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Source: *Economic and Political Weekly*, Vol. 41, No. 19 (May 13-19, 2006), pp. 1885-1890

Published by: Economic and Political Weekly

Stable URL: <https://www.jstor.org/stable/4418209>

Accessed: 11-06-2020 17:32 UTC

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## When Did the 'Hindu' Rate of Growth End?

*A new orthodoxy holds that there is nothing unusual about economic growth after 1991-92, since comparable growth rates were witnessed during the 1980s prior to the 1991 reforms. However, the incipient or first phase of liberalisation began in 1974-75, and not in 1980, as a response to a crisis of enormous proportions in the economy. Treating 1980 as the year that marked the end of the "Hindu" rate of growth is an artefact of the unwarranted homogenisation of the entire history of economic growth prior to that year, and is misleading as to claims about economic liberalisation.*

BALDEV RAJ NAYAR

It has been abundantly clear for some time that the institution of economic reforms through a paradigm shift in economic policy in 1991 was followed by an acceleration of the growth rate (Table 1). Such acceleration thus marked an impressive break with the so-called "Hindu" rate of growth of 3.5 per cent and vindicated in the process the faith of the reformers in the efficacy of reforms. However, a new orthodoxy – following the works of Rodrik and Subramanian (2004), Virmani (2004) and Panagariya (2004) – has, meanwhile, emerged that holds that there is nothing unusual about economic growth after 1991-92 since comparable growth rates were witnessed during the 1980s, prior to the 1991 reforms.

### New Orthodoxy

Rodrik and Subramanian (2004) question the attribution of India's higher growth rates in the 1990s to economic liberalisation, since similar rates were characteristic of the 1980s, when, in their view, there had been little or no liberalisation. Averring that the transition to higher growth started around 1980, long before the initiation of liberalisation, they hold strongly to the view that it was generated by attitudinal change – not policy change

– on the part of the state to a pro-business (in contrast to a pro-liberalisation or pro-market) approach. Consequently, the change "left little paper trail in actual policies but had an important impact on investors' psychology". For them, "this change was inaugurated with the return of a much-chastened Indira Gandhi to political power in the 1980s" and served as "the essential trigger" for the 1980s economic boom [Rodrik and Subramanian 2004: 3-5, 28].

Virmani's (2004) position is somewhat similar, forcefully maintaining that the structural break to a higher growth rate occurred precisely in 1980. Interestingly, he, too, resolves the paradox of "dramatic changes in the growth rate" amidst little or modest reform by resort to social psychology: "The same leader [Indira Gandhi], who had instituted the earlier control policies that slowed the economy, was changing the direction of economic policy. As she was perceived to have learnt from her own experience, the changes were more credible to both potential beneficiaries and losers" [Virmani 2004: 33-41].

Representing a different position, Panagariya (2004) focuses largely on the period after Rajiv Gandhi's accession to power in 1984 and argues that it was reform activism, indeed, that "played a significant role" in the impressive growth performance during several

years prior to the 1991 reforms. Importantly, he holds that the 1980s reforms, because of their demonstrated success, played a foundational role in enacting the 1991 reforms and thus were a "precursor" to the latter. At the same time, in a sweeping assessment that lumps together a vast period but with little systematic specification, Panagariya (2004) differentiates both the 1980s and 1990s reforms from "the isolated and sporadic liberalising actions during 1960s and 1970s, which were often reversed within a short period".

Two propositions clearly stand out in the three studies discussed above. One, that the year 1980 marks a structural break in India's economic growth, with the Hindu rate of growth prevailing before it and the more robust growth coming after it. Even Panagariya – who has methodological reservations about specifying precisely any particular year as the starting point for growth acceleration during the 1980s – agrees nonetheless that "growth rates between the 1980s and 1990s are comparable". Regardless, the year 1980 seems to have gained considerable acceptance as marking the real initiation of improved growth performance. Two, there is the additional belief that the growth acceleration starting in 1980 is related to the return of Indira Gandhi to power in that year with a suddenly changed ideological position, aiming to move away from her earlier socialist rhetoric or policies. This article takes serious issue with both propositions.

