CHAPTER 5

INDIA

Table 5.0

India : Selected Macro-economic Indicators

Population (mln. persons 1983)	: 733.2
Area (thousand sq.km.)	: 3288.0
Per Capita income (GNP)	
US$ (1983)	: 260.0
Indian Rs. (1983)	: 2625.7
GDP Growth (average annual rate %)	
1965 - 73	: 2.8
1973 - 83	: 4.0

GDP by kind of Activity (%)

	Agri	Ind.	(Mfg.)	Service
1965	47	22	15	31
1982	11	26	15	38

GDP by type of expenditure (%)

	Govt. constr-ution	Pvt. const-rution	I	(Savings)	Expenditure	(Importations)
1965	10	74	18	16	4	6
1982	11	67	25	22	6	10

Estimated parameters

MPC	: 0.70
MPS	: 0.30
ICOR	: 5.36
MPX	
a) with respect to GDP	: 0.09
b) with respect to world income	: 0.00007 a
MPM	
a) with respect to GDP	: -0.06 a
b) with respect to world income	: 0.45
consumption elasticity with respect to GDP	: 0.86
elasticity of exports with respect to GDP	: 1.80
elasticity of imports with respect to GDP	: 0.95

MPC = Marginal Propensity to Consume
MPS = Marginal Propensity to Save
ICOR = Incremental Capital-Output Ratio
MPX = Marginal Propensity to Export
MPM = Marginal Propensity to Import

Source : Same as Table 5.4

Overview

If, in the 1950s, one had been given the privilage to predict a Third World country having the most likelihood of embarking on an industrial revolution and with the best prospects of fostering economic growth in the modern era, the consensus, surely would have been India. A large domestic market, a relatively diversified natural resource base, quite elastic supplies of skilled and semiskilled labour, a polity apparantly committed to development, a relatively efficient bureaucracy and almost no shortage of domestic entrepreneurship it had an impressive list of potentials. Yet, despite having such high credentials to its name, India has disappointed-both in terms of absolute level of industrialization as well as its contribution to per capita growth. India's overall economic performance has been better since its indepedence in 1947 than before, but particularly worse than most other countries, especially in the 1960s. India's GNP per capita growth was merely 1.4 percent a year between 1960 and 1978. Apart from creating a highly diversified industrial base, facilitated to a great extent by the aforementioned factors, it's overall economic performance, when compared to similar developing nations, has been dismal more so when compared with the experience of the East Asian 'Gang of Four'-Hongkong, Singapore,Republic of Korea and Taiwan -or even the semi-industrialized and other newly industrialized economies like Brazil, Argentina, Mexico, Yogoslavia and such. Table 5.1 presents an at-a-glance view of their economic performance in a comparative framework.

Economic growth : Selected NICs and SICs (Average annual Percentage growth rate)

	Argentina	Brazil	India	Korea	Mexico	Singapore	Taiwan
Value Added in Agriculture							
1953-60	0.5	4.0	2.5	2.3	5.7	n.a	3.9
1960-66	3.2	3.8	-0.5	5.8	4.7	2.5	5.3
1966-73	0.7	5.9	3.0	3.2	2.4	3.1	3.8
Manufacturing							
1953-60	5.8	10.1	4.8	13.6	8.5	n.a	10.1
1960-66	5.3	4.5	6.2	13.0	9.7	10.3	12.3
1966-73	7.3	11.8	4.7	21.0	7.6	15.0	22.0
Gross National Product							
1953-60	3.2	6.3	3.5	5.6	6.5	n.a	6.9
1960-66	3.6	4.1	2.8	7.3	7.1	7.3	9.4
1966-73	4.8	9.3	3.8	10.7	6.4	12.7	10.7
Per Capita GNP							
1953-60	1.2	3.4	1.6	3.0	2.8	n.a	3.2
1960-66	2.1	1.1	0.5	4.5	3.7	4.5	6.2
1966-73	3.3	6.4	1.5	8.8	2.9	10.9	7.9
Population							
1953-60	2.0	2.9	1.9	2.7	2.9	4.8	3.6
1960-66	1.5	2.9	2.3	2.7	3.4	2.8	3.2
1966-73	1.5	2.9	2.3	1.9	3.4	1.8	2.8

Source : Balassa, B. and Associates (1982)

Along the way towards development, somewhere, India faltered and backtracked. The isolationist stand that it chose to adopt on the lines of proponents of a more inward-looking development, chiefly Nurkse and Prebisch, resulted in its relative failure to industrialize compared with the relative ease with which the East Asian countries succeeded in transforming their agricultural economies into modern industrial ones. The aim of this chapter is to focus mainly on the influence of external forces which have and a significant bearing on India's economic performance over a period of four decades since the initiation of its development process as a distinctive identity in its own right. But before that, a brief review of its overall economic performance, both in a historical as well as modern perspective, would prove helpful in understanding better the process of development.

5.1 ECONOMIC GROWTH IN A HISTORICAL AND MODERN PERSPECTIVE

Historically, India Has been one of the pioneers of Third World industrialisation with already a century of industrial expansion and growth of entrepreneurship behind it. The tradition of economic growth, entrepreneurship and industrialization which modern India inherited was quite impressive by contemporary standards. This certainly made easier the task of Indian planners considerably enabling them to start building on a semi-industrialised base which was already endowed with entrepreneurial activity. India could thus have planned further industrialization by exploiting these advantages. However over time, one obvious set of policies became evident that set apart the performance of India and the NICs and that was the inward-looking approach characterized by protectionism which actually predates Independence. The difference lied in the success of Republic of Korea, Singapore and Taiwan in switching trade policies in the mid-1960s whereas India, despite belated and half-hearted attempts, failed to liberalize and in turn transform its agrarian economy into an industrial one on the lines of the East Asian NICs. Unllike policymakers in the NICs who where determined to switch policies that did not work, those in India tenaciously held on to policies which through experience were proved dysfunctional.

The Indian experience with industrialization in the decades sinces since 1947 has been a subject of mixed reactions which have regressed from great optimism to exaggerated despair. Its performance has been in some ways remarkable, in most ways disppointing. In its individual respect, among its notable achievements, India can boast of an impressive and a generally steady growth rate of GNP at about 4 percent p.a. over virtually the first three five-year plants. For the decade 1955-65, the growth rate was 4.5 percent on an annual average at current prices. Table 5.2 indicates the national income estimates in a historical perspective. The estimates show that over the period of 1900-47 per capita income rose from Rs. 52.2 to Rs. 62.2 which was an increment of barely 20 percent in nearly five decades - a proof of the negligible impact on the overall growth of the economy of a century of industrialization during the British rule.

