Neither adjustment nor reform

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Economic Liberalization in India: Analytics, Experience and Lessons by Deepak Nayyar; Calcutta, Orient Longman, 1996, Pages 72, Rs. 70.

"NEITHER adjustment nor reform" is the verdict of Deepak Nayyar after a critical appraisal of the structural adjustment programme and economic reforms initiated in July 1991 and going on since then. The author is Professor of Economics at the Jawaharlal Nehru University, New Delhi and was for some time Chief Economic Adviser to the Government of India. And the appraisal is based on his R.C. Dutt Lectures on Political Economy, the prestigious lecture series organised by the Centre for Studies in Social Sciences, Calcutta. It is one of the rare assessments of the economic reforms that combines economic erudition and inside knowledge of the working of the policy-making apparatus of the country. Those who do not have professional training in economics may find the material rather heavy, but most of what Professor Nayyar has to say should be intelligible to anyone who is willing to invest the time to go through the 60 pages of the lectures, conveniently divided into nine sections.

Nayyar first traces the economic crisis of June 1991 to the cavalier macro-management of the economy in the 1980s that "sought to use the current account deficit in the balance of payments as a means of financing the excess of investment over saving for the economy in general and the excess of expenditure over income for the government in particular." When translated into plain language, it means that the liberalisation policy of the 1980s was an attempt to stimulate economic growth in the country and to finance the deficits of the government on the basis of borrowings from outside. In this sense the crisis was neither sudden nor unexpected. It was man-made and policy-induced. It was not a reflection of the failure of the strategy of development since the mid-1950s as is now being made out by interested parties who are desperately searching for a rationale for the present reforms.

What is being attempted now is again to depend on foreign resources, but on direct foreign investment which is expected to provide non-debt-creating and investment-financing capital flows. Such a strategy is to be preferred to what was attempted in the 1980s, but brings with it at least two sets of problems. The first is that the capital flows may not be of the direct foreign investment kind: on the contrary, in the context of the present phase of international capitalism, the flow may be portfolio capital whose interest is not to augment investment, but to make quick profits, mainly through speculative activities in the stock markets and in dealings in foreign exchange. The second set of problems is that the reliance even on direct foreign investments, if not very carefully monitored and administered, can have adverse consequences on domestic capabilities, particularly in the long-term. What may be a remedy for a short-term crisis may, thus, turn out to be the source of retardation in the long run.

After arriving at these possibilities through the 'analytics' Nayyar concentrates on examining the Indian experience largely with respect to the second set of problems. Section 6 and 7 which deal with this issue deserve special attention. Nayyar faults the fiscal adjustment in the government sector which constitutes the core of the macro-economics of the adjustment on several grounds. No attempt has been made to curb the revenue deficit of the government which has moved up from around 2.6 per cent of GDP in the 1980s to almost 4 per cent of GDP now. On the other hand, the process of fiscal adjustment has created a massive squeeze on public investment, especially in the infrastructural sector where the budget support came down from 1.75 per cent of GDP in 1989-90 to 0.81 per cent in 1993-94. The allocations for the social sectors – education, health, family welfare, water supply, sanitation, housing, urban development, etc. – stagnated in real terms and remained unchanged as a proportion of GDP. The burden of adjustment was borne mainly by the poor. So much for the adjustment.

In terms of the reforms, though the dismantling of the complex regime of controls has certainly been desirable, it was wrong to expect that deregulation, by itself, would reduce monopoly and increase competition in the economy. The Indian experience has been that acquisitions, mergers and takeovers in the industrial sphere have enabled the larger and stronger firms to enlarge their market shares. Trade liberalisation was done on the anticipation that resources would shift from the non-traded goods sector to the traded goods sector, but in the presence of structural rigidities, it is doubtful whether the economy will have the capacity to switch resources adequately in this manner. The reforms in the public sector have been "shallow and superficial," and while the number of industries reserved for the public sector stands reduced, "there has been no systematic review of the portfolio of public investment that might lead to restructuring or rationalisation."

As for the capital markets, "the assumption that market forces, supported by a newly constituted Securities and Exchange Board of India, would suffice to discipline that capital market is somewhat heroic in a situation where, at least so far, trading malpractices abound, disclosure rules are almost non-existent and investor protection is slender."

In the lectures, which are meant primarily to evaluate the reforms, Prof. Nayyar does not offer any alternatives. But he points out that the restructuring of an economy over time has three inter-related components: the management of demand in the short run, the management of incentives to induce supply responses in the medium term and the development of capabilities and institutions in the long term. The crux of the problem is that the three constantly interact, but there is no built-in meachanism to keep them in balance. The balance presupposes certain social objectives which cannot be considered as "given". These objectives are evolved essentially through the political processes and their achievement calls for carefully designed interaction among the variety of social institutions which are the hallmarks of a functioning democracy and the state and the market. To think that economic development is best achieved through any single agency functioning alone – be that the state or the market – is an illusion. Bringing out this fact is the main contribution of Prof. Nayyar's work. ■