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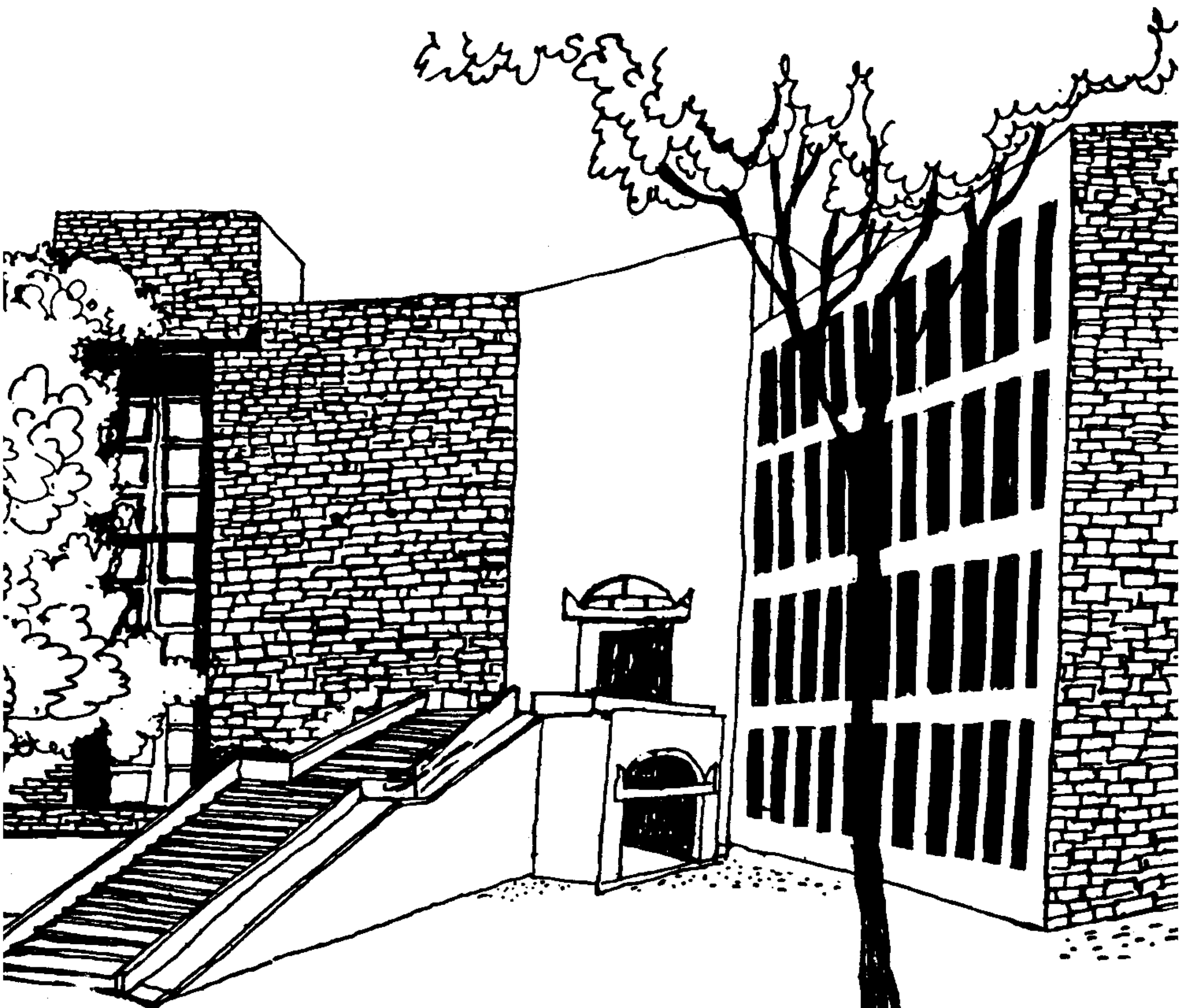

INDIAN ECONOMY IN 1990s

By

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ABSTRACT

There is a silver lining in the dark clouds at the horizon for the Indian economy. In the short term India has to sacrifice little growth in the fiscal year 1991-92 and in all likelihood it would not be very good in 1992-93. In the short run, the external economic environment is not favourable especially prospects of foreign trade in immediate future is not favourable due to slow down of the world economy. The budget success depends on restraining the inflationary pressure, boosting exports and raising productivity. India needs a bit of luck. A couple of good monsoons and low international price of oil and co-operation from the organised labour will be very helpful. If India uses next two years constructively there is no doubt that Indian economy would deliver a vibrant and an exuberant nation which would surprise the world - and itself.