The period since 1951 witnessed an altogether new phase in economic development. The government decided to undertake to

Table 5.2

(Undivided) India's Absolute and Per Capita National Income : 1900/1-1946/47

	National Income (Rs. million)	Per Capita Rs.
1900/1-1904/5	15,022	52.2
1905/6-1909/10	15,753	53.0
1910/11-1914/15	17,300	57.0
1915/16-1919/20	17,662	57.9
1920/1-1924/5	18,442	59.3
1925/6-1929/30	20,498	62.9
1930/1-1934/5	21,306	61.6
1935/6-1939/40	22,498	60.6
1940/1-1944/5	24,407	61.6
1942/3-1946/7	25,243	62.2

Source : Bhagwati, J. and Desai, Padma (1970).

regulate and accelerate progress in a planned framework within which decisiions relating to trade, level of foreign aid, level of investment expenditure and such growth-related policy variables were taken. It was then that the overall strategy of inward-oriented development was adopted; chiefly and more importantly, so the argument goes, to rehabilitate an economy squeezed by the drain of enormous wealth by years of British colonial rule and devastated by the Partition.

In the modern period, India's verall economic performance has been impressive in many respects, albeit inadequate to its evergrowing needs. The rate of growth of national income has significantly and substantially increased over its historical trend. The per capita income growth, though not as marked as that of national income, has been distinct. Table 5.3 A & B shows that national income grew at an annual average rate of 3.5 percent (at constant prices) during the First Five-year plan, 4.0 percent during the Second plan and 2.9 percent during the Third plan. Per capita income growth was an annual average rate of 1.6 and 1.8 percent in the first two plans and almost same as the previous plan in the first four years of the Third plan. An obvious fact becomes clear that population growth has eroded the growth rate of income. Thus, India's overall performance, in terms of absolute and per capita incomes during the three plans is on the whole quite significant though, in view of its exteremely low level of initial income and standards of living, it is inadequate. Moreover, it represents a distinct improvement over the performance in the previous historical period of five decades. As noted by K.N. Raj, "the rate of economic growth that

Table 5.3

A. National income, absolute and per Capita, at constant prices : 1948-67.

	Conventional estimates of net national Product (at 1948/9 prices). (Rs. Crores)	Conventional estimates of Per capita net national product (at 1948/9 prices) (Rs.)
1948/9	8,650	249.6
1949/50	8,820	250.6
1950/1	8,850	247.5
1951/2	9,100	250.3
1952/3	9,460	255.7
1953/4	10,030	266.2
1954/5	10,280	267.8
1955/6	10,480	267.8
1956/7	11,000	275.6
1957/8	10,890	267.3
1958/9	11,650	280.1
1959/60	11,860	279.2
1960/1	12,730	293.3
1961/2	13,060	294.0
1962/3	13,310	291.9
1963/4	13,970	299.2
1964/5	15,000	313.7
1965/6	14,660	299.4
1966/7	14,950	298.8

B. Annual growth rates of national income, absolute and per capita, by each plan.

	Net national Product(NNP)	Per capita NNP
First Plan	3.5	1.6
Second Plan	4.0	1.8
Third Plan	2.9	0.4

Source : Same as Table 5.2

has been achieved in India since 1950-51 is 2 to 3 times as high as the rate recorded earlier under British administration. As a result, the percentage increase in national income in the last thirteen years has been higher than the percentage increase realized in India over the entire preceding half a century"[1].

After about a decade and a half of planned development since its initiation in 1950, the general idea that emerged regarding the policy stance adopted by India was that firstly, for the entire period of over a decade 1951-63, import substitution in the investment group seemed to predominate. Secondly, for the 1951-57 period, broadly coinciding with the First plan, there was relatively substantial import substitution in consumer goods followed by capital and intermediates group and finally, for the 1957-63 period, approximatey with the beginning of the Second plan, emphasis was shifted to heavy industries. Import substitution in consumer goods was lowest and substantially higher in capital and intermediate group with capital goods usually dominating.

After 1966, beginning with the June 1966 devaluation of the Rupee, there was a new wave of liberaization. But, as it shall be argued, the attepts were half-hearted and the conceptual policy was not altogether clear. This cost India very highly in terms of growth. The period of over a decade after the devaluation, was a period of what could be termed a 'dark decade' in the history of Indian economic development. It was only in the late 1970s around

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1. op.cit., in Bhagwati J.N. and Desai P.(1970) "India:Planning for Industrialisation",OECD,Oxford Uni.Press,London,Pg 65.

1978, that liberalization in the real sense was adopted as the key to enhaced growth and development. It was specifically during the period thereafter that India managed to create an industrial base and achieve a technological maturity that was perhaps even greater than that of S.Korea and Brazil. This is particularly evident in the amount of R & D that Indian firms did in 1980 especially the machine tools, equipment for processindustries and electrical equipment. A recent study has shown that Indian firms spent more on R & D in absolute terms as well as percentage of output and that India's percentage were several times those of korea except in the machine tool sector where Korea spent 4.2 percentage of sales and India, 3.4 percentage of output. At the same time another study shows that though Brazilian manufactured exports were three times those of India in 1980, the latter's exports of technology were much larger than those of the former. It is in this sense that India's IS policy is argued to have been exceptionaly successful since it has led to the creation of an impressive indigenous technological capacity[2].

Within such a broad framework, the chapter proceeds to analyse the Indian performance on the external front, especially regarding foreign trade and foreign capital. It is pertinent to note that the performance has to be viewed not from individual standards but in the international context, relative to the performance of other countries of the same genre.

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2. Chenery, H. and Srinivasan, T.N. (1989)-"Handbook of Development Economics", Vol II North Holland, Amsterdam, Pp 1633.

5.2 FOREIGN TRADE & TRADE POLICIES - Their Contribution to Indian Economic Growth :

When India began its development process around the same time as the NICs, it also chose to adopt a strictly inward-oriented stretegy of heavy protection to domestic industries. It involved essentially the operation of a tight import regime of restrictions which became especially pronounced after the 1956-57 exchange crisis. Import controls in India which remained essentially qualitative (non-tariff) actually date back to the Second World War. They were imposed first in 1940, beginning with mainly consumer goods, extended gradually and covered virtually all imports by 1942. The aim of the policy was basically to conserve foreign exchange which was scarce, thus imposing direct control over foreign exchange utilization. In the subsequent years, the controls experienced a change-over from qualitative to quantitative licensing. Of the many objectives of the country's development policy which remain dominant influences even today include reducing external dependencethrough import substitution in products and technologies and curtailing and regulating the role of foreign companies. The pursuit of these objectives led to the creation of a set of inward-looking policy tools, the main ones being control over access to capital, domestic and foreign, control on DFI in India, control over foreign exchange payments and control over a large proportion of imports and exports via licensing. There were occasional periods of 'liberalizations', which were marked by interim periods of increasing restrictions whenever the balance-of-payments situation became tight as was the case during 1949. The First-Five-Year plan period, 1951-55, was generally one of progressive liberalization, more so towards the terminal years. Although the mechansim for import and exchange control went through many structural changes, it remained intact upto the beginning of the 1956-66 decade. Till then, the government sought intermittently to reduce reliance on the import control system by using the tariff meahcnism. During the second half of 1954, the tariff structure underwent significant changes. Nonetheless, Indian tariffs have remained much higher than in other industrializing nations with large internal markets and diversified industrial structure (see Table 5.4). The import policy that was prevalent at the time ruled out foreign competition because of the 'indigeneous availability' criterion : as long as an item was domestically produced it was automatcially protected from import-conpetition, no matter how much its cost of production exeeded the c.i.f price. If the item was, nonetheless, to be imported, the buyer had to provide conclusive evidence that he could not obtain the item from indigenous producers. The policy was at its zenith around 1965 when it began to be liberalized gradually with major changes following the devaluation of the Rupee in 1966.

