UNIT 165 – UPSC - New Industrial Policy of the Government: liberalization, deregulation and privatisation

The Industrial Policy specifies the relevant roles of the public, private, joint and co-operative sectors; small, medium and large scale industries. It emphasises the national significances and the financial development strategy. It also explains the Government's policy towards industries, their establishment, functioning, progress and management; foreign capital and technology, labour policy, and tariff policy. The Industrial Policy of India has determined the pattern of financial and industrial development of the economy. The Industrial Policy revealed the socio-economic and political philosophy of development (Gupta, 1995).

Main objectives of New Economic Policy -1991

The main objectives to launch new economic policy (NEP) in 1991 are as follows:
The main objective was to plunge Indian economy in to the field of 'Globalization and to give it a new drive on market orientation.
The new economic policy intended to reduce the rate of inflation and to remove imbalances in payment.
It intended to move towards higher economic growth rate and to build sufficient foreign exchange reserves.
New economic policy aimed to accomplish economic stabilization and to convert the economic policies in to a market economy by removing all kinds of unnecessary restrictions.
New economic policy wanted to permit the international flow of goods, services, capital, human resources and technology, without many restrictions.
In the mid-1991, the government has made some drastic changes in its policies bearing on trade, foreign investment exchange rate, and industry, fiscal of fairs. The various elements constitute an economic policy. It has been documented in literature that economic development ultimately depends on industrialization. Industrial policy is meant for all those principles, rules, regulations

and procedures concerning the rate of growth, ownership, location pattern, and function of industrial undertakings in the country in a way to industrialization. Before independence, India had no policy for industrialization. In 1947, after independence, India has changed the scenario. The industrial policy was announced by government of India in 1948 and Industries act 1951 was passed to give a material shape to this policy. This policy was changed in 1956 to give a concrete policy. It was further altered to give shape to the mixed economy and ideology of socialist pattern of society. The political party, Janta Dal had modified the policy in 1977 (Pathak, 2007). Due to change in government, policy was again revised in 1980. The national front government brought some changes in its industrial policy in 1990. In the decade of 1990s, the government of India decided to deviate from its previous economic policies and learn towards privatization in order to come out from the economic crisis. In July 1991 when the devaluation of Indian currency took place and the government started announcing its new economic polices one after another (Gupta, 1995). Though these polices pertained to different aspects of the economic field, they had common some factors. The economic element was to orient the Indian system towards the world market. Government launched its new economic policy which has three important features such as Liberalization, Privatization and Globalization. Liberalization of the economy means to free if from direct or physical control imposed by the government. Economic changes were based on the assumption that market forces could guide the economy in a more effective manner than government (Pathak, 2007).

New Economic Policies: Liberalization, deregulation, Privatization

In 20th century, there has been a wave of economic policy transformations in the developing world, with one country after another taking the liberalization cure, often imposed by the international financial institutions. This wave of reform had been preceded by a quarter century of state directed effort at economic development, during which time the goals of economic self-reliance and import substitution industrialization were the trademarks of development strategies in developing countries. These goals seemed particularly justified, given the long experience of these countries with colonialism and the agricultural nature of their economies. However, all this seemed to be overtaken by the successive flow of liberalization (Gupta, 1995).

Liberalization:

Liberalization is vital element of contemporary economic policies in India and other part of world, based upon the idea that removing restrictions on domestic economic activity as well as on the trade relations with other countries that has a beneficial impact on the economy. Liberalisation is the procedure of release the economy from the dominion of excessive bureaucratic and other restrictions imposed by the State. The phrase "liberalization" infers economic liberalization. Economic liberalization constitutes one of the basic elements of the new Economic policy (NEP) which the Indian Government launched in the middle of the year 1991. Other significant aspects of the policy are Privatization of the public sector, Globalization and market friendly state. The main trust of the new economic policy is "liberalization". The principle of this policy is that greater freedom is to be given to the businessperson of any industry, trade or business and that governmental control on the same be reduced to the minimum (Gupta, 1995). The purpose of the liberalisation was to dismantle the excessive control framework that reduced the freedom of enterprise over the years, the country had developed a system of licence permit raj'. The aim of the new economic policy was to save the businesspersons from unnecessary harassment of seeking permission from Babudom (the bureaucracy of the country) to start an undertaking. The main drive of the process to economic liberalization is to set business free and