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1. Overview

The panic measures taken in the first half of 1991 by the Chandrashekar government are bearing bitter fruits now. Those measures were essential at that time as the government coffers were empty and the external situation in the Gulf had brought the situation to the boil. Subsequently, the liberalisation of the Indian economy under the Rao government has kept the market cheerful in anticipation that economy in general is going to show higher growth and productivity. The anticipation is well founded but capital market should brace itself for the bad news. On all accounts, except the fiscal deficit measure the government's estimates were over-optimistic for 1991-92 and so is the case for 1992-93 budget estimated figures. There is no promised land after that if the government does not bring structural reforms in the labour laws and introduces a bold exit policy. The RBI measure to free deposit and lending rates, coupled with scrapping the incremental cash reserve ratio of 10%, is going to ease the monetary condition in few months time. One must not loose sight of macroeconomic stability - i.e. price stability and low external deficit - which is the linchpin of successful liberalisation, not the deregulation of financial sector *per se*.

The privatisation proceeds should not be frittered away in doing window dressing to show reduced fiscal deficit only and shift the burden on the public sector financial institutions. The government should try to retire part of the domestic debt. The retirement of debt through the use of the proceeds from the sale of equity of public enterprises would pump additional funds into the money and capital market in a non-inflationary way and help finance a rising volume of investment as well as broaden the base of the stock market operation. The reduction in short term debt shall help in reducing total government sector expenditure as a proportion of the GDP in the medium term. There is no trade off between fiscal adjustment and structural reform. One cannot assure that the liberalisation programme and other structural reforms would be painless, but all economies have to brace themselves to bear some pain of growth.

2. Forecast

The forecast for the Indian economy suggests a bright prospects in the medium term if the economic reforms stay on course. First, the good news; if the time bound programme initiated by the Finance Minister as indicated in the Letter of Memorandum to the IMF and Structural Adjustment Loan/Credit to the World Bank, in letter and spirit, it is very likely that barring wide spread droughts in the country, the country is going to show a phenomenal rise in economic growth. In the medium term and in long term these structural changes are going to transform the Indian economy into an vibrant economy.

Table 1: Exogenous Variables

	1990	1991	1992	1993	1994	1995
World						
Trade growth (%)	4.0	1.5	2.0	6.0	5.9	5.5
Real Short-term Interest	4.0	4.1	3.7	3.8	3.8	4.2
Real Long-term Interest	5.7	5.4	5.0	4.6	4.1	4.4
O.E.C.D. Inflation	4.5	4.3	3.4	3.0	2.9	2.9
Crude Oil($/barrel)	18.0	20.0	18.0	18.0	19.0	19.0
Domestic						
	90-91	91-92	92-93	93-94	94-95	95-96
Rainfall (% of normal rainfall)	106.0	92.0	100.0	100.0	100.0	100.0

Table 2: Forecast

	90-91	91-92	92-93	93-94	94-95	95-96
GDP growth (%)	5.6	2.0	2.5	4.0	6.3	6.3
WPI (%)	12.1	12.0	10.0	8.0	6.5	6.0
CPI (%)	13.6	13.2	11.5	8.5	7.0	6.5
Exports (%GDP)	6.2	7.2	7.5	7.9	8.2	8.3
Imports (%GDP)	8.2	8.1	8.5	8.7	9.0	9.0
Current a/c (%GDP)	-3.5	-2.5	-2.0	-1.4	-0.9	-0.7
Current a/c ($ bill)	-9.9	-6.0	-5.3	-4.0	-3.0	-3.0
Capital a/c ($ bill) (principal repayment)	-3.0	-3.0	-3.3	-4.0	-4.5	-5.0
Exchange Rate (Rs/$) (open market, nominal)	18.2	24.5	32.0	33.5	35.8	37.6
Production (growth; %):						
Agriculture	3.7	0.0	1.0	2.1	2.2	2.2
Non-agriculture	7.0	2.9	3.3	5.0	8.0	8.0
Investment (% gdp):						
Private Sector	14.0	12.0	13.5	15.0	15.5	15.2
Public Sector	10.5	9.5	5.0	4.0	3.5	3.5
Govt. expdt. (%gdp) (Central + State + UTs)	34.2	32.6	31.4	31.2	31.0	31.0
Central govt. def.(%gdp)	9.0	6.3	5.0	4.0	4.0	4.0

