said that he expected the growth rate of 7 per cent in 1993/94 - the second year of the Eighth Plan. So if growth is to attain the Eighth Plan target of 8.2 per cent, growth rate for the remaining three years of the plan - 1994/95, 1995/96 and 1996/97, has to be of the order of about 10 per cent per annum. (It may be recalled in passing that the base year of the Eighth Plan, 1991/92 suffered a slight decline in industrial production. This 'statistical' advantage of the plan is, however, ignored here).

Government seems determined to achieve a very high growth rate of industry in future, as is seen from the strengthening of the liberalisation policies and measures initiated earlier. Thus, for example, infrastructural bottlenecks which held back growth during 1965/74(80), and the minimisation of which accelerated growth during 1975(81)-1990, even now continue to receive attention as a high priority problem. This is seen from the fact that of the total public sector outlay of the Eighth Plan, infrastructure sectors (energy, transport and communication) get 46 per cent - about the same as in the Seventh Plan. In fact, in view of new open door policy for the entry of private sector, including multi-nationals, coupled with various incentives investment in these sectors would be far more than earlier. The importance of private investment in future is highlighted by the fact that of the total investment in the Eighth Plan, the share of private investment, which as noted earlier was being stepped up from the Fourth Plan onwards, is raised to 55 per cent in the Eighth Plan - 3 percentage points above that of Seventh Plan. The Eighth Plan document has given an outline of a number of liberalisation measures called for to achieve the targets.

A lull for some time after mid-1991 reforms, the security scam and the Ayodhya incident, among others, had created a doubt in regard to the willingness and capacity of the government to carry further and forward the reform measures. The 1993/94 budget, however, should clear such a doubt, as the budget marks a clear, decisive and substantial progress in liberalisation. To refer just to a few major budget proposals in three areas :

1. Direct Taxes: Complete tax holiday for new undertakings in power, tax relief on payments under voluntary retirement schemes, and tax reliefs to foreign institutional investors investing in securities.
2. Indirect Taxes: Import duties and excise duties removed completely from a few items and reduced considerably from a large number of items in varying proportions.
3. Rupee made fully convertible on current account.

And yet with these and such other liberalising measures as may be adopted during the Eighth Plan, growth rate of the order 10 per cent per annum during the last three years of the Eighth Plan which is necessary to achieve the target of 8.2 per cent for the Plan may not be achieved. The reason for this pessimism stems not merely from the disappointing growth performance of 1991/92 and 1992/93 inspite of favourable policies, but also from the fact of lag with which these supply-rigidity reducing measures, considered in the context of the macro-level concerns of low fiscal deficit, low inflation and comfortable foreign exchange position - would work. These concerns could even lessen the force of liberalisation measures at the sectoral levels in the near future as they did in 1991/92 and 1992/93.

All-in-all, it may perhaps be more realistic to hope for an average rate of growth of about 7.5 per cent for the remaining four years of the Eighth Plan. This together with the 4 per cent growth for the first year may yield an average rate of growth of about 7 per cent per annum. On this judgement, 8.2 per cent growth for the Eighth Plan seems to be unattainable.

But beyond the medium-term during the Ninth and the Tenth Five Year Plan periods, higher growth rate of the order of 9-10 per cent per annum seems quite feasible. This optimism is based on the assumption that by the end of the Eighth Plan we would have attained stability at the macro-level as regards fiscal deficit, inflation and foreign exchange, and the period of adjustment of the economic agents to the new policies would also have been over, so that the logic of liberalisation will begin asserting itself with full force in practice.

This logic would lead to higher growth in several ways. First, a number of changes in industrial licensing, foreign investment, foreign technology agreements, the MRTP Act, etc., have done away with the prior clearance of the government. In such cases, project time. and, therefore, project cost will be reduced. This will free material and human resources for more productive use: from cultivating contacts with persons with power and influence to get such clearances. Thus, the input cost per unit of output in the proposals which are freed from prior clearance requirements will go down, and reduce cost.

Second, the changes in respect of foreign investment, foreign technology agreements and rupee convertibility are designed to attract capital, technology, and marketing and managerial expertise from abroad. These measures, together with reduction in import duties, will give a boost to exports in particular. They will lead to additions of scarce resources of technology and capital from abroad. In as much as these resources are also more efficient, industrial production will increase both through their higher productivity as well as through their additionality.