The foreign exchange crisis occurred in the beginning of the Second Plan undermined the increasingly liberal measures and the willingness to use tariff policy to mitigate the pressure on quantitative restrictions. As a result the import control regime became tigher. The continuing balance-of-payments difficulties and plans for rapid industrialization through the following decades also influenced the thinking behind such

Table 5.4

Trade and Import Policy Regimes (Selected Asian Economies)

Country	Trade[a] X % GDP	Trade[a] M % GDP	Trade[a] Bal. $Mln	Average Tariff rates (%)	Import Policy Indicators[b]: NTB frequency rates (%) Lic.	Quotas	Prohibitions	STMS
Central South Asia								
China	9.4	17.3	783	NC	NC	NC	NC	NC
Bangladesh	5.7	17.3	-1441	74.7	17.7	0.8	-	3.4
India	4.5	7.1	-4971	71.5	17.5	12.5	-	6.3
Pakistan	8.7	15.2	-2252	80.6	40.0	2.4	-	2.6
Sri Lanka	20.8	37.9	-872	41.2	18.7	-	-	9.8
South-East Asia								
Indonesia	24.2	18.2	5214	30.9	6.8	1.2	8.7	1.8
Malaysia	50.8	47.5	900	10.4	5.9	-	3.9	-
Phillippines	12.4	20.2	-3086	29.9	4.1	18.9	0.7	6.4
Singapore	131.5	169.6	-6325	00.5	8.2	-	0.6	-
Thailand	15.7	25.4	-3919	25.9	6.8	-	4.3	-
East Asia								
Hong Kong	68.8	75.2	-2059	NC	NC	NC	NC	NC
Korea,Rep.	30.4	32.6	-1747	32.9	26.7	-	-	-
Taiwan	50.3	40.7	4781	NC	NC	NC	NC	NC

Note : a - data refer to 1983
b - NTB = Non-Tariff Barriers.
STMS = State Trading Monoplies.

Source : Asian Development Bank (1990).

tightness of the policy. The liberalization measures that followed the devaluation and became prominent around mid-1970s provided improved access to foreign capital borrowing, imported technology and imported capital goods.

5.2.1 Export Policy and Performance :

The import control system that was adopted in the early 50s was such that it tended to discriminate against exports. The effective export exchange rate on the average was inevitable less than the effective import exchange rate. One of the important aftereffects of the principle of indigenous availability was that the exportable items, as a rule,had to rely on inferior-quality domestically produced inputs which, in turn created increasing difficulties for capital equipment inthe highly competitive international markets. This was especially true of new exports which as it is were at a grave disadvantage in cultivating foreign markets almost from scratch. Secondly, until as late as the end of 1964, the whole industrial licensing and import policy was unfavourable to manufactured exports mainly because of their substantial inward-looking bias. Thus, when India began its development, exports were a neglected sector. Whatever attention was ultimately given, beginning with the later part of the Third Plan, was insufficient. In fact, Prof. Mahalanobis opted for an import-substitution growth model for the IInd plan in view of the general decline in India's terms of trade. He implicitly assumed a closed economy with a sitution of stagnant export earnings through inelastic export demand. This automatically led to the proposition that an increasing share of investment would require an increase in the domestic production of capital goods which comprise the investment. As a result, the export policy, over the period, evolved from indifference, pessimism, positive discouragement to growing encouragment via increasing subs idization.

The period from 1950 to the 1966 Devaluation :

India's export performance during the first three Plan periods is quite succintly made obvious in Table 5.5. As the table indicates, a significant feature of India's exports has been the preciptious decline in its share in world exports since independence continuing practically for about a decade and a half. India's exports exports grew relatively slowly form 1953 to 1965. In a comparative framework. India's export performance still lags behind some of the Asian economies.

Table 5.6 shows India's growth of exports in relation to the NICs. As seen in the table, it was the very rapid growth in manufactured exports that explains the successful export performance of the NICs whereas India experienced low rates of growth for its exports both primary as well as manufactured. An important reason for such a dismal performance has been its undortunate commodity composition. The principal export commodities-jute, tea, cotton textiles, tabacoo and vegetable oilseeds and oil-exhibited not simply a dismal earnings growth rate but also a falling share in the world market. The inelastic-world-demand bottleneck for these commodities also played a significant role in India not being able to expand its export earnings. The picture of India's export performance is filled out further by the estimates of the behaviour of export volumes and

Table 5.5

India's exports and Share in World exports,1947-66

(1)	World exports (US $ million) (2)	Indian exports (US $ million) (3)	(3) as a % of (2) (4)
1947	48,549	1,234	2.5
1948	54,058	1,371	2.5
1949	55,102	1,288	2.3
1950	57,110	1,146	2.0
1951	77,140	1,611	2.1
1952	74,170	1,295	1.7
1953	74,930	1,116	1.5
1954	77,670	1,182	1.5
1955	84,550	1,276	1.5
1956	93,880	1,300	1.4
1957	100,880	1,379	1.4
1958	96,080	1,221	1.3
1959	101,780	1,304	1.3
1960	113,200	1,333	1.2
1961	118,700	1,396	1.2
1962	124,700	1,403	1.1
1963	136,000	1,631	1.2
1964	152,600	1,749	1.1
1965	165,500	1,686	1.0
1966	181,300	1,606	0.9

Source : Same as Table 5.2

Table 5.6

Growth of exports, 1953-65
(Index numbers of value in 1965, 1953 = 100)

Exporter	Primary	Manufactures	Total exports
Argentina	134	117	113
Brazil	95	529	104
Mexico	177	430	196
Hong Kong	28	443	311
India	149	150	149
Pakistan	78	3.820	120
Philippines	186	280	193
Taiwan	186	3.214	352
All developing countries	165	283	174
World	168	291	220

Source : Little, I., Scitovsky, T. and Scott, M. (1970).

prices contained in Table 5.7. As the estimates strongly indicate, the First Plan period showed onthe average an improvement over the previous three years' average export performance. This was largely achieved due to the enormous price-gain during the two Korean boom years, 1951 and 1952. On the other hand, the average export volume showed a continuous mild improvement through these years. As against this, the Second Plan period experienced stagnent average prices and volume.