India's private enterprise, which has done well in spite of heavy regulation imposed by the government, could set the tone for an upswing in the economy. Now the bad news; if the entrenched political interest groups do not oblige and do not relegate their economic power to the people or the Bureaucracy drags its feet in the implementation of the reforms we are likely to have an insipid growth rate in the medium term and in the long term as well. This will deliver a heavy blow to the credibility of Indian economy and an opportunity missed for long time to come. This would present a pitiful sight of a weak and tired caged lion waiting to be fed by its captors. The outcome in years to come would see a moderate rate of inflation around 6% p.a. and a growth rate of 6%-6.5% per annum.

3. External Factors

We have assumed some external factors for our forecast. Underlying assumption in this forecast is that India is still quite insulated from the world economy and unlikely to affect any external variable.

3.1 World Interest rates

Due to the slow down of economic activity in the U.S. we have very low short-term and medium-term interest rates. The Fed is not going to raise the rates dramatically in the run up to the presidential elections. The monetary condition in the London market are already quite tight. Any easing in German rates by the Bundesbank before the end of the present wage round is unlikely which suggests that it will be early June before there is any movement downward. This would see interest rates in whole of the EEC coming down. Japanese growth has slowed down considerably due to a slow down in the world activity and a tight monetary policy. The rapid slow-down led to cuts in discount rate of 0.5% in both November and December last year. The Bank of Japan is likely to ease its monetary policy further; especially now when there are good indications that the US is coming out of recession. This is good news for India as the servicing burden of her foreign debt would be that much lighter as long as short-term borrowing is kept under control.

3.2 World Energy Prices

The weakening of world oil prices recently can only further reduce inflation in the G7 countries. Oil prices have fallen by around $4 a barrel from a fourth quarter high and are now around $19 a barrel. The recent OPEC agreement has done nothing to stop the downward trend. The OPEC agreement would unravel as Saudi Arabia has said that it will produce above its quota. Saudi Arabia is unwilling to relinquish the market share it gained during the gulf war and argument over quotas can only increase during the year as Iraq and Kuwait resume exporting. However, the nominal crude prices are unlikely to crash as Saudi Arabia would oblige her Texan friend by cutting its production in time of need.

World energy prices are likely to hover around $18-$20 a barrel and hence would fall in real terms in the medium term. The world reserve of crude oil according to the International Energy Agency is all time high and as a result of low economic activity demand is unlikely to pick up. Return of Iraq and Kuwait to world energy market is going to increase the supply in the near future and put a downward pressure on crude prices and both would like to raise the oil revenue to finance its reconstruction.

3.3 World commodity prices

The prices of primary commodities are likely to remain depressed as the economic position of every G7 nation is one of recession or near recession. But in the medium term the commodities would maintain their prices in real terms. Except for edible oil price rise which affects India's trade balance adversely. Prices of other commodities are not going to affect India's trade balance in medium term as India, like in the late eighties, is going to follow a competitive exchange rate policy for rupee until it has dual exchange rate policy and later on markets are unlikely to over-value rupee in medium term.

3.4 World trade growth

World trade growth is going to be sluggish next year as the developed economies are beset with various domestic problems and consolidating high growth phase of late eighties. The indications are that the US economy is showing signs of recovery. The slow down in both Japan and Germany was rather more rapid than anticipated and the rest of the G7 countries have had difficulty in sustaining a recovery and in a number of cases their economies have turned down again.

The glimmer of hope for the world trade from the East European countries has been dashed as their main trade partner and supplier of crude oil - former Soviet Union - is grappling with its political identity and new trade institution and development of links with new and old trading partners would take more than a year or so. The $18 billion loan from G7 to Commonwealth of Independent States is to keep them afloat. However, there is very good chances that in 1993 and 1994 world trade volume would grow in the region of 6% p.a.