### A Revisionist Perspective

It seems that the presumed shift in Indira Gandhi's ideological or policy orientation – invoked by Rodrik and Subramanian (2004) and Virmani (2004) as an explanation for growth acceleration in 1980 – appears as a 'deus ex machina' in their studies. They offer no evidence as to when and, more importantly, why the shift in Indira Gandhi's ideological orientation took place. That shift remains essentially undiscussed and unexplained. Besides, can these studies be taken as definitive on the point that economic reforms in India did not begin until the 1980s? A little recourse to history – which often has little attraction for most

economists – is essential in order to shed light on the question.<sup>1</sup>

## Lurch to the Left

With the twin aims of building socialism and economic independence, India launched in 1956, under the aegis of the Second Five-Year Plan (1956-57/1960-61), a gigantic and ambitious import substitution strategy focused on heavy industry, intended to be established basically in the public sector. The Second Plan, however, ran into trouble right from the start because of the twin capital and foreign exchange constraints, and was rescued only through special resource mobilisation by foreign donors. Subsequently, the Third Plan (1961-62/1965-66), which persisted with the heavy industry strategy, was also headed for trouble, fundamentally because

of the resource constraint and the imbalanced nature of the economic strategy with its relative neglect of agriculture and consumer goods.

Soon tiring of providing vast amounts of aid with no end in sight, the US successfully pressured India into devaluation in 1966 as part of a liberalisation package. That was in one sense the beginning of economic liberalisation in India, but the effort was soon aborted, because its centrepiece, the rupee devaluation, proved to be a veritable disaster. At that moment, Indian politics took a decisively radical turn to the left led by Indira Gandhi, who split the Congress Party in 1969, but remained at the head of the government with the support of the Communist Party of India (CPI) and some regional parties.

Regardless of what precisely her own ideological views were, Indira Gandhi

presided in the next several years over what Nayar has called “the reign of ideology”. The trigger in the party split had been her decision to nationalise all the major banks, bringing under public ownership commercial banking covering over 85 per cent of the country’s deposits. After the split, the government tightened the screws on the private sector, especially big business, through new and stricter constraints. The Monopolies and Restrictive Trade Practices Act, 1969, barred all business houses with assets of more than Rs 200 million from expansion or diversification. The Industrial Licensing Policy was also modified in 1970 to restrict 20 large industrial houses and their individual firms to only “core” industries (new projects worth over Rs 50 million). Thus, those in society who had the most capacity to produce and invest were placed in a straitjacket.

Even after Indira Gandhi won the 1971 elections and the government was no longer beholden to the CPI for parliamentary support, as it had been between 1969 and 1971, socialism remained ascendant. The government continued on the radical path, nationalising the coal industry, general insurance, the copper industry, a significant segment of the steel industry, and a substantial part of the textile industry. Finally, as if in an ideological delirium, the government nationalised the wholesale wheat trade in 1973, aiming eventually to nationalise the entire wholesale foodgrains trade. In addition, through the Foreign Exchange Regulation Act, 1973, it envisaged coercing foreign firms in India to reduce their equity to 40 per cent or withdraw from India altogether.

## Change of Economic Course

What finally brought an end to the nationalisation spree and “the reign of ideology” was a gathering economic crisis in the early 1970s, throwing up challenges to the government on two fronts: soaring inflation amidst widespread scarcities and a sudden and severe deterioration in the balance of payments position. Behind the developing crisis lay multiple causes. Whether or not resulting from the government’s hostility toward and restrictions on big business, manufacturing grew at the rate of less than 4 per cent during the first half of the 1970s, which performance was lower than the already depressed rates of the last half of the 1960s.<sup>2</sup> Meanwhile, droughts in 1972 and 1974 ravaged