to run on commercial lines. The underlying conviction is that commerce and business are not matter to contain to fixed national boundaries. Unnecessary government restrictions which hamper economic and commercial activities and flow of goods and services must be removed. The liberalization aims to liberalize commerce and business and trade from the clutches of controls and difficulties.
The concept of Liberalization: There is acceleration economic policy reform in the developing world in current period which is visualized as significant consequence of a changed world economic system. Main feature of the changed world economy is the moderate of the heightened economic Globalization which provides new external challenges as well as opportunities for growth (Gupta, 1995). In management literature, to 'Liberalize' means remove or loosen restrictions on an economic or political system. Generally, Liberalization) refers to removal or relaxation of restrictions imposed by the previous government usually in areas of economic or social/Industrial policy. The economic liberalization in India refers to the current reforms in India. Liberalization is implemented for encouraging growth of private sector, simplification of policy, regulation, tax structure, facilitating Foreign Direct Investment, restructuring public sector for efficiencies, providing incentives for exports and allowing more imports, put emphasis on modernization of plants and equipment through liberalized imports of capital goods and technology, expose the Indian industry to competition by gradually reducing the import restrictions and tariffs, moving away from protection of small scale industries (Sivadasan, 2007).

Main features of the policy of liberalisation: There are numerous features of liberalization.

1. Lessened Government control and freelance to private Enterprises.
2. Capital Markets opened for private Entrepreneurs.
3. Simplification of licensing policy.
4. Opportunity to purchase foreign exchange at market prices.
5. Right to take independent decisions regarding the market.
6. Better opportunity for completion
7. Widened liberty in the field of business and trade

Evaluation of Liberalization:
In Indian viewpoint, it is very difficult to establish that the process of economic liberalization taken up by the government of India in 1990's has really brought huge economic gains to India. The process has brought some benefits through suffers from some deficiencies.
The Gains: The liberalization process has aided the free movement of goods and services that has led to better industrial performances. Industrial organizations have now become more effective and market responsive. Country's exports are on the increase. Sectors such as information technology and computer software registered incredible advancement.
The Deficiencies: Liberalization process has its insufficiencies also. The economic reforms including liberalization were introduced all of a sudden and proper background was not created to take their full advantage and to face their consequences.
Liberalization in India: The Government of India began the economic liberalization policy in 1991. Even though the power at the centre has changed, the speed of the reforms has never loosened till date. The sector accounted for just one-fifth of the total economic activity within the country. The sectorial structure of the industry has changed, although gradually. Most of the industrial sector was dominated by a select band of family-based conglomerates that had been dominant

historically. Post 1991, a major restructuring took place with the emergence of more technologically advanced segments among industrial companies. Currently, more small and medium scale enterprises contribute considerably to the economy. The important characteristics of the new policy may be explained under the four categories such as liberalization; Privatization of the public sector, Globalization and market friendly state. Liberalization is the freedom for the entrepreneur. The new policy permits foreign direct investment to a large extent and in huge number of industries than earlier.

In the middle of 1990, the private capital had surpassed the public capital. The management system had moved from the traditional family based system to a system of qualified and professional managers. One of the most significant effects of the liberalization period has been the emergence of a strong, wealthy and flexible middle class with significant purchasing powers and this has been the instrument that has driven the economy since. Another major advantage of the liberalization period has been the shift in the pattern of exports from traditional items such as clothes, tea and spices to automobiles, steel, IT. The "made in India" brand, which did not evoke any sort of loyalty has now become a brand name by itself and is now recognised around the world for its quality. The reforms have transformed the education sector with a huge talent group of qualified specialists which are available to share their knowledge and competence.

With the New Industrial Policy' 1991, the Indian Government intended to integrate the country's economy with the world economy, improving the efficiency and productivity of the public sector. To accomplish this objective, existing government regulations and restrictions on industry were removed. The major aspects of liberalization in India were as follows.