The GATT proposals (the Dunkel report) is likely to unravel as the developed countries could not reach an agreement in Japan even after extending the Easter deadline. The liberalisation in textiles and services would be lost to the detriment of the world economy.

3.5 Domestic rainfall

Rainfall is assumed to be about average. We are not as pessimistic, as some commentators have suggested that it is a statistical freak that India has got average rain in three years in a row. Above average rain in some region and below average rain in other regions in medium term is going to produce a desirable average. Long term series of rainfall index suggests that on average over a three year period India gets average rainfall. According to the Indian Meteorological Department forecast the parameters like northern hemisphere temperature, wind pressure etc. which are supposed to affect monsoons favourably in India suggests that there are good chances that in 1992-93 India shall have a normal monsoon.

4. Output

In the forecast output growth for the year 1991-92 is 2.0%. In 1992-93 growth is going to be hit hard and may reach just 2.5% after the rapid liberalisation process. But having digested the reform package and having got used to the new economic environment, the economy may grow at a rate of 4.0% in 1993-94 and around 6.5% thereafter.

5. Production

The preliminary figures of 1991-92 of industrial production show a marked slow down in the economic activity. Cause of this has to be found in the tight monetary policy of the government and almost penal rate of interest on short term bank loans.

5.1 Agricultural Production

The agricultural production in the current fiscal year has been at a standstill and the government had pinned its hope that an increase in agricultural production would contain the rise in price level. But a real worry in the minds of farmers is that in the given political climate it is highly unlikely that the subsidies on the fertilisers would be maintained. Therefore, if they have to buy fertiliser at a higher price later, they may as well keep a bit of stock now and sell it in open market during lean period when price is remunerative. Not only that, State subsidy on electricity will soon go on the anvil. The issue is hot and may get a hammer blow any time.

As we have assumed an average rainfall over the horizon of our forecast the growth rate of the agricultural production is 2.2% in the medium term. In the medium term one or two years may post a bad harvest due to inadequate precipitation but that shortfall is immediately recovered in the next crop season if Lord Indra casts a favourable look on Indian agriculture.

Some commentators are sounding alarm bells due to low level of *government* food stocks. The strategy to increase procurement would need to improve the profit margin by raising procurement prices. This would entail raising prices in the fair price shops in line with inflation to keep fiscal deficit under control.

5.2 Non-agricultural Production

The industrial production had been the first casualty of the economic slow down and a tight monetary policy in 1991-92. In the past few years domestic industry enjoyed a protected market and sellers market. In the brave new world of decontrolled environment entrepreneurs would be called upon to be more responsive to the market forces and consumers demand than the wishes and idiosyncrasies of bureaucrats. The wind of change is blowing through board rooms and from the news reports it seems that industrialists are fast adapting to their new environment and freedom.

Automobile, consumer durables, textiles and capital goods have been hardest hit with producers planning to cut down production and retrench staff. In many industries stocks are piling. What the economy is witnessing is a slow-down induced not so much by a fundamental lack of demand as by import and credit curbs, plus selective tax hikes for consumer durables. A survey done by National Council for Applied Economic Research in September 1991 suggests that industrialists do not reckon that there is lack of demand for their products, but they are not able to produce as much as they would because of rise in credit cost, non-availability of funds and curbs on import of raw materials.

Hydrocarbon and telecommunication sector is going to see major liberalisation in few months time. The growth in these two sectors is going to give a major boost to industrial production in the next fiscal year and it would have ripple effect in the whole economy.

In our forecast a quick adjustment takes place in the short term and it seems that given the liberalisation the industrial production will bounce back in 1993-94 and a 10% p.a. growth rate in the medium term is achievable. As the government has already promised that it is going to lower the import duty, it is going to tinker with the excise duty and state governments' may tinker with the sales tax. This tinkering will raise industrial prices in short run. This is inescapable during the structural adjustment period and by the end of fiscal year 1993-94, hopefully, all the major adjustment may have taken place.