**Table 1: GDP Growth Rates 1951-52 To 2004-05**  
(In per cent)

| Year                              | GDP  | Year        | GDP  | Year        | GDP |
|-----------------------------------|------|-------------|------|-------------|-----|
| 1951-52                           | 2.3  | 1975-76     | 9.0  | 1990-91     | 5.6 |
| 1952-53                           | 2.8  | 1976-77     | 1.2  | 1991-92     | 1.3 |
| 1953-54                           | 6.1  | 1977-78     | 7.5  | 1992-93     | 5.1 |
| 1954-55                           | 4.2  | 1978-79     | 5.5  | 1993-94     | 5.9 |
| 1955-56                           | 2.6  | 1979-80     | -5.2 | 1994-95     | 7.3 |
| Average                           | 3.6  | Average     | 3.6  | Average     | 5.0 |
| 1956-57                           | 5.7  | 1980-81     | 7.2  | 1995-96     | 7.3 |
| 1957-58                           | -1.2 | 1981-82     | 6.0  | 1996-97     | 7.8 |
| 1958-59                           | 7.6  | 1982-83     | 3.1  | 1997-98     | 4.8 |
| 1959-60                           | 2.2  | 1983-84     | 7.7  | 1998-99     | 6.5 |
| 4-Year                            | 3.6  | 1984-85     | 4.3  | 1999-00     | 6.1 |
| Average*                          |      | Average     | 5.7  | Average     | 6.5 |
| 1960-61                           | 7.1  | 1985-86     | 4.5  | 2000-01     | 4.4 |
| 1961-62                           | 3.1  | 1986-87     | 4.3  | 2001-02     | 5.8 |
| 1962-63                           | 2.1  | 1987-88     | 3.8  | 2002-03     | 3.8 |
| 1963-64                           | 5.1  | 1988-89     | 10.5 | 2003-04     | 8.5 |
| 1964-65                           | 7.6  | 1989-90     | 6.7  | 2004-05     | 7.5 |
| Average                           | 5.0  | Average     | 6.0  | Average     | 6.0 |
| 1965-66                           | -3.7 | 2005-06     | 8.1  |             |     |
| 1966-67                           | 1.0  |             |      |             |     |
| 1967-68                           | 8.0  |             |      |             |     |
| 1968-69                           | 2.6  |             |      |             |     |
| 1969-70                           | 6.5  |             |      |             |     |
| Average                           | 2.9  |             |      |             |     |
| 1970-71                           | 5.0  |             |      |             |     |
| 1971-72                           | 1.0  |             |      |             |     |
| 1972-73                           | -0.3 |             |      |             |     |
| 1973-74                           | 4.6  |             |      |             |     |
| 1974-75                           | 1.2  |             |      |             |     |
| Average                           | 2.3  |             |      |             |     |
| Other averages for select periods |      |             |      |             |     |
| (a) 1956-57                       |      | (d) 1975-76 |      | (h) 1991-92 |     |
| to 1974-75                        | 3.4  | to 1978-79  | 5.8  | to 2005-06  | 6.0 |
| (b) 1956-57                       |      | (e) 1975-76 |      | (i) 1992-93 |     |
| to 1979-80                        | 3.5  | to 2005-06  | 5.6  | to 2005-06  | 6.4 |
| (c) 1965-66                       |      | (f) 1980-81 |      | (j) 1992-93 |     |
| to 1974-75                        | 2.6  | to 1990-91  | 5.8  | to 1996-97  | 6.7 |
|                                   |      | (g) 1980-81 |      |             |     |
|                                   |      | to 1991-92  | 5.4  |             |     |

*Note:* \*The given four-year period starts with 1956-57 when the second five-year plan, focused on heavy industry and the public sector, was launched.

*Source:* Central Statistical Organisation, *National Accounts Statistics 2005*, Gol, New Delhi, 2005, Statement S-1.2. For 2000-01 and after, Press Information Bureau, Gol, *Press Note*, January 31 and February 7, 2006.

agricultural production, with the average growth rate for the first-half of the 1970s averaging only 1.5 per cent, which was much lower than the population growth rate. The consequence was immense food shortages and a rise in prices. The final coup de grace was delivered by the quadrupling of oil prices by OPEC in 1973.