The overall low growth of exports during the period is automatically explained by the domestic policies towards exports followed by India. From 1948-50 to 1958-60, there was very little positive encouragement given to exports and much was done to discourage them. Following the balance-of-payments crisis of 1956-57-imports having rose much faster than anticipated-the level of protection to the home market was stepped up. With the introduction of stringent controls, imports conse qently fell. Moreover, the policies towards exports comprised of export controls and quotas, export taxes and other policies whose effect preempted exportables for domestic consumption. Of course, the growing strength of domestic demand accentuated the problem. In general the period, especially 1956-61, witnessed the imposition and consolidation of the quantitative restriction (QR) regime.

In contrast, around 1961, in the Third plan, with more attention devoted to the balance of payments and export promotion policies entered a second phase characterised by partial and halting efforts at liberalization. Export subsidization was steadily and strongly undertaken in order to reduce the degree and consequences of the exchange rate overluation. In many ways,

Table 5.7

Export Earnings, Volume and Price indices, 1950-66 (1958=100)

Year	Value of Indian exports(US $ Mln.)	Export Value index	Export Price index	Export Vol. index
1950	1,146	93.86	98	95.78
1951	1,611	131.94	143	92.27
1952	1,295	106.06	117	90.65
1953	1,116	91.40	100	91.40
1954	1,182	96.81	102	94.91
1955	1,276	104.50	100	104.50
1956	1,300	106.47	101	105.42
1957	1,379	112.94	101	111.82
1958	1,221	100.00	100	100.00
1959	1,304	106.80	100	106.80
1960	1,333	109.17	109	100.16
1961	1,396	114.33	111	103.00
1962	1,403	114.91	106	108.41
1963	1,631	133.58	106	126.02
1964	1,749	143.24	106	135.13
1965	1,686	138.08	112	123.29
1966	1,606	131.53	111	118.50

Source : Same as Table 5.2

the period from 1962 to 1966 was one of increasing attempts to reduce the adverse impact of the earlier phase of QR-regime. Owing to serious attempts at encouraging exports, manufactured exports, which had increased by only about 13 percent from 1953 to 1960, thereby increased by about 35 percent in value from 1960 to 1965. In fact,both imports and exports reached the targetted levels-13 & 20 percent respectively-but it was found that this was consistent only with a much slower growth in output than expected. Going by the performance of the Third Plan (Table 5.7), the average export performance appears to have picked up significantly above that of the Second Plan, both in value and volume though as a percentage of World Trade, there was no improvement and in fact, some deterioration (Table 5.5). However, the improvement was confined to the first three years of the Plan after which it tapered off to stagnancy. Moreover, though the improvement was considerbable by Indian standards it was unspectacular when compared with the experiance of other countries. An important contributing factor to such performance, besides the complex export policies and overall environment of controls and regulations was that erroneously, the emphasis on export promotion in India was on encouragement of non-traditional exports at the cost of neglect of those commodities which accounted for majority of its export earnings. The new exports which were sought to be encouraged, were difficult to market abroad. Exports of some products like bicycles, automobilies and parts, diesel engines, though increased remained small.

The export subsidization policies mentioned above took two major forms : (a) fiscal measures which included mainly outright subsidies and tax concessions and exemp tions among others and (b) import entitlement schemes which entitled exporters to premium - carrying import licenses. These measures sought to improve the direct profitability of export sales. Besides these, there were other promotional activities by the government like budgetary appropriations for market development which indirectly raised the profitability of sales in foreign markets. Over a period of time, however, the import entitlement scheme became the principal instrument of export promotion. The import licences, which the eligible exporters received, fetched high import premia as per the rate of the value of effective exports. From 1962-63 onwards, import duties also began to be used more frequently to mop up the import premia and add to national revenue. As regards the effective exchange rates, system, during the few months prior to the June 1966 devaluation, the system reached a stage of de facto, though adhoc and partial, devaluation with significant elements of a flexible exchange-rate policy.

These schemes were definitely instrumental in sustaining the spurt in India's export performance during the Third Plan. They were, however, not without drawbacks. In fact they suffered from numerous defects, a major being, as mentioned earlier, the creation of a complex system of policies and controls and the misguided encouragement of non-traditional exports. Nonetheless, they did manage to drive home an important fact-that export earnings could be increased by making exports profitable. They, in fact, served to remove the widespread elasiticity pessimism that had permeated earlier thinking and policies and thus managed to get India's export performance off the hook constituted by an overvalued exchange rate.

Against the background of such partial shifts towards a more rational trade and exchange-rate policy alongwith a still substantial carry-over of the inefficient package of import and export policies, the June 1966 devaluation was announced.

The Period from 1966 to late 1970s :

The devaluation of 1966 in response to the overvalued exchange rate that made exports unprofitable in relation to domestic sales, was perhaps the most important and significant turning point towards a greater and m ore sophisticated reliance on the market mechanism. In a way, the shift had begun well before the actual devalution via partial liberalization which ultimately culminated in this major move. However, as it shall be seen, this shift towards economic liberalism fell short of restructing the system and enhancing the economic performance of India.

Simulataneously, with the devalution, there were radical changes in the import licencing policies which became much more liberal. It was realized that there was no alternative to imports if the country wanted to achieve speedy development.The import liberalization measures introduced by the government granted almost total freedom to selected industries to import their raw materials and components although restrictions on sources and the necessity to secure licences were continued. In general the import liberalization was limited in scope to a great extent since the principle of indigenous availability described earlier continued to plague the administration of the licensing system. This was partly the outcome of recession in industrial investment and output that occured during the same period of import liberalization and devaluation. It proved impossibleto dismantle the protection given to industries through import controls at such a time when effective demand for output in several industries was lacking. Thus, in the real sense, the import liberalizatin was ill-timed. Moreover, industrialists who had been conditioned to the comfortable situation of a totally sheltered market could not be expected to switch over to a system which involved international competition and competitiveness however efficient it might be projected to be. In a way, the thinking was still conditioned by the planning philosophy of the earlier period ; that anything which could be produced and supplied from domestic capacity must antomatically be precluded from imports.

An important aspect of the devaluation of the Rupee from Rs. 4.76 to Rs. 7.50 per dollar, by 36.5 percent, was it was accompanied by a significant reduction in import duties and the elimination of the import entitlement schemes. Thus, the net devaluation was much smaller.