6. Investment

6.1 Private Investment

If one assumes that the stock markets are forerunners of future profitability and investment of private sector, it would be hard to find any operator in the bull market to have a moment for Cassendra. But that is the nature of stock exchange. The short term gyrations of stock market defy all economic analysis, but given the nature of the market, gloom and doom may set in equally rapidly especially when adequate capital norms are brought in. Notwithstanding all this, the market is indicating that the wind of change which is sweeping the Indian economy is going to be successful and profitable to the private sector. In our forecast the private investment may grow as much as 20% per annum in the medium term. However, the tight monetary policy is going to affect investment unfavourably in the current fiscal year. Interest rates may fall as much as two percentage points in the fiscal year 1992-93 and another two percentage points next year. Thus we may have interest rates in the region of 16% by the end of 1993.

Some blue chip companies whose new issues are likely to be underwritten by IFC are going to raise funds from the foreign capital market. India is currently in a situation that is very difficult to compare with any other country. However, countries like Mexico, Brazil, South Africa, Turkey and Egypt could be competing for similar kind of investment in future as India.

The signing of the Multilateral Investment Guarantee Agency (MISA) convention - an affiliate of the World Bank - may help in pursuading foreign investor on the attractiveness of investment in India. The MISA gives a security cover to a foreign investor against non-commercial risks involved in investing in India. India needs all the help, in the short term, to bring in foreign exchange by boosting exports and bringing in foreign investment to avoid a serious foreign exchange crunch. Therefore, there is all the more urgency to make the operations of stock brokers more transparent with adequate capital norms as a stock market riddled with insider trading etc. deters a direct foreign investment as well.

6.2 Public Investment

Public sector investment is going to show further decline in medium term. The overwhelming desire of the government to contain the fiscal deficit would have its first casualty in the planned investment. It is unlikely that the public investment in real terms would remain at todays' level though in nominal terms it may fulfil its plan target as was the case over the last plan.

7. Government Expenditure

In the eighties government expenditure as a proportion of GDP had been rising steadily. In earlier aborted attempt of economic liberalisation - a gradual process which started in 1981 and in 1985 with a bang - India started at the right step but in the middle of the dance, due to distraction from powerful economic groups, found herself out of step with the economic tune. Consequently, at the dawn of the nineties the overworked macroeconomic management needed resuscitation and a stiff dose of economic medicine to cure her from the economic ills. It is not the government expenditure which gave rise to such a situation but it was the way it was financed which gave rise to the sorry state of affairs. Like any patient, who during recuperation period has to follow a strict diet - so is the case with the Indian economy. As widely known it was ever expanding fiscal deficit which fuelled the 'Rajiv Boom' of late eighties; hence there is going to be a strict watch on this single figure. This may explain why the Finance Minister has emphasised this single economic variable.

In the forecast government expenditure has been 'kept' at the same level as promised to the Fund and the Bank in 1992-93. In medium term the government expenditure and the central government deficit as a percentage of GDP is expected to fall slowly as it would be possible to provide for all public services and revenue budget heads without resorting to 'old' methods.

8. Inflation

Inflation (WPI) in the last fiscal year (1991-92) was about 13% and the forecast suggests that next year inflation (WPI) would be around 10% and gradually come down to 6% in years to come. The government has decided that except for decontrol of some minor fertilisers, there would be another 25%-30% price hike of fertilisers by the end of this years kharif season. The removal of subsidies on fertilisers and petroleum products would be gradual. This would put pressure on inflation in the coming years as a result of increase in food prices and transport cost. The reduction or removal of subsidies raises costs in several sectors, laying the ground for cost push inflation. This means a double digit inflation in this fiscal year and around 8% in the fiscal year 1993-94. But from 1994 onwards inflation would come down to a lower level as competitive forces unleashed on the Indian economy would ensure higher production at competitive prices.

9. External Trade

The new export-import policy announced on April 1,1992 is formulated on the basis of trust. The negative list of imports consists of 3 banned items, 68 restricted items and 8 canalised items. Consumer goods continue to be in the restricted list. Even imports of second hand capital goods is allowed, some without license, while others with license. Hotel and tourist industry would have special import facilities. Full rupee convertibility is allowed to 100% EOUs as these units have been adversely affected by the partial convertibility of rupee.

For the fiscal year 1991-92, the current account deficit is going to remain at the level of $6 billion and in terms of rupees it would show a similar deterioration. This is worse than projected by the Finance Minster in his 1991-92 budget. As mentioned earlier, the developed economies were having an economic slow down and domestic turmoil in the Soviet Union and other East European led to government restrictions on Indian exports to rupee payment area. Under such unfavourable external environment and import curbs, a growth of about 7% in exports in $ terms to general currency area is not bad. Overall fall of only 1.8% in $ terms, if not encouraging than it is not discouraging either. These figures may not be good in absolute terms, but in relative terms, it is a good showing in a year of structural adjustment.