As a result, the dominant characteristic of the first-half of the 1970s – as earlier in the second-half of the 1960s – was economic stagnation and turmoil. The average GDP growth rate for the former period was an abysmal 2.3 per cent, even lower than the already poor record of 2.9 per cent of the latter period (Table 1). The Hindu growth rate would have, indeed, shone in comparison with such dismal performance. Besides, inflation, which was only 5.6 per cent in 1971-72, rose to 10 per cent the next year, and then soared to 20.2 per cent and 25.2 per cent in the subsequent two years [Joshi and Little 1994:105]. The rising inflation and widespread shortages of essential goods (including food) ravaged the poor, the workers and the middle classes. The massive social discontent resulting from this economic wreckage burst forth into street demonstrations, riots and violence; industrial unrest became widespread. The escalating industrial unrest culminated in an “unprecedented” threat by the two million employees of the government-owned railways to go on strike in May 1974, an action that “promised to destabilise the country” by shutting down the economy altogether [Joshi and Little 1994: 54-55]. Meanwhile, seeking to exploit the social discontent, opposition parties mounted a major offensive against the government and transformed the situation into a political crisis. Economic destabilisation threatened to escalate into political destabilisation.

Late 1973 marked a turning point. The government decided to jettison its earlier radical and populist thrust of imposing restrictions on the private sector and of relentlessly expanding the public sector. It now opted for a growth-oriented approach. Critical to the government’s change of course was its revised assessment about the results of the series of radical policies that it had pursued over the preceding half decade. Indira Gandhi had apparently become disillusioned about the radical course, especially after the fiasco that had followed on the food front in the wake of the government’s takeover of the wholesale wheat trade. Jha (1980:171) refers to “the suspicion that grew in Mrs Gandhi that she

had been made use of by the communists and their fellow travellers in the Congress to pass legislation whose effect was to disrupt production, without making society significantly more egalitarian”. The oil price shocks highlighted for Indira Gandhi and her government the fact that the thrust on insulation from the world economy had not only been futile but also injurious.

In January 1974, the government rescinded its takeover of the wholesale wheat trade, marking the first reversal in the relentless expansion of control by the state over the market. Then it signalled its new economic course by savage action on the labour front in the belief that inflation had already reached intolerable levels and wage concessions were therefore no longer politically acceptable. In May, it ruthlessly crushed the threatened railway strike by large-scale arrests of trade union leaders and workers. Any pretensions to socialism were thus really buried in these quite brutal actions against labour, even if the rhetoric about socialism lingered on. Finally, the government adopted a deflationary policy package in July 1974, which shifted the focus of economic policy from the pursuit of social justice and socialism to economic orthodoxy. There can be no doubt that it was the severe economic crisis of the early 1970s that induced the government to take recourse to economic orthodoxy and to resort to the liberalisation cure, however mild in form. It changed economic course by resorting to a set of more orthodox measures, which constituted a radical departure from the path that it had pursued in recent years. If policy reversal has the potential for enhancing credibility about reform, as Virmani maintains, then it actually took place in 1974. At the heart of the policy shift was the abysmal growth performance over the previous decade and its social and political consequences.

### Incipient Liberalisation

What the government essentially did in the face of the enormous economic crisis was to turn to economic reform, including adopting an economic stabilisation package. The crushing of the railway strike in June 1974 was the opening move in the attack on inflation, in that it prevented demand from escalating further and pre-empted wage demands from labour in other areas of the economy. The government followed up this tough action with equally stern measures in the areas of

taxes, wages and prices. In combination with changes in fiscal and monetary policy, these drastic measures proved extremely efficacious. With prices beginning to fall by October, the cycle of inflation had been broken. The trend continued into the next fiscal year, so that the wholesale price index for 1975-76 was 1 per cent below that for 1974-75.

On the external front, the government obtained no-conditionality or low-conditionality loans from the IMF, with the largest amount coming from the new oil facility. Explicit devaluation was politically unacceptable. But the government really needed no action on this front except to quietly continue with the creeping devaluation that resulted from linking the rupee in late 1971 to a weak sterling, and the value of the rupee fell by 20 per cent between 1971 and 1975. While overt devaluation was avoided, covert devaluation was sustained, with the result that exports (including manufactures) got a boost despite the economic stagnation, industrial slowdown and the gathering economic crisis.

Through the devaluation of the early 1970s, India thus began the long process of reintegration with the world economy. Indeed, the 1970s saw a consistent rise in the economy’s openness ratio (the share of foreign trade in GDP) [Rodrik and Subramanian 2004, Figure 5]. But a new element in international integration also emerged. The oil price hikes opened new markets in west Asia not only in terms of exports but also for Indian manpower. Remittances from Indian workers, another indicator of integration with the world economy, jumped from \$ 97 million in 1972-73 to \$ 470 million in 1975-76 [Joshi and Little 1994:122].