With the end of the Third Plan, a new era started, Instead of concentrating on only imports, attending to exports was also considered to be important. It became imperative to increase exports in order to finance the increassing volume of imports and to the extent that import demand could be satisfied. The liberalization measures were thus the outcome of planned efforts at making the situation more conducive to exports. However,in the zeal to encourage exports to a greaer extent, several new export promotion schemes began to be introduced with increasing government interference which contradicted the notion of trade on a freer basis. Once again over time, the policies, began to look inward-oriented in terms of such interference in trade rather than making it absolutely free. The basic problem of the shift in policy emphasis to offset biases against exports was the 'indigenous availability' criterion which prevented exporters from freely importing intermediate inputs. Within such complexity of the system, efforts to increase exports intensified year after year.

Table 5.8 A & B presents two different estimates of India's export performance in the post-devaluation period. The devaluation of 1966 did have some effect on exports. As a refult, by the end of the Fifth Plan, India managed to increase its exports to a sizeable figure from $ 1812.99 million to $6183.77 million-an increase of over threefold (Table 5.8A). However, to conclude that the post-devaluation liberalization measures were responsible for such an apparantly positive development would prove nothing short of fallacious. By whatever estimates, if one observes India's exports in the global context, the most striking feature is the decline in its share of world exports (Table 5.8A & B). As both the tables indicate, the declining trend of India's share of exports in the world continued till 1974. Between 1974 and 1977, there was a brief reversal, whereupon the decline continued. The share in 1979 was the lowest that India had over obtained.

Table 5.8

A. India's Exports and Share in World exports : 1966-77
(All figures US $ million).

Year	India's Exports	World Exports	India's exports as percentage of world exports
1966	1812.99	190200	0.95
1967	1590.40	198900	0.80
1968	1805.59	221100	0.82
1969	1878.19	253200	0.74
1970	2137.53	290600	0.74
1971	2143.71	325200	0.66
1972	2595.47	387900	0.67
1973	3258.85	537700	0.61
1974	4108.86	797500	0.52
1975	4826.89	822400	0.59
1976	5743.30	933500	0.62
1977	6183.77	1058800	0.58

B. India's share of World exports, 1948-1979 (Millions of US $)

Export	1948	1960	1970	1974	1977	1979
India's Exports(A)	1386	1331	2026	3930	6378	6702
World Exports(B)	57189	128275	313860	840779	1127247	1627030
A/B (Percentage)	2.42	1.13	0.65	0.47	0.57	0.41

Source A. International Financial Statistics Yearbook, 1980, IMF.

B. Martin, Wolf (1982).

After 1973, the world economy as a whole entered a more sluggish phase following the prolonged boom that preceded. In such an environment, India's export performance was naturally affected. An indication of this is give in Table 5.9 which compares the growth of total exports of India with nine other developing economies. Between 1972 and 1978, India's export level slipped from fourth to eight rank among these economies and its growth rate ninth, ahead only to Yugoslavia. However, the peak in India's export growth between 1974 and 1976 was a result of sharp declines in those of developing economies as much as of India's own growth. Between 1976 and 1978, India's export growth was again relatively poor. Moreover, the levelling of the exchange rate also contributed to the slow growth of exports. It is worth nothing here that in 1975-76 and 1976-77 in an environment of a favourable and bouyant world trade , India's export growth needed exploitation of particular unique opportunities such as market research and exploration of potential foreign demand , consultancy on total management and establishing global contacts with potential export markets. This in turn required action by the government, failing which , stagnation tended to result. More important than the analysis of the growth pattern itself is a comparison with India's competitors. For this one needs only to focus on manufacturing which has been the most dynamic sector for developing country exports and includes many of India's most rapidly growing exports. Table 5.10 presents an oerall picture of manufactured exports of India and certain major developing economies from 1965 to 1978. During this period India slipped

Table 5.9

Value and Growth of Total Exports of Selected Developing Economies, 1972 to 1978

Developing economy	Value (US $ million)				Growth rate (percent)			
	1972	1974	1976	1978	1972-74	1974-76	1976-78	1972-78
Argentina	1,941(7)	3,931(7)	3,912(9)	6,394(7)	42.3(4)	-0.2(10)	27.8(2)	22.0(6)
Brazil	3,991(1)	7,951(1)	10,128(1)	12,659(2)	41.1(5)	12.9(6)	11.8(8)	21.2(7)
Hong Kong	3,476(2)	5,907(2)	8,522(2)	11,499(4)	30.4(7)	20.1(3)	16.2(7)	22.1(5)
India	2,415(4)	3,906(8)	5,339(6)	6,167(8)	27.2(9)	16.9(4)	7.5(10)	16.9(9)
Korea, Republic of	1,624(10)	4,460(5)	7,715(4)	12,695(1)	65.7(1)	31.5(1)	28.3(1)	40.9(1)
Malaysia	1,722(9)	4,234(6)	5,295(7)	7,413(6)	56.8(3)	11.8(7)	18.3(6)	27.5(4)
Mexico	1,845(8)	2,957(10)	3,468(10)	5,438(10)	26.6(10)	8.3(8)	25.2(3)	19.7(8)
Singapore	2,181(6)	5,785(3)	6,586(5)	10,134(5)	62.9(2)	6.7(9)	24.0(5)	29.2(2)
Taiwan	2,916(3)	5,518(4)	8,155(3)	12,624(3)	37.6(6)	21.6(2)	24.4(4)	27.7(3)
Yugoslavia	2,237(5)	3,805(9)	4,896(8)	5,668(9)	30.4(7)	13.4(5)	7.6(9)	16.8(10)

Note : Figures in parentheses indicate ranks
Source : Same as Table 5.8B.

Table 5.10

Manufactured Exports of Selected Developing Economies, 1965 to 1978
(millions of US Dollars)

Developing economy	1965	1970	1974	1976	1978	1965-78 Compound growth (% a year)
Argentina	83.9(9)	247,9(9)	963.2(9)	975,5(9)	1,687.9(9)	26.0(4)
Brazil	124.3(7)	368.2(8)	1,920.7(7)	2,332.4(7)	4,212.2(5)	31.1(3)
Hong Kong	989.9(1)	2,329.1(1)	5,444.6(1)	7,859.2(1)	10,610.2(3)	20.0(7)
India	783.9(2)	1,051.2(3)	2,031.2(6)	2,802.7(6)	2,713.3(7)	12.7(10)
Korea,Republic of	103.8(8)	640.4(5)	3,775.5(3)	6,746.8(3)	11,248.7(1)	43.3(1)
Malaysia	69.9(10)	151.(10)	547.4(10)	798.5(10)	1,395.8(10)	25.9(5)
Mexico	164.1(6)	391.3(7)	1,218.2(8)	1,010.1(8)	1,701.4(8)	19.7(8)
Singapore	300.5(4)	427.6(6)	2,316.8(5)	2,920.2(2)	4,534.4(4)	23.2(6)
Taiwan	186.2(5)	1,139.7(2)	4,630.4(2)	6,921.0(2)	10,838.4(2)	36.7(2)
Yugoslavia	616.7(3)	1,001.4(4)	2,524.4(4)	3,382.5(4)	4,036.4(6)	15.5(9)

Note : Figures in parentheses indicate ranks.
Source : Same Table 5.8B

form second largest to seventh in the group. Between 1965 and 1978 its share in the total manufactured exports of developing economies fell from 14 to 5 percent.