Volume of imports under the draconian measures of the early 1991 showed a sharp fall in 1991-92. The improvement in trade deficit has been entirely due to import compression.

In our forecast the trade balance in 1992-93 would improve in $ terms and as % of GDP. However, we are not as optimistic as the FICCI is in their forecast about trade balance. The Federation forecasts a positive trade balance of Rs. 2,200 crore by 1995-96. The Commerce Ministry goal of foreign trade attaining the level of 20% of GDP and a trade surplus in five years time is little too optimistic. This implies an increase in foreign trade by one percentage point of GDP every year for the next five years. Main causes for our comparatively pessimistic forecast are: first, the industries are going to replenish their inventories which they ran down in 1991, but as they have to buy foreign exchange at market price they are likely to be very cautious. Second, trade liberalisation is going to give vent to pant up demand for new technology and latest plant and machinery from domestic manufacturers. However, deterioration in trade balance due to import of capital goods should not alarm anyone as it would enhance the supply side of the economy and would improve the quality of Indian products in the medium term. This is why we shall see a small trade deficit for few years.

From 1992 onwards we may see a higher growth in export volume than that of import volume. Our forecast suggest a trade deficit of about 0.7% of GDP which can easily be financed from transfer payment etc. In short, the overall current balance of payment situation would be under control.

10. Exchange Rate

The success of partial convertibility has influenced the finance minister to change his mind to full convertibility on trade account much earlier than he had indicated earlier. The RBI assurance that the BoP and reserve positions are stable has also played a role in expediting the decision to make the rupee fully convertible on the trade account. The main reason is that the government wants to eliminate grey market (*havala* trade) so that all the remittances come through the official channel which is estimated to be $2 billion per annum. The March figures suggests only half of the remittances through the *havala* trade have been lured to official channels. If all the remittances come to India through the official channel it would give a big boost to India's foreign reserve. The finance ministry is considering a proposal to reduce import duty on gold which is essential to kill the *havala* trade. On the other hand prices of the canalised items like POL, fertilisers etc. would go up about 10%-12% in rupee terms and if this increase in prices is passed on to consumers, it may notch up inflation by another one percentage point.

The premium of 10%-12% on foreign currency in the open market indicate market's confidence in the stability of rupee. The timing for full convertibility of the rupee would depend on this important factor. However, the timing of the full convertibility would depend on the behaviour of the monsoon, on export performance and on the level of foreign reserves in the coming year. The government has liberalised foreign investment by Indian companies selectively and investment by selected financial institutions in the capital market. This way government is able to test the water before taking the final plunge.

In the forecast it is assumed that India would not have full rupee convertibility before March 1994 or so. All the indications are that a unified exchange rate is not going to have a run on the rupee. On the contrary it shall give tremendous incentive to exporters. The goods market is far more competitive than it is thought of. It is the domestic indirect tax system which has made Indian goods uncompetitive in the world market. It must be emphasised that the world will not come to an end after the full convertibility of rupee as the experience of neighbouring countries suggests.

Under our scenario, rupee is going to slide downward to keep Indian exports competitive in the world market as that is how the lack of productivity and higher inflation rate compared with our competitors and trade partners is compensated. This had been the underlying policy of the government in the eighties and it is unlikely to change in the medium term.

11. Interest Rates

The slack season's credit policy announced in mid-April takes the financial sector down the path of deregulation. The abolition of controls on deposits and loan interest rate is going to spur competition among banks. The interbank market is going to acquire new strength as new instruments are going to emerge. The competitive forces are going to be boosted under the liberalised interest rates and the competition between the banks and non-banking financial institutions would be intense. The expected impact of deregulation on interest rate would be downward adjusted as inflation rates start coming down and inflation expectation subsidizes in months to come.