Economic stabilisation does not necessarily equate to economic liberalisation; its key purpose is to restore balance to the macroeconomy. But in this specific instance of the mid-1970s, coming as it did after a sustained bout of radicalism, and the earlier abandonment of the nationalisation of the wholesale wheat trade sent a strong signal of change in economic direction. However, this course change encompassed more than contractionary measures and covert devaluation. In a clear indication of its intent to proceed in a liberal direction, the government established a special cabinet committee in May 1975 for an export-promotion drive and went on to institute a number of measures to promote exports.

First and foremost, the government made a radical departure from its earlier hallmark of imposing restrictions on production in the name of planning and curbing monopolies. In its drive to boost non-traditional exports, the government allowed an automatic increase in production capacity of 25 per cent over five years without requiring prior permission in the case of 15 export-oriented engineering industries. More broadly, to facilitate expanded production for exports, the government shifted to automatic licensing for export-oriented industries to import raw materials and components. To the same end, it increased import entitlements for selected industries. The government also liberalised the provision of finance for the export sector at concessional rates of interest. Further, it increased the cash incentives for exports and expanded such entitlements to industries hitherto not covered, such as engineering, chemicals, synthetic fibres and garments. Importantly, the government took to "selective abolition of export licensing and simplification of procedure. The licensing formalities were dispensed with in regard to nearly two-thirds of the 300 items, which were subject to export licensing earlier." It was not exactly a bonfire of all controls and restrictions, but it marked a significant start for the process of liberalisation [Joshi and Little 1994:122]. One can quibble over whether this set of reforms – and equally that of the early 1980s – constitutes liberalisation or merely attitudinal change. But this much is clear – it marked a reversal of the radical course hitherto pursued. And even an attitudinal change must in a complex and continental-size economy as India's at some point translate into policy changes.

Economic liberalisation is a process. As such, it does not emerge fully evolved suddenly, all at once. Rather, it develops over a period of time and goes through several phases or stages, often marked by fits and starts. In India's case, liberalisation can be regarded as having emerged in the crucible of a crisis of enormous proportions in the economy, which then snowballed into a larger systemic crisis in the form of the declaration of the state of emergency in June 1975. Contrary to Panagariya's (2004) position, that liberalisation episode in its entirety cannot be considered as consisting of ad hoc measures; further, there was no reversal of them. The incipient or first phase of liberalisation can thus be said to have begun in the fiscal year 1974-75 or, for the sake of simplicity,

roughly around 1975, and not in 1980 as some scholars have assumed. The reforms of the 1980s and 1990s can thus be regarded as second and third phases in a longer stretched-out liberalisation process. The fundamental cause in generating the first phase of liberalisation was dissatisfaction with the growth performance under the earlier economic regime over a whole decade from 1965-66 to 1974-75.

### Growth under Incipient Liberalisation

Did the first phase of liberalisation starting in 1975 accelerate the growth rate in the manner that the second and third phases have done? The short answer is, yes!

Economic performance in the first few years after the change of economic course in 1974-75 is remarkably different from that during the entire previous decade. The economic growth rate in 1975-76 was 9 per cent, helped no doubt by revived agriculture following good rains, and by the discipline imposed by the state of emergency. The rates in the subsequent three years were 1.2 per cent, 7.5 per cent and 5.5 per cent. In these four years (1975-76 to 1978-79), the average growth rate was 5.8 per cent (Table 1) – the same or similar to those for the second and third phases. The growth impulses imparted by the change in economic course had thus generated a positive impact on the growth rate. Remarkably, foreign exchange surpluses also accumulated over the period.

However, the fall in the growth rate in 1979-80 or the fifth year to a negative 5.2 per cent requires explanation. Two major external shocks were the chief culprits in this particular performance: an unprecedented drought that resulted in the sharpest post-independence decline of 12.77 per cent in agricultural production<sup>3</sup> and the doubling of oil prices by OPEC. The consequence of these two devastating external shocks was once again high inflation and severe deterioration in the

balance of payments. A direct consequence of the external shocks, the fifth year's performance is simply an aberration, unrepresentative of the pattern of economic growth inaugurated by liberalisation's first phase.