Following the foreign exchange crisis of 1973-74, the government took a number of steps not only to manage it, but also to end it. Import controls were progressively loosened and exports received a marked increase in encouragement, through incentive as well as exchange-rate policy. In a way the foreign exchange crisis was successfully sought to be managed by a combination of export growth and import substitution though in a way the form of liberalization changed to some extent towards export promotion. Foreign aid also facilitated the policies which is discussed later in a separate section.

What actually happened was quite contrary to expectations. Since there was little rationalization in policy changes there were a multiplicity of individual policy interventions which resulted in wide variance in effective incentives. It was a path of liberalization which had every chance not merely of increasing economic inefficiency, but also to reduce protection to what India considered highest priority sectors. The basic aim of the import control policy was obviously to save foreign exchange. The best was to achieve this, as seen by the government, was to exclude both nonessential goods as well as goods that India could produce itself. Thus, the trade regime provided particularly strong protection to goods whose imports were considered nonessential, thereby increasing the incentive to domestic producers of such goods-essentially the final consumption goods including luxuries like cars, air conditioners, refrigerators. At the same time, the basic aim of industrial planning was to promote what were thought to be essential industires, capital goods, chemicals and fertilizers,steel and the like and the liberalization was focused on imports of such goods. As a result naturally the incentive to produce these goods fell. Owing to such paradox, variances in incentives began to grow and economic efficiency declined.

Another major threat was caused by failure to liberalize rapidly enough when exports and other sources of foreign exchange grew which served to thwart the export drive. This led to the reabsorption of exports exports into the domestic economy. Once again a significant and central feature of the policy regieme was the retention of the 'historical' principle of 'indigenous availability'.

Thus, in an overall perspective, the liberalization measures adopted by the government during the period as a move toward an outward-looking regime were only hesitantly begun and lacked long-term perspective. Partly, as a result, exports ceased to grow rapidly when the domestic economy picked up and input constraints began to be felt. The approach taken by India after 1973, viz, to increase exports and other sources of foreign exchange and then to liberalize seemed to be only a short-term potentially fruitful technique. If the opportunity to move beyond piece-meal liberalization toward a more radical change in trade strategy were not taken, there was every danger that India would not merely remain fixed at the far-from-satisfactory half-way stage but would ultimately regress to the traditional position of being constrained by the foreign-exchange bottleneck and thereby relapse into the earlier phase of the QR-regime.

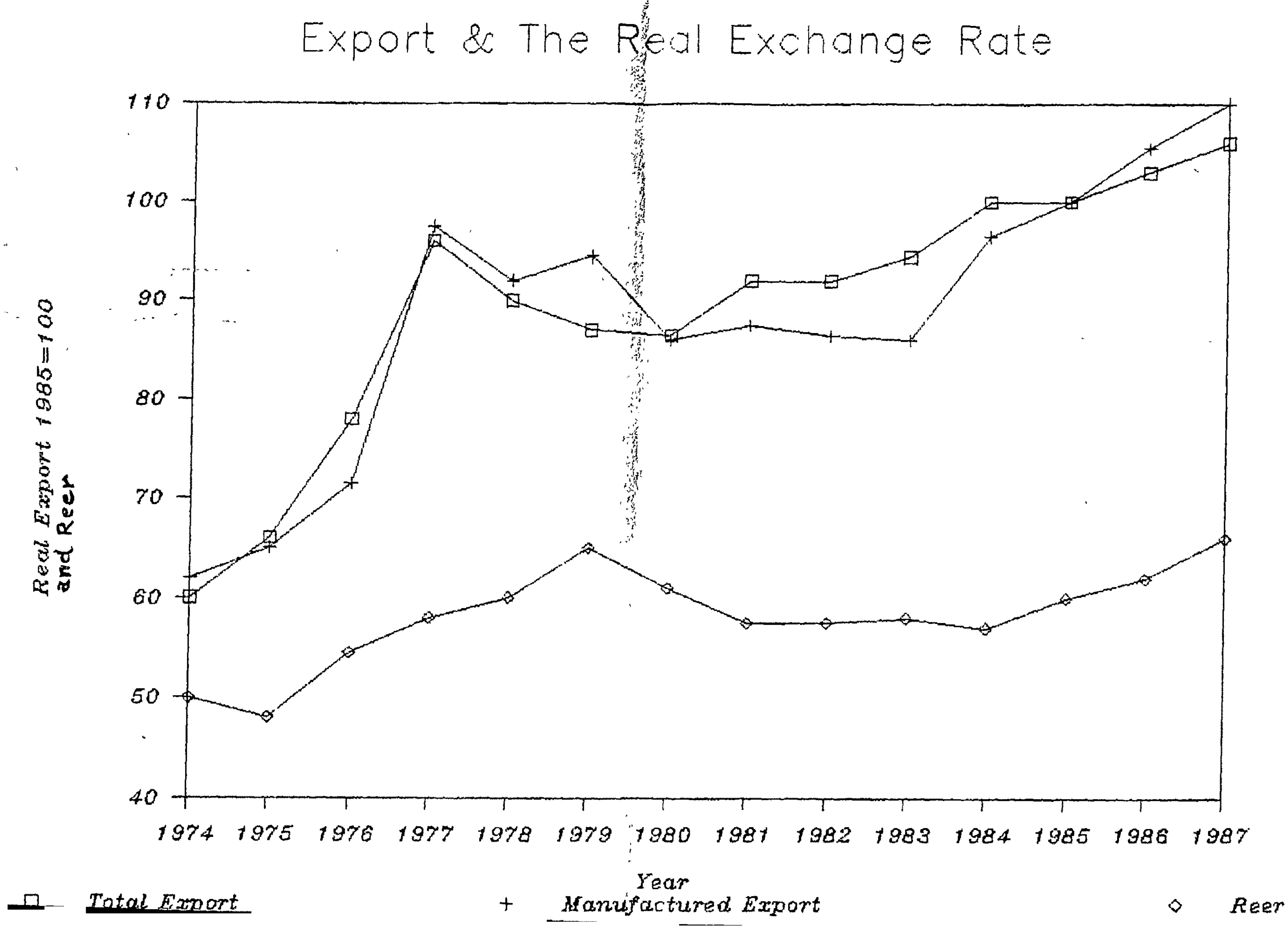
Nonetheless, it did appear that the changes which took place after 1974 were cumulatively significant not as any major shift in India's trade regime but as an indication of the country's interest in exports and its determination to ensure aequate profitability. Besides incentives being made more generous, many bureaucratic obstacles were also removed.