The money market is already gearing up for this. The establishment of a Bombay Interbank Offered Rate (BIBOR) shall go a long way in market deepening. It shall also help in better planning and in forecasting cost of funds and therefore profitability. The financial institutions too have proposed an 'anchor' rate of interest rate which should be a bench-mark for their interest rate structure. The basic long-term rates are hovering between 18.5% and 20%, which are often criticised by industry as being too high and almost unsustainable. By scrapping the incremental cash reserve ratio of 10%, the RBI has demonstrated its willingness to release more credit to revive agricultural and industrial production. Taken along with the 8.5% reduction in SLR at the time of budget, the move means that the banking sector is free to deploy additional 18.5% of incremental deposits for commercial advances. This shall bring down the long term rates. The rates are likely to fall by 2 percentage points in this year as competition hots up between FIs and banks.

12. Debt

12.1 Foreign Debt

The immediate fear of servicing of the foreign debt is over and prudent fiscal policy coupled with denationalization is going to reduce debt to GNP ratio in the nineties. The IMF facility has given a sufficient cushion to India for the next three years when government is most likely to change the portfolio of its foreign debt. In the last three to four months India has not retired any short term debt and is sitting pretty on its reserves.

The negotiation for the Extended Fund Facility (EFF) for $5-$7 billion has been put off until October 1992. The reasons for such a move are as follows. First, the world interest rates are all time low, which has given much needed respite to the government. Second, after the monsoon, the need for such a facility can be estimated with greater confidence. Third, the trend of world trade would be better known, and post budget export performance would be known by that time. Fourth, to get the [illegible]nancial sector reforms and exit policy are essential. The exit policy is becoming a sticky issue and politically it is a hot potato. Nevertheless, the EFF is going to help India in lengthening the IMF loan over 7-10 year period and repayment burden will be less as some of the EFF fund will be soft loan under the Extended Structural Adjustment Facility (ESAF). This is crucial for the on going reform process as $72 billion foreign debt will remain an important source of pressure on the BoP.

Principal repayments will amount to $3 billion in 91-92 and 92-93, but will rise to an annual average of $7 billion in the latter half of the nineties. Disbursement from existing and expected new commitments of commercial lending plus official lending for project purposes are $4.6 billion in 1991-92, about $6 billion in 1992-93 and 1993-94 and $7 billion in 1994-95. Therefore, exceptional financing needed would decline from $3.7 billion in 1991-92 to $2.8 billion in 1992-93. Assuming the export growth in the forecast, it will further decline to $2 billion in 1994-95 and will get completely eliminated by 1996-97.

In the forecast the debt to GDP ratio is going to fall far more rapidly. Although, liberalisation is going to increase import volume and probably import intensity of some of the domestic industries, but India would be able to pay all this from foreign direct investment and growth in export volume.

12.2 Domestic Debt

Given the tight fiscal stance, which government is most likely to take in the near future and try to have a neutral budget in the medium term, domestic debt as a proportion of GDP would show a gradual fall. In 1991-92 itself it has fallen from 29.3% to 28% mainly due to rapid inflation. By international standards the stock of domestic debt is not very large but monetary overhang it has created in the domestic economy is a real worry in the long term. In the medium term, however, its indirect influence on the banking sector will remain Achilles heel in liberalising the banking industry.

In recent years, the internal debt has grown due to compound interest rate. Interest rate payments have been growing faster than the non-interest revenue expenditures. Therefore, along with cutting the growth of revenue expenditure, the problem of growth of interest payment must be attacked directly by liquidating some of the debt.

The logic behind it is that the ratio of interest to GDP was around 4.5% in 1991-92 and it is likely to be 4.6% in 1992-93. To bring down fiscal deficit to the budget estimate of 5% means that the government has only 2.6% of GDP for government capital formation as the revenue deficit is around 2.4%. In 1993-94, if the government wants to reduce fiscal deficit to 4% of GDP, the government would have around 1.4% of GDP for government capital formation. But the government has an alternative. Additional disinvestment in PSUs can be used in purchasing of market debt. The stock of internal debt can be brought down by 5% of GDP (roughly Rs. 25,000 crore) in three years. This will lead to a saving of Rs. 2,875 crore computed at 11.5% rate of interest. The containment of fiscal deficit to 4% of GDP from 1993-94 would be less painful. Without liquidation of a substantial part of the existing stock of internal debt, it would not be possible to eliminate the revenue deficit within next five years.

