ECONOMIC REFORMS -

Economic reforms refer to a set of economic policies directed to accelerate the pace of 'growth and development'.

Reasons/Need For Making Economic Reforms

1. Poor Performance of Public Sector:
   - ❖ In the 40 years period (1951-90), public sector was assigned the work for the economic development of India.
   - ❖ However, the overall performance of public enterprise was very disappointing.
2. Deficit in Balance of Payment (BOP):
   - ❖ It arises when foreign payments for imports exceed foreign receipts.
   - ❖ Even after imposing heavy tariffs, there was a sharp rise of imports.
   - ❖ On the other hand, there was a slow growth of exports due to low quality and high prices of Indian goods in the international market.
3. Inflationary Pressures:
   - ❖ There was a consistent rise in the general price level in the economy due to increase in money supply and shortage of essential goods.
   - ❖ As, to control inflation a new set of policies were required.

4. **Fall in foreign exchange reserves:**

   ❖ Foreign exchange reserves fell to the lowest level and it led to the foreign exchange crisis in the country.

   ❖ The government was also not able to repay its borrowings from abroad.

5. **Huge burden of debts:**

   ❖ The expenditure of government was much higher than revenue.

   ❖ As a result, government had to borrow money from banks, public and international financial institutions like IMF etc.

6. **Inefficient Management:**

   ❖ The government was not able to generate sufficient revenues from internal sources such as taxation, running of public sector enterprises, etc.

   ❖ Government expenditure began to exceed its revenue by such large margins that it became unsustainable.

NEW ECONOMIC POLICY

The New Economic Policy (NEP) was announced in July 1991. It consisted of wide range of economic reforms. The main aim of the policy was to create a more competitive environment in the economy and remove the barriers to entry and growth of firms.

The New Economic Policy can be broadly classified into two kinds of measures:

Stabilization Measures: They refer to short- term measures which aim at:

i. Correcting weaknesses of the balance of payments by maintaining sufficient foreign exchange reserves; and

ii. Controlling inflation by keeping the rising rice under control.

Structural Reforms Measures: They refer to long-term measures which aim at:

i. Improving the efficiency of the economy;

and

ii. Increasing International competitiveness by removing the rigidities in various segments of the Indian economy.

- NEP
  - Liberalization
  - Privatization
  - Globalization

Liberalization

Components of NEP

Three broad components of New Economic Policy are:

i. The policy of liberalization (L) in place of licensing (L) for the industries and trade.
ii. The policy of privatization (P) in place of quotas (Q) for the industrialists, and
iii. The policy of globalization (G) in place ofpermits (P) for exports and imports.

Thus, LPG was set to replace LOP in 1991 LPG are the supporting pillars, on which the structure of new economic policy of our Government has been erected and implemented since 1991.

liberalization

- **Liberalization means removal of entry and growth restrictions on the private sector.**
- Liberalization involves deregulation and reduction of government controls and greater autonomy
- (freedom) of private Investment, to make economy more competitive.
- Under Liberalization, business is freely allowed to run on commercial lines.

Purpose of Liberalisation

- It was done to unlock the economic potential of the country by encouraging
- private sector and multinational corporations to invest and expand.
- To Introduce much more competition Into the economy and creating
- incentives for Increasing efficiency of operations.

Economic reform under Liberalization

- 1) Industrial sector reforms
- 2) Financial sector reforms
- 3) Tax reforms
- 4) Foreign exchange reforms
- 5) Trade and investment policy reforms

Industrical sector Reforms:

- ***REDUCTION IN INDUSTRIAL LICENSINGS*** :
- **The new policy abolished industrial licensing for all the project, except for a short list of industries like , liquor, Defence equipment etc.**
- **No license were needed to set up new units or to expand or diversity business.**
- **Only industries related to security and strategic considerations needed licensing.**
- ***DECREASE IN ROLE OF PUBLIC SECTOR:***
- The striking feature was the substantive reduction in the role of the public sector in the future industrial development of the country.
- The number of industryes reserved for the public sector was reduced from 17 to 3 industries L.e. Defence equipment's,
- Atomic energy generation, and
- Railway transport.
- ***De-reservation under small-scale industries:***
- Many goods produced by small scale industries have now been de-reserved.
- The Investment ceiling on plant & machinery for small undertakings enhanced to rupees one crore.
- ***Mestrictive Trade Practices (MRTP) Act:***
- Earlier production capacity was linked with licensing.
- Now, freedom from licensing implied freedom from capacity constraints.
- ***Freedom to Import Capital goods:***
- Liberalization also implied freedom for the industrialists to import capital goods with a view to upgrading their technology,

2) Finanical sector Reforms:

- ***Change in role of RBI:***
- The role of RBI was reduced form regulatory tap facilitator of financial sector.
- ***Origin of principal Banks;***
- The reforms policies led to establishment of private sector banks ,indian as well as foreign .
- ***Increase in limit of foreign investment:***
- The limit of foreign investment in banks was raised to around 51%
- Foreign institutional investors (FII) such as merchant bankers ,mutual funds and pension funds were now allowed to invest in indian financial markets.
- ***Ease in Expansion Process:***
- Banks were given freedom to setup new branches (after fulfillment of certain conditions) without the approval of the RBI.

3) Tax Reforms/fiscal reforms:

Direct Taxes:

- 1. They consist of taxes on Incomes of individual as well as profits of business refer enterprises.
- 2. For example, income tax and corporate tax.
- ***Indirect taxes:***
- 1. This refer to those taxes which affect the Income and property of persons through their consumption expenditure.
- 2. For example, Goods and Services Tax (GST).
- ***The major tax reforms made are:***
- **1. Reduction in Taxes:** Since 1991, there has been a continuous reduction in income and corporate tax as high tax rates were an Important reason for tax evasion.
- ***2. Reform in Indirect taxes***: Considerable reform have been made in Indirect taxes to facilitate establishment of common national market for goods and commodities.
- ***3. Simplification of Process:*** In order to encourage better compliance on the part of taxpayers, many producers have been simplified.

4)Foreign Exchange Reforms :

i. Devaluation of Rupee:

- Devaluation refers to reduction in the value of domestic currency by the government.
- To overcome Balance of Payments crisis, the rupee value was devalued against foreign currencies.

ii. Market Determination of Exchange Rate:

- The government allowed rupee value to be free from its control.
- As a result, market forces of demand and supply determine the exchange value of the Indian rupee in terms of foreign currency.

GST:

The goods and service tax act was passed in the parliament on 29th march, 2017 to simplify and introduced a unified indirect tax system in India. The Act came into effect on 1st July, 2017. This is expected to generate additional revenue for the government, reduce tax evasion and create 'one nation, one tax and one market'

5)Trade and investment policy reorms:

- **The reforms in the trade and investment policy was initiated** -
- To increase the international competitiveness of industrial production.
- To promote foreign investments and technology into the economy.
- **The important trade and investment policy reform include:**

1) Removal of Quantitative restrictions on Imports and Exports: Under new economic policy, quantitative restrictions on imports and exports were greatly reduced.

2) Removal of Export Duties: Export duties were removed to increase the competitive position of Indian goods in the international markets.

3)Reduction in Import Duties: Import duties were reduced to improve the position of domestic goods in the foreign market.

4)Relaxation in Import Licensing System: The Import Licensing was abolished, except in case of hazardous and environmentally sensitive industries.