Third, some changes such as opening up of some areas reserved earlier for public sector for private enterprise, privatisation of public sector, delicensing and reduction in import duties would make Indian enterprises more competitive among themselves and vis-a-vis imports.

Fourth, some measures thought of for the public sector such as purposeful formulation and the implementation of Memorandum of Understanding and its monitoring, professionalisation and greater autonomy may be expected to improve the performance of the enterprises that will remain in the public sector.

Fifth, amendments in the MRTP Act regarding large houses and dominant undertaking may be expected to promote large and efficient scales of production and greater emphasis on controlling and regulating monopolistic, restrictive and unfair trade practices will curb the anti-competitive behaviour of the firms in the monopolistic, oligopolistic and ineffectively competitive markets and thus, promote competition and through it efficiency.

To sum up this point : additionality of resources and improvements in technological, allocative and X-efficiencies that will follow from pro-competiti~~ve~~on policies are expected to yield respectable rates of growth in industry - of the order of 9-10 per cent per annum in the long period, after the Eight Plan period most of which is bound to remain a period of transition which for reasons discussed in the previous section, would produce only modest growth.

That this logic is not an empty box is vouchsafed by the experience of a number of countries which have followed liberalisation policies. Hong Kong, Korea (South), Singapore, Taiwan, Indonesia, Pakistan, Malaysia, Thailand and China have grown at high rates recently, especially in industry and manufacturing. True, relative to India, the first four are small countries, but the next four are not that small, and China is, indeed, big. So it seems that size of the country may not be that important in accounting for growth as it was thought of earlier. In any case, we should take whatever message is relevant for our country. To cite some statistics from the *World Development Report, 1991: Industrial* growth during 1980-1989 was 12.4 per cent in Korea (South), 5.3 per cent in Indonésia, 6.5 per cent in Malaysia, 7.3 per cent in Pakistan, 8.1 per cent in Thailand and 12.6 per cent in China. With 6.9 per cent, India compared favourably with Indonesia and Malaysia but poorly with the other four countries. When a comparison is made on *manufacturing* growth for this period, India with its 7.3 per cent was at the bottom in this list. Comparable figures were: 13.1 for Korea (South), 12.7 for Indonesia, 8 per cent for Malaysia, 7.9 for Pakistan, 8.1 for Thailand and 14.5 for China. This experience points to the potential of 10 per cent for India in the long run.

Finally, a word on social objectives of the industrial sector – in particular protection/promotion of small industry, reduction in regional imbalances and prevention of concentration of economic power. As is well known, we have been having specific policies since planning to subserve these objectives. What about these policies now and in future, and how would these objectives be served?

The new economic policies unleash a strong dose of competitive forces. These forces promote economic efficiency and through that produce growth. Specific policies designed to further social objectives do so, often, constraining the efficiency induced growth. In view of the primacy of efficiency based growth that is patent in the new policies, the latter policies, which were in any case, not very substantive or significant, for a greater part of the planning period earlier, now become more secondary than before. So only a feeble boost from such policies may be expected for social objectives in future.

And yet, inspite of low priority of social policies in the past, considerable progress has been recorded on social objectives. Modern small industry has emerged as a sector to reckon with, inter-state disparities as also intra-state disparities in industrially developed states have narrowed, and the concentration of economic power has declined. While policies and measures on behalf of social objectives have played a role in producing the results thereon, it is suggested that a more significant role may have been played by high growth itself through its percolation effect. If this interpretation is accepted, the new efficiency-based, high growth promoting policies may be expected to strengthen the progress on social objectives as well in the long run. However, in the short period of transition, progress on social objectives will be retarded, partly because of diminished importance of policies for these objectives, and partly because growth itself will only be modest.

VII : SUMMING UP

Although answers to the three questions posed in the first section are already given in the previous section, this paper may be concluded by putting them in a summary form here.

(1) The Eighth Plan target of 8.2 per cent industrial growth is unattainable. Seven per cent seems to be realistic.

(2) As to the 10 per cent figure for the Ninth and the Eighth Plans, we suggest that we could get 9 per cent, and could go up to even 10 per cent.

(3) The prospects of progress on social objectives in the near future of the Eighth Plan period are not quite good, but they seem to be bright in the period beyond.