1. Abolition of licensing: New Industrial Policy'1991 abolished licensing for most industries except 6 industries of strategic significance. They include alcohol, cigarettes, industrial explosives, defence products, drugs and pharmaceuticals, hazardous chemicals and certain others reserved for the public sector. This would boost to setup of new industries and shift focus to productive activities.

2. Liberalization of Foreign Investment: Earlier prior approval was essential by foreign companies, but in present, situation automatic approvals were given for Foreign Direct Investment to flow into the country. A list of high-priority and investment-intensive industries were delicensed and could invite up to 100% FDI including sectors such as hotel and tourism, infrastructure, software development etc. Use of foreign brand name or trade mark was permitted for sale of goods.

3. Relaxation of Locational Restrictions: There was no requirement to get approval from the Central Government for setting up industries anywhere in the country except those specified under compulsory licensing or in cities with population exceeding1 million. Polluting industries were required to be located 25 kms away from the city peripheries if the city population was greater than 1 million.

4. Liberalization of Foreign Technology imports: For business projects in which imported capital goods are required, automatic license would be given for foreign technology imports up to 2 million US dollars. No permissions would be required for hiring foreign technicians and foreign testing of indigenously developed technologies.

5. Phased Manufacturing Programmes: Under PMP, any enterprise had to progressively substitute imported inputs, components with domestically produced inputs under local content policy. However new industrial policy'1991 abolished PMP for all industrial enterprises. Foreign Investment Promotion Board (FIPB) was set up to speed up approval for foreign investment proposals.

6. Public Sector Reforms: There was more autonomy to the Public Sector Units through the Memorandum of Understanding restricting interference of the government officials and allowing their management's greater freedom in decision-making.
7. MRTP Act: The Industrial Policy 1991 modernised the Monopolies and Restrictive Trade Practises Act. Regulations relating to concentration of economic power, pre-entry restrictions for setting up new enterprises, expansion of existing businesses, mergers and acquisitions have been abolished.

It has been observed that India, in the period of economic reforms, is at the intersection. On one side, India is gaining economic wealth and credit, but on other side, social inequality is developed. Currently, as India is one of the fastest growing economies in the world, the social aspects have been ridden roughshod by the economic benefits. What has been conveniently forgotten or suppressed till date have been the disparities, mainly the socio-economic issues. This has led to growing dissatisfaction among the population. The rift between the rich and the poor has increased so enormously that the rich are just getting richer and the poor are just becoming poorer. The actual benefits of the economic reforms have infrequently infiltrated to the lowest sections of society.

In the agricultural, there is also unequal growth, as it is a field that has been left high and dry in the chase of agricultural reforms. The sector has been opened up to the multi-nationals, without having evolved a comprehensive shelter for farmers, most of who are poor and own very little land of their own. Small scale industries have been virtually overlooked. Most of the industries have closed down in the last few years due to tough competition from multi nationals who have unparalleled financial and political power. Various schemes must be systematically scrutinized and efforts must be made to understand that the rewards must reach everyone.

Impact of Liberalization on Indian Economy:

1. Increase in Employment.
2. Arrival of New Technology or Development of Technology.
3. Development of Infrastructure.
4. Identity at World Level.
5. Increase Our Currency Value (INR).
6. GDP Growth.
7. Increase Consumption and Adaptation of New Lifestyle.
8. Increment in Competition.
9. Increment in Foreign Investor.

It is well recognised in management literature that liberalization entails elimination of state control over economic activities. It implies greater sovereignty to the business enterprises in decision-making and removal of government interference. It was believed that the market forces of demand and supply would automatically operate to bring about greater efficiency and the economy would recover. This was to be done internally by introducing reforms in the real and financial sectors of the economy and externally by relaxing state control on foreign investments and trade.

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Deregulation: Deregulation is heated issue for many government bureaucrats and giant businesses. Since last many decades, huge number of economies, both in developed and developing countries have deregulated their banking systems.