### Should 1980 Still Be Privileged as a Breakpoint?

In view of the above, it is questionable whether 1980 can be genuinely considered to constitute the break from the Hindu rate of growth, as some economists have argued. Indeed, it is precisely the recovery in the agricultural growth rate to 12.89 per cent in 1980, following the drought year of 1979 that gives the illusion of a major boost to growth in 1980-81, and thus lends plausibility to 1980 as the year marking the break. That outcome is, however, simply an artefact of the change in the forces of nature, not a consequence of any attitudinal or policy change. It seems that, persuaded by the prevailing orthodoxy of a generalised Hindu rate of growth of 3.5 per cent, these economists have arbitrarily homogenised the entire period before 1980 in relation to growth. In starting with 1980, and thus ignoring the 1975-76 to 1979-80 period, they may well have been deterred by the figure of 3.6 per cent as the average growth rate for the second-half of the 1970s, which is so uncannily close to the Hindu rate of growth. However, such a position is untenable.

The period before 1980 is not a homogeneous one, and needs to be disaggregated for an adequate analysis. One can ignore the period of the First Five-Year Plan 1951-52 to 1955-56, which did not represent any significant change in economic policy inherited from the colonial era. Following the launching of the socialism-inspired heavy industry strategy in 1956, the growth rate for the four years at the upper end of the 1950s was 3.6 per cent. It accelerated to 5 per cent in the first-half of the 1960s, but it dropped

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drastically thereafter, so that the average for the subsequent decade was about half, at 2.6 per cent (Table 1). In the light of this differentiated picture of pre-1980 growth, the performance of the half-decade of 1975-76 to 1979-80 has to be seen not against a mythic Hindu rate of 3.5 per cent but against the actual performance of the previous decade. Thus considered, this half decade is as much a break from the previous decade as the first half decade of the 1980s is from the assumed Hindu rate of growth.

Even when the fifth year of the second-half of the 1970s is factored into the calculation, the average for that half decade is 56.5 per cent higher than the average of 2.3 per cent for the preceding half decade. This is not very different from the 62.9 per cent increase in the growth rate for the first half decade of the 1980s (5.7 per cent) over the Hindu growth rate. Treating 1980 as marking the end of the Hindu rate of growth is therefore an artefact of the unwarranted homogenisation of the entire history of economic growth prior to 1980, and is misleading as to claims about economic liberalisation. It is 1975, and not 1980, which truly marks the end of the Hindu rate of growth as much as it does the beginning of economic liberalisation in India. This position is confirmed not only by the data provided here on growth rates but also by the data on real gross fixed capital formation [Joshi and Little 1994, Tables 5-16].

Interestingly, in employing "recent developments in time-series econometrics" to the issue precisely of structural breaks in the economy, Jessica Wallack (2003) found 1974 and 1980 to be "the two most robust break" years among four potential break dates. This finding differs somewhat from that of Rodrik and Subramanian (2004) and also from Virmani (2004), but it fits in closely with the analysis advanced here.

### Why the Fixation on 1980?

If this position is correct, then it raises the question as to why the singular fixation on 1980. There are two possible explanations with a considerable degree of plausibility. One is that 1980 is a convenient benchmark, because of the initiation around that time of a larger reform and deregulation movement favouring the market over the state in some powerful countries (the UK under Thatcher and the US under Reagan), and the subsequent development

of the "Washington consensus" at the international financial institutions (IFIs). Before 1980, it is assumed, there prevailed the dark age of no economic reform, while that year marked the dawn of the age of reform. Economic reform elsewhere, including India, then simply represents "policy diffusion". Interestingly, Indira Gandhi returned to power precisely in January 1980.

But such an overall impression of the reform process is misleading. If the analysis presented above is correct, then it is obvious that the policy shift to economic reform in India, coming as it did a half decade before 1980, owed nothing to emulation of a generalised reform movement abroad or to coercion by IMF. Instead, it was rooted in India's own experience with the economic performance of earlier socialist policies. Even the turn to the IMF in 1980 to cope with the external shock from OPEC's oil price hike was based on a homegrown programme rather than one imposed by the IMF [Stiles 1991, chapter 6].