13. Labour

If there is any single interest group which holds the key of *Kuber's Khajana*, it is organised labour. Their proportion in the total labour force is very small but they can mutilate the entire privatisation and liberalisation programme. It is not they who would see their bread and butter snatched, in fact they have got used to so much of free jam that they do not even want to part with that. It is beyond doubt that a stabilisation programme affects unorganised labour adversely. But what is meant here by adverse effects is keeping standstill and not absolute poverty and hunger. Labour has a great stake in this programme, and going by the experience of other mixed economies, not only for themselves but for future generations to come as well.

Restructuring means we have to get more efficient. This in turn means we must switch our resources from sick, unviable units to new competitive one. Employment is unlikely to suffer in the process, although the power of the organised labour will.

It is necessary to synchronise reforms in all the sectors of the economy. It is possible to run farther ahead in globalising trade & industry and financial sector than labour sector, but beyond a point the exercise will break down. Furthermore, there is no point in opening up our economy completely to international trade of no Indian company can do anything about surplus labour while competing countries can. If Indian companies cannot sell assets, whereas their competitors can. This will reduce the competitiveness of Indian industry.

According to an official document prepared by the industry ministry, the National Renewal Fund (NRF) will have three constituents namely an insurance fund for employees (IFE), a employment generation fund (EGF), and a national renewal grant fund (NRGF). The EGF will provide resources for approved employment generation scheme and the NRGF will deal with immediate requirements of labour in sick units arising from revival or closure of such units. It shall be disbursed in the form of grants. These two components shall be operational for 10 years. Only the IFE which will be set up through contributions from employees and employers will be operational after 10 years. So far so good. But, the fund, according to the study would be made available not only to compensate displaced labour but also for the revival of industrial undertakings, interest subsidies to financial institutions to provide soft loan, approved employment generation scheme in organised and unorganised sector and excess resource requirement for the public distribution system in defined areas. Its implementation is likely to be very difficult, messy and almost impossible. What we really need is a safety net for labour and not a fund to subsidise all social programmes government undertakes in the next ten years.

Some studies show that an introduction of exit policy would make ten million people unemployed. They arrive at such alarming figures by totting up all those people employed in sick or poorly doing units. But, what should be remembered that closure is one of the option for a sick unit; other options are revival, amalgamation, selling the enterprise and retrenchment. Under the alternatives all workers do not get unemployed.

In fact, it would be in the interests of the workers to have an exit policy with government funding a national renewal fund; rather than the present state of affairs wherein private firms are free to declare lock outs without compensation to workers. Moreover, exit policy is crucial as it concerns future investors, especially foreigners. Since the investment programme for the 1990s depends critically on foreign investment, the government should consider an exit policy which applies only to future jobs, while exempting existing ones. This is not a very good solution as it will create a pool of uncompetitve enterprises. But at least this will make everyone happy in the short run.

The human pain in the short term for a part of the organised sector cannot be wished away. The unorganised labour would be asked to pay the price and would be consulted in few years time at the hustings. Hopes are that adjustment in the organised labour is well underway and having got used to new economic environment, the privatisation and the liberalisation programme would be bearing fruits by then.

14. Tax Reforms

The Economic Times-Marketing & Research Group and Credit Capital Finance Corporation poll suggests that the Rao government is going to last more than two years. On the other hand major opposition parties are not clamouring for a poll. Ironically it seems that a minority government is stronger than the previous majority government in bringing about major structural reforms.

The Chelliah report is going to recommend restructuring of corporate taxes and it is more than likely that in 1993-94 budget direct corporate taxes would be lowered. This shall attract more direct foreign investment than expected now. This would be very much in line with the IMF's EFF loan. As the Fund would like to see India as a winner in the year of its golden jubilee in 1994. It is unlikely that India shall be refused this loan in October 1992. But the conditions attached to that especially on implementation of an exit policy is a stumbling block

15. Conclusion

There is a silver lining in the dark clouds at the horizon. In the short term India has to sacrifice little growth in the fiscal year 1991-92 and in all likelihood it would not be very good in 1992-93. In the short run, the external economic environment is not favourable. The budget success depends on restraining the inflationary pressure, boosting exports and raising productivity. India needs a bit of luck. A couple of good monsoons and low international price of oil will be very helpful. If India uses next two years constructively there is no doubt that Indian economy would deliver a vibrant and an exuberant nation which would surprise the world - and itself.