Concept of deregulation: Management studies have demonstrated that Deregulation is the procedure to eliminate or reduce state regulations. Every industry has definite rules and regulations that must follow. These rules are created by industry associations and regulators, as well as the government. Adekanye (2002) stated that the deregulation policy was adopted in 1987 against a crash in the international oil market and the reactant deteriorating economic condition in the country due to stringent policies in the financial sector. Adekanye indicated that the policy was adopted to achieve fiscal balance and balance of payment availability as well as liberation of the financial system by altering and restructuring the production and consumption pattern of the economy, eliminating price distortions, reducing the heavy dependency on crude oil export and consumer goods importation, enhancing the non-exports base and achieving sustainable growth. Deregulation occurs when the government pulls back from the industry a bit, therefore loosening its grip on particular rules and regulations. Many research reports envisages that deregulation will lead to more firms and less obligatory power (Alesina et al. 2005), increases in average firm size and profits through reductions in capacity restrictions (Campbell and Hopenhayn 2005), increased dispersion in sales, assets, and profits (Syverson 2004), and increased turnover and firm-age distributions tilting toward younger firms (Asplund and Nocke 2006).

It has been explained in several management reports that deregulation is a fact where governments leave the market economy to the market forces and not stifle it and constrain it with numerous laws, rules, and regulations. Deregulation entails managing and supervising the economy in a manner that would largely be a hands off approach combined with oversight over its functioning related to legal and compliance aspects alone. Alternatively, deregulation means that the governments do not obstruct with the businesses in a day-to-day manner and act only when specific objections against businesses are brought before them. Most models of deregulation undertake that firms are able to proficiently assign resources within the firm and that factor markets are frictionless. Panagariya (2008) recorded that remnants of industrial regulation still impact the operation of Indian firms and may restrain their flexibility in adjusting to new economic circumstances. Deregulation also means that governments do not fix prices or put in motion price controls leaving the process of determining the optimal pricing to the market forces of demand and supply. Deregulation is a trend in emerging markets or the developing countries ever since the 1990s when these markets began to globalize their economies and open them up to foreign competition as well as liberalize their economies internally so that domestic firms are able to compete freely without the heavy hand of the state.

The purpose of deregulation is to permit a particular industry to raise greater competition, create a freer marketplace and expectantly enhance economic growth both within that marketplace and in general. When industries become deregulated, it gives industry's actors greater scope in which to improve their products, craft their brand and, ultimately, appeal more to customers.

Financial deregulation in India began in 1992, following the Indian economic crunch of 1991, and it is a vital element of the ongoing process of economic and structural transformation. In the Indian context, two forces can affect firm profits and determine the total impact of deregulation on firm size and profitability. First, free entry can lead to a rearrangement of factor resources from less efficient domestic firms to more efficient firms, such that revenue and size distributions become

left truncated. Second, fast economic development can lead to an increase in market size, precipitating a rightward shift in the revenue distribution for the surviving domestic firms.

Advantages: When deregulation works, there are several advantages: Deregulation offers the consumer in the form of lower prices, more providers and better products. A company that was not performing well and maintained only a small market share before deregulation would also be likely to benefit from this act. When the company faces fewer restrictions, it might be able to explore opportunities that the government had previously not allowed or severely restricted. The businesses are left to themselves to determine their operational processes and strategic imperatives without the government interfering in their working. This means that they can launch new products, fix prices according to demand and supply, expand into newer regions, acquire land and other fixed assets without having to take a thousand permissions, and finally, the businesses interact and interface with the customers directly without the state setting the agenda or the action plan. Deregulation in an emergent market economy also means that the state is at last giving full play to market forces as opposed to centralized planning those results in greater efficiencies for the businesses and more profits as well. This is the reason why many businesses welcome deregulation with open supports and encourage the governments to deregulate more sectors so that the private companies would have the chance to bring in efficacies and actualize synergies leading to a win-win situation for both the businesses and the consumers. Another benefit of deregulation is that businesses can focus on their core competencies without having to submit themselves to constant scrutiny and constant pressure from the government.
Disadvantages: It has been stated in management reports that when firms perform well on its own despite government regulations, it would definitely realise deregulation as an obstacle, as it will make the rules negligent for its competitors. It can be said that a successful company might view deregulation as a way to allow the competition to play by fewer rules in order to give it a fairer shot. This easing of rules can also lead to a breakdown within the entire industry as different companies use this flexibility to their advantage though it can ultimately end up being to their drawback. Deregulation impacts those at the bottom of the economic ladder most as without the protective hand of the state; they might left at the mercy of the profits first businesses, who care more for their profits rather than social and environmental responsibility.
It is said that Deregulation is a procedure in which the government reduces industry restrictions for smooth operation of business. The government removes a regulation when businesses complain it interferes too much with their ability to compete, especially with foreign companies. Deregulation to the economy will bring about a high level of competitiveness, therefore higher productivity, more efficiency and lower price of overall goods and services. Deregulation policy was designed to restructure and diversify the productivity of the economy in order to reduce dependency on the oil sector and also to achieve fiscal and balance of payment viability. Additionally, it lays basis for sustainable non-inflationary or minimal inflationary growth rate.