The other possible explanation is that some of the influential writing on liberalisation in India has come from reformers with a background of work in the World Bank and IMF. They have also played roles of one kind or another in the liberalisation process in the 1980s and 1990s. Arvind Virmani is one example; others are Shankar Acharya, Montek Singh Ahluwalia, and Raja Chelliah. These and other reformers have justifiable pride in the part they played in India's economic reforms, though their role was largely technical in nature, and not one of policy determination. Understandably, the mental horizon of these economists may have remained focused on the post-1980 era of reforms in which the IFIs have had a significant role.

Some critics have even argued that the entry of such reformers into India's economic bureaucracy was part of a conscious design on the part of the World Bank to move the Indian state to a reformist track [Sengupta 2004]. The significant aspect, however, is that these IFI-background officials entered India's economic bureaucracy in the 1980s when economic reform had already achieved some salience. After the confusing Janata Party interregnum (1977-79), the reform process of the time, particularly in the light of Indira Gandhi's dramatic return to power in mid-January 1980, seemed like a new beginning in India's economic history. It may have

seemed credibly so since Indira Gandhi inherited an economy in a shambles, with high inflation (near 20 per cent) and a looming balance of payments crisis. The year 1980 may have also seemed an appropriate watershed since India soon entered into negotiations with the IMF and, in 1981, obtained what was until then the largest loan in IMF history, undoubtedly with some reform conditionalities. Thus, it would not be unreasonable for those present at what appears to be the birth of reform to take 1980 as marking a break in India's economic policy.

But if the story narrated earlier about the first phase of liberalisation is correct, then this is a mistaken view. The shift, both in terms of economic policy and accelerated growth began in 1975, and not in 1980. While the confusion in Janata Party's economic policy is deserving of notice, it is significant that two important committees set up by its government advocated further liberalisation – the P C Alexander committee and the D R Dagli Committee. The early 1980s thus represented continuity with the policies of 1974-75 and after, not a break with them. That continuity derived from the success of those earlier policies. It is difficult therefore to agree with the proposition that Indira Gandhi changed economic course in 1980 because she had been "chastened" by her absence from power. The change had occurred earlier in 1974-75, motivated by considerations precisely of improving economic performance, not mere power.

When Indira Gandhi returned to power in 1980, she had already shed her socialist colleagues and her socialist ideology, though she continued to employ socialist rhetoric to mask her liberalisation policy. One of the first noteworthy economic policy actions of her government was the issuance of the Industrial Policy Statement in July 1980 in order to adjust the Industrial Policy Resolution of 1956 to new circumstances. Continuing the economic liberalisation inaugurated in the midst of the economic crisis in 1974-75, the new policy extended the permission for automatic expansion of capacity by 25 per cent over five years to a much larger number of industries.<sup>4</sup> It further adopted a more liberal stance toward the import by industry of raw materials, spare parts and, especially, technology. Significantly, the number of foreign collaborations approved annually suddenly more than doubled. These various reforms were consolidated in the Sixth Five-Year

Plan.<sup>5</sup> Interestingly, when India went in for the IMF loan in 1980, it pre-empted the application of conditionalities to it on the plea of having already accomplished the necessary reforms on its own [Stiles 1991:114-15, 121, 122].

A more dramatic shift in industrial policy took place in 1982, which incorporated two new measures. One extended the principle of automatic expansion of licensed industrial capacity so as to permit expansion by one-third, rather than just one-fourth as before. The other enlarged the list of “core” industries that would be open to large industrial houses and foreign companies.<sup>6</sup> Again, the government allowed the private sector to enter new areas of industrial activity, such as power and oil exploration, that were earlier closed to it.<sup>7</sup> Further, the government abolished administered prices for pig iron and brought about the partial decontrol of cement.<sup>8</sup> Significantly, Indira Gandhi appointed two important committees whose recommendations would have a considerable impact on subsequent policies on licensing controls and trade liberalisation.