Economic Performance in the 1980s :

The 1980s in general were marked by significant and consistent moves towards progressive liberalization and grreater outward-orientation of the economy. The government took a number of measures to stimulate exports recognising the importance of export growth in containing the trade deficit and reducing the need for external financing. All in all, exports showed an increasing trend though the increase was slow since their sharp rise after 1976.

Fig. 5.1 presents the picture of India's economic performance for the period 1974 to 1987. Compared to the low level of exports in 1974 which rose steeply to a substantial level in 1977, the high level was somewhat maintained throughout the 1980s (in constant terms). In fact, in the later half of the 1980s as the figure shows, there was an increase in the level of exports above the 1977 level. Of course, as mentioned above, the yearly increases have not been as steep as those of the later half of 1970s. Moreover, manufactured exports performed somewhat better than total exports. However, from 1980-81 to 1985-86 as a whole,

FIGURE 5.1


Export & The Real Exchange Rate
110
100
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these grew by only 2.9 percent p.a. current prices and 3.7 percent p.a. in constant prices (1.5 percent in real terms from 1976-77 to 1985-85). Also, as regards the real exchange rate, as the figure shows, it improved for exporters in 1975 which also contributed to total as well as manufactured export growth. After 1976-77 the real exchange rate remained relatively constant until 1985-86. The low growth of total factor productivity (TFP) also served to worsen India's export competitiveness. Though labor productivity and capital intensity have been rising there was little improvement in TFP. The improved labor productivity mainly reflected increasing capital intensity but overall technical progress was slow. As a result, industrial growth as well as export competitiveness was hard to sustain. Table 5.11 presents the performance of selected key economic variables which summarizes the Indian economic performance in the first half of the decade of 1980s.

As seen in the table, India's falling and somewhat stagnant share in world exports which has been a consistent feature of its performance since the beginning of its development process in the 80s. Particularly, India's share of manufactured exports declined from 0.6 percent to 0.4 percent of world exports form 1976 to 1983, when at the time the developing country share of manufactured exports rose from 15.9 percent to 17.5 percent. Overall export performance continued to be disappinting except for a few manufactured exports. The performance during 1980s reflects the continuing superior profitability and securty of the domestic market which the export incentives failed to offset. Although the trade regime has been liberalized in some important

Table 5.11

India : Key Economic Variables

	1980/81	1981/82	1982/83	1983/84	1984/85	1985/86
<u>Incentive Indicators</u>						
1. Real Effective Exchange Rate						
Index 1980-100	100.0	100.0	101.6	98.9	102.7	105.9
Annual change (% p.a.)		0.0	1.6	-2.7	3.8	3.1
2. Real Interest Rates (% p.a.)						
Short term (Treasury Bills)	-5.9	-4.6	-2.4	-4.3	-1.5	-0.2
Long term (IDBI)	-0.2	-4.0	6.3	4.3	7.3	8.8
<u>External Trade Indicators</u>						
Exports (Mln. US $)	8332	8447	8386	8667	8746	8956
Imports (Mln. US $)	15893	15333	14385	14360	14400	16066
Trade Bal.(Mln. US $)	-7561	-6856	-5999	-5693	-5654	-7110
1. India's exports as % of :						
Exports of non-oil developing countries	2.7	2.6	3.0	2.8	2.7	2.3
Exports of developing countries	1.4	1.4	1.7	1.8	1.8	1.6
World Exports	0.5	0.5	0.6	0.6	0.5	0.4
LDCs manufactured exports	2.8	2.8	2.8	2.3	2.1	n.a.
2. Manufactured Exports						
Real Growth rate	1.5	-1.3	0.3	10.7	4.4	4.6
% of total exports	66.1	67.6	68.4	69.3	71.2	72.8
3. Commodity Terms of Trade						
Index 1980/81-100	100.0	104.3	106.0	106.8	110.0	112.9
Annual change (% p.a.)	-27.5	4.3	1.6	0.8	3.0	2.6

Source : Same as Fig. 5.1

ways through continuous efforts, the changes made hitherto have been quite small when compared with what India needs if it wants to take full advantage of its considerable potential for much faster economic growth. As Bhagwati and Srinivasan commented on the overall effect of the domestic policies which proved to be a major constraint on growth, "India's foreign trade regime in conjunction with domestic licensing policies in the industrial sector, led to economics inefficiencies and impaired her economic performance.........and adversely influenced export performance[3]".

All in all it may be noted that IS in itself was not bad but India did not not select the right sectors in which it had competitive national advantage. In fact, IS was not pursued on the basis of economic rationale so that India's industrial economy became extremely high-cost which further priced it out in the competitive international market. Table 5.12 summarizes the Indian growth performance form the 1st to the 7th Plan.

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3. Quoted in Tandon R. and Hatti N.," Export and Development : The Indian Experience", Ashish Publishing Co., New Delhi,1987 Pp.385.

Table 5.12

Plan Performance (Annual Growth Rates)

	GNP at factor cost Current prices	GNP at factor cost 1980-81 prices	Per capita NNP Current prices	Per capita NNP 1980-81 prices
First Plan (1951-56)	1.7	3.7	-0.5	1.7
Second Plan (1956-61)	9.4	4.1	7.1	1.9
Third Plan (1961-66)	9.5	2.7	6.9	0.1
Annual Plans (1966-69)	11.6	2.4	9.3	-0.1
Fourth Plan (1969-74)	10.9	3.4	8.4	0.9
Fifth Plan (1974-79)	10.6	5.0	7.9	2.6
Annual Plan (1979-80)	9.5	-4.9	5.7	8.2
Sixth Plan (1980-85)	15.1	5.5	12.5	3.2
Seventh Plan (1985-90)	13.6	5.5	11.2	3.4

Source : Suri, K. (1992)

Table 5.14

Purpose-wise distribution of Foreign Aid (Total three Five-Year Plans)
(in Rs. millions)

	Authorization	Utilization
1. Industrial development	23104 (60.5)	15413 (57.5)
2. Transport and Communication (including railways)	4578 (12.04)	4287 (16.0)
3. Iron & Steel projects	5106 (13.4)	3617 (13.5)
4. Power projects	3233 (8.5)	1943 (7.2)
5. Wheat loans	1060 (2.8)	1060 (3.9)
6. Agricultural development	655 (1.7)	259 (1.0)
7. Ports & Development	391 (1.0)	248 (0.9)
Total	38037 (100)	26827 (100)

Note : Figures in parentheses indicate percentage of distribution
Source : Same as Table 5.2

5.3 THE ENHANCED ROLE OF FOREIGN CAPITAL :

Foreign capital in India has played a significant role in giving a shape and direction to its economic growth. Before it attained independence, a considerable amount of foreign capital, mainly British, flowed into India. The capital came in the form of both equity capital and loans. Moreover, the source of foreign capital was mostly always private.

While much of India's planning strategy, after Indenpendence has been conceived in terms of a closed economy framework, external resources-financial and technological have made a significant contribution to its economic development. These resources, over time, began to taken the form of both private as well as official transfers. However, the dominant position has been assumed by official transfers with foreign investment and technical collaborations playing a relatively minor role.

What follows is a detailed review of each form of foreign capital inflow and their importance in India's growth particularly since the beginning of planned development efforts, 1950 onwards.

5.3.1 Foreign Aid and Foreign Borrowing :

The foreign aid programmes have been so designed as to assist India in its planned development. In a period of four decades till 1992, India has received more foreign aid than any other developing nation-about $55 billion since the beginning of its First Five-Year Plan in 1951, but has proved to be an unmitigated disaster for the country. Inspite of 45 years of aid-financed centrally planned development, India remains one of the poorest nations in the world and has had one of the lowest growth rates of all developing countries.

Foreign aid assumed a dominant role in India when a centrally directed heavy industrialization and self-reliant import-substitution strategy was adopted at the beginning of the second Five-Year Plan in 1956-57. Prior to this (the heavy industry-Oriented 2nd Plan), India had n ormally run a current account surplus had built up substantial reserves of foreign exchange. Since the very beginning of India's independence the use of foreign capital had been a sufficient condition for the development of the economy.

Immediately upon independence, particularly during the framing of the First Five-Year Plan, much attention was given to the restructuring and reorgainsation of the shattered economy. Agriculture and industry alike needed to be developed almost from scratch. At the time, agriculture assumed absolute importance in the Indian economy. It was, however, realized that domestic resources were not sufficient to incur such a huge expenditre in the public sector- to the extent of Rs. 2069 crores. As such, a part of the expenditure was sought to be financed by external assistance. The US financial and economic assistance to India thus commenced in 1951 with a loan of $189.7 million (Rs. 142.28 crores) to purchase two million metric tons of wheat. Since 1951, the US extended assistance in many other fields of India's development programmes. Over the years, a substantial part of aid had been in the form of food grains and other agricultural commodities and India was the largest recipient of US agrucullturał commodities under the Public Law-480 [PL-480 (food for peace)] programme. Food imports under this head were used to meet the shortfall in domestic production. Besides this, 23 percent of India's total national investment for development of industries in public sector undertakings was provided by the US, which lent its skill in agriculture, education, health and family planning, power and industry. About 60 percent of the total foreign aid to India came from the USA in varied forms-food, technical assistance and loans.

The amount expected from external sources during the Second Plan was very great; in fact, four times that of the First Plan-Rs. 800 crores. But the amount actually raised was even greater. Out of the total assistance of Rs. 2568.8 crores authorised during the Second Plan, loans and credits ammounted to Rs. 1280 crores, grants Rs. 157.9 crores and miscellaneous other assistance, Rs. 1130.9 crores. During the period, external assistance came from various sources viz. Canada, UK, West Germany, Japan, and of course, mainly US and USSR. Apart from these, countries like Poland, Yugoslavia and Czechoslovakia authorised loans repayable in rupees.

The total aid authorised by the IBRD was Rs. 265.3 crores as compared to Rs. 57.7 crores during the First Plan. These loans were basically for development purposes. Moreover, there were food loans like the PL-480 assistance. Purposewise, out of the total aid of Rs. 1382.5 crores available for utilization during the Second Plan, about 56% went towards the industry. All in all, the USA and the IBRD continued to be the sources of external

Table 5.13

A. Authorized and Utilized External Assistance to India 1951-67 (in Rs. Crores at pre-devaluation prices)

Item	Up to end of 1st plan	During 2nd plan	1961 -62	1962 -63	1963 -64	1964 -65	1965 -66	Total 3rd plan	1966 -67
I. Authorized									
1. Loans	226.89	1280.78	391.5	596.40	456.45	492.91	412.73	2349.99	702.42
2. Grants	137.96	125.47	22.47	14.74	15.69	25.66	59.31	137.87	39.41
3. Commodity Assistance	16.92	1130.73	-	43.33	4.91	225.20	177.19	450.63	249.30
Total I	381.77	2536.98	413.97	654.47	477.05	743.77	649.23	2938.49	991.13
II. Utilized									
1. Loans	126.42	724.75	228.92	306.73	388.67	485.48	498.68	1908.48	427.06
2. Grants	70.18	160.64	21.74	14.85	16.32	20.02	34.22	107.15	46.44
3. Commodity Assistance	5.07	344.81	88.01	122.72	185.19	218.12	239.18	853.22	228.40
Total II	201.67	1430.2	338.67	444.30	590.18	723.63	772.08	2868.85	701.90

B. Utilization of External Assistance by India as percentage of Net National Product at factor cost : 1951-52 to 1966-67

	1951 -52	1952 -53	1953 -54	1954 -55	1955 -56	1956 -57	1957 -58	1958 -59	1959 -60	1960 -61	1961 -62	1962 -63	1963 -64	1964 -65	1965 -66	1966 -67
Total Aid	0.86	0.47	0.19	0.11	0.40	1.05	2.37	2.71	2.28	2.86	2.29	2.89	3.34	3.54	3.80	3.04

Source : A. Economic Survey 1967-68 Govt. of India
B. calculated from Table 5.13II and Table 5.3A

assistance though other foreign governments also extened considerable aid. An important development regarding foreign assistance for economic development of India was the increasing realization on the part of other friendly countries of the growing requirements of foreign exchange during the development process and the greater willingness to extend their cooperation in the task.

In the Second Plan, loans for the development of both industry and agriculture were provided but in the First Plan a ground was prepared for a more balanced development with certain limitations, while the Second Plan laid greater emphasis on the development of basic industries and infrastructure which naturally required large amounts of external assistance.

Consequently, by the Third Plan, the drawing on foreign exchange resources became so heavy that no more resources were available except those that were required as minimum. As it was not possible to meet all the foreign exchange requirements with the export earnings which were inade quate, external assistance from international institutions and foreign governments remained an important source of financing developmental and maintenance import requirements.

During the Third Plan, it became possible to gauge the very substantial magnitude of aid received by India at absolute value as well as a proportion of world aid flow. For example the proportion of Development Assistance Committee (D.A.C.) aid that came to India during 1962-63 was as high as nearly 14 percent. Over the three Five-Year Plans, aid flow increased significantly-authorised as well as utilized. (See Table 5.13A). Moreover, the increase was steady even when measured as a proportion of national income (See Table 5.13B). An important feature of the external assistance during 1962-63 was an appreciable increase in the quantum of assistance and softtening of terms and conditions of the grants. About two-thirds of the loans were authorised on more favourable terms than previously. The loans from the USA, AID and IDA carried only small service charges and were for long maturity periods of forty to fifty years. At least two-thirds of these were for non