Privatization: Privatization is strongly related with the phenomena of globalization and liberalization. Management scholars described Privatization as the transfer of control of ownership of economic resources from the public sector to the private sector. It means a decline in the role of the public sector as there is a shift in the property rights from the state to private ownership. Privatization is a managerial approach that has fascinated the interest of many groups of people, academicians, politicians, government employee companies of the private sector and public. It is

observed that the public sector has several issues, since planning, such as low efficiency and profitability, mounting losses, excessive political interference, lack of autonomy, labour problems and delays in completion of projects. In order to overcome these issues, new industrial policy'1991, initiated the process of privatization into the Indian economy.
Another term for privatization is Disinvestment. The objectives of disinvestment were to raise resources through sale of PSUs to be directed towards social welfare expenditures, raising efficiency of PSUs through increased competition, increasing consumer satisfaction with better quality of goods and services, upgrading technology and most importantly removing political intervention.

Concept of privatization: According to Steve H. Hanke, Privatization is the process whereby the public operations are transferred to the private sector. Barbara Lee and John Nellis define the notion of privatization as the general process of involving the private sector in the ownership or operation of a state-owned enterprise. There this phrase to private purchase of all or part of a company. It cover "contractedly out" and the privatization of management through management contracts leases or franchise arrangements. Privatization refers to any process that reduces the involvement of the state, public sector in economic activities of a nation.
Main objective of privatization:
The process of Privatization has been generated with the main intention of improving industrial efficiency and to assist the inflow of foreign investments.
It also wants to make the public sector undertakings strong, able efficient companies. It recommends a change in the role of the government from that of the "owner manager" to that of a mere "controller" or regular'
It also has aim to ensure proficient utilization of all types of resources including human resources. Privatization insists on the government to concentrate on the area such as education administration and infrastructure and to give up the responsibility of looking after business and running industries. It is expected to strengthen the capital market by following appropriate trade policies.

Privatization can be of three prominent types:
1. Delegation: Government keeps hold of responsibility and private enterprise handles fully or partly the delivery of product and services.
2. Divestment: Government surrenders the responsibility.
3. Displacement: The private enterprise expands and gradually displaces the government entity.

Privatization in India:
In India, Privatization has been acknowledged with a lot of confrontation and has been dormant initially during the initiation of economic Liberalization in the country. Privatization is also one of the aspects of the new economic policy which came to take shape in the decade 1990. In India, massive Privatization was done in the decade of 1980s when Rajiv Gandhi assumed office as the Prime minister of India. The issue of Privatization in India has to be understood in the context of the relative incompetence of the public sector industries, lack of financial resources, defective competition system, and continuous labour problem.
When India became independent, it embarked upon planned economic development. In order to increase the economic development, it gave more importance to the public-sector on which the Government had its control. The Industrial Policy Resolution of 1956 also gave importance to the public sector industries. The growth of the public sector assume importance in the Indian

economy. It contributed to employment opportunities, capital formation, development of infrastructure, and increase in exports over the years, and many other areas. But it failed in certain respects such as to generate adequate surpluses to support sustained growth. The public sector was also a failure in obtaining consistent revenues, fulfilling labour demands and interests, encouraging industrial researches, reducing the cost of the production, achieving technical expertise, and in successfully facing the competition at the hand of the private sector. Gradually, a new industrial policy started taking its shape. The principle of this policy is marketed forces must be allowed to play their role in shaping the economy.
The main aspects of privatization in India are as follows:
1. Autonomy to Public sector: There was more sovereignty to selected PSUs referred to as 'Maharatnas'(CIL, ONGC, NTPC, SAIL & IOL) and 'Navaratnas'(BEL, HPCL, BPCL, BHEL, GAIL etc.) to take their own decisions.
2. De-reservation of Public Sector: The number of industries reserved for the public sector were reduced in a phased manner from 17 to 8 and then to only 3 including Railways, Atomic energy, Specified minerals. This offers opportunities for more areas of investment for the private sector and increased competition for the public sector forcing greater accountability and efficiency.
3. Disinvestment Policies: Till 1999-2000 disinvestment was done basically through sale of minority shares but since then the government has undertaken strategic sale of its equity to the private sector handing over complete management control such as in the case of VSNL and BALCO.

Advantages of privatization: 1. Efficiency, Absences of political interference, Quality service, Systematic marketing Use of freedom technology.
2. Accountability.
3. Innovation.
4. Research and development.
5. Infrastructure.

Arguments in favour of privatization:
1. Privatization is necessary to revitalize the state owned enterprises.
2. Privatization is necessary to face global competition.
3. Privatization is needed to create more employment opportunities in future.
4. Helpful for mobilizing and investing resources.
5. Recognition of talents and good performance of work.

Argument against privatization:
1. Profitability alone should not become the sole yardstick to measure efficiency
2. Role of public sector undertaking from the socio-economic angle also cannot be overlooked.
3. Protection of the interests of the weaker section.
4. Price fixing policy here is not profit oriented.
5. Argument that the private sector is more efficient than the public sector is not right.

Though privatization offers some advantages to companies such as increased efficiency, it has an adverse impact on the employee morale and creates fear of dislocation or termination. Private sector focuses more on profit maximization and less on social objectives unlike public sector that initiates socially viable adjustments in case of emergencies and criticalities (Lokyo, S., 2012).
There is lack of transparency in private sector and stakeholders do not get the complete information about the functionality of the enterprise (Ahmad, 2011). Privatization has provided

the excessive support to the corruption and illegitimate ways of accomplishments of licenses and business deals amongst the government and private bidders. Lobbying and corruption are the common issues tarnishing the practical applicability of privatization (Ahmad, 2011).
Privatization loses the task with which the enterprise was established and profit maximization agenda boosts misconducts like production of lower quality products, elevating the hidden indirect costs, price escalation etc. (Lokyo, S., 2012).
Privatization results in high employee turnover and a lot of investment is required to train the lesser-qualified staff and even making the existing manpower of PSU abreast with the latest business practices (Lokyo, S., 2012).
There can be a clash of interest amongst stakeholders and the management of the buyer private company and initial confrontation to change can impede the performance of the enterprise (Ahmad, 2011).
Privatization heightens price rise in general as privatized enterprises do not enjoy government subsidies after the deal and the burden of this inflation affects the common man.
To summarize, it can be reviewed that economy of country depends on industrialization. Industrial policy is meant for all those principles, rules, regulations, and procedures concerning the rate of growth, the ownership, location pattern, and functions of industrial undertaking in the country in way to industrialization.
Deregulation, competitive efficiency and globalization are three major factors of new industrial policy. It is well established that Indian economy is a vibrant economy that exhibit remarkable potential of growth. Globalization, liberalization and privatization are major strategic mandates for economic policies. Market oriented reforms are sustainable and are gaining acceptance with resistance to privatization going down due to the benefits like improved efficiency through target oriented management and disposition of public funds into social and physical infrastructure of the nation.