In the light of the foregoing evidence, it is patent that all this was no “liberalisation by stealth”. The new policies were part of the record, inside and outside Parliament, and were the object of public criticism and attack. It is equally obvious that the shift to favouring economic liberalisation, having taken place over the period from 1974 to 1980, had occurred prior to the government’s recruitment of IFI-background economists. Consequently, the induction of such economists into India’s economic bureaucracy was not the cause of the shift of opinion in the government in favour of liberalisation but the consequence of it.

The shift in intellectual opinion in favour of liberalisation at the top, that seems evident with Indira Gandhi’s return to power in 1980 underlines another aspect of the reform process. Panagariya had pointed out that the success of the reforms of the 1980s had been played out, by building confidence among the politicians, which played a foundational role in the subsequent reforms in 1991. But what would then explain this risk-taking by the pushing of economic reforms in the 1980s? It would seem that it is precisely the experience of success with the reforms of 1974-75, which had been worked out in the context of a desperate economic crisis, that lay at the base of the expansionary, rather than contractionary,

adjustment to the economic crisis of the early 1980s.

## Conclusions

At the broader theoretical level, this case study of India’s experience with economic liberalisation testifies to the robustness of the proposition of reform advocates that liberalisation makes for acceleration in the rate of economic growth. This is certainly true of the phase of liberalisation marked by the paradigm shift in economic policy in 1991. But it is equally true, as more recent work by economists has shown, of the within-system economic policy reforms of the 1980s.

More distinctively, the present case study has demonstrated that economic liberalisation should be more accurately seen as beginning in 1974-75 (rather than in 1991 or 1980), when the government headed by Indira Gandhi changed economic course. That government did so under the compulsions of an enormous economic crisis arising out of external shocks and the failure of earlier ideology-inspired economic policies. Sufficient and compelling evidence has been provided on this point. It is therefore difficult to agree with the proposition that only in 1980 Indira Gandhi “realigned herself politically with the organised private sector and dropped her previous rhetoric” about “socialism and pro-poor policies” [Rodrik and Subramanian 2004:4]. In reality, as argued here, the change began much earlier – in 1974-75. Indira Gandhi’s last phase at the head of the government from 1980 to 1984 marks no new departure, but truly represents continuity in economic policy with the reforms of 1974-75. Interestingly, in dividing India’s planning experience into various phases, the eminent economist, P N Dhar, who was Indira Gandhi’s principal advisor and chief of staff during the 1970s, treats the third phase “1973-74 to 1984-85” as all of a piece as regards economic policy [Dhar 2003, chapter 1].

As a consequence, the issue of the credibility of reforms of the 1980s has to be seen in a different light. Virmani had attributed the patent success of the period’s rather modest reforms, in considerable part, to their sharper credibility because Indira Gandhi had learnt her lesson from the consequences of her previous mistakes. If she “learnt from her own experience” indeed, she did so in 1974-75, and the credibility of her later reforms derived from her actions at that earlier time, and

the successful experience of economic actors with those actions. Similarly, the success of the liberalisation policies undertaken in 1974-75 enables us to understand why Indira Gandhi continued with similar policies on returning to power in 1980. Verily, it is 1975, and not 1980, that constitutes a break in both economic policy and economic growth. [27]

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## Notes

- 1 The historical parts of the account below rely on Joshi and Little (1994) and Nayar (1989).
- 2 See Central Statistical Organisation, *National Accounts Statistics – Back Series 1950-51 to 1992-93*, Statement 5, <http://mosp.nic.in>.
- 3 World Development Indicators (WDI) Online.
- 4 Industry minister Charanjit Chanana in *Lok Sabha Debates* (July 23, 1980), pp 367-82.
- 5 *Sixth Five-Year Plan 1980-85*, Planning Commission, GoI, New Delhi, 1981, Chs 1 and 16.
- 6 Industry minister N D Tiwari, in *Lok Sabha Debates*, April 21, 1982, pp 484-85; and *Economic Survey 1982-83*, Ministry of Finance, 1983’, p 30, GoI, New Delhi.
- 7 *Times of India*, New Delhi, August 19, 1982.
- 8 *Economic Survey 1982-83*, pp 25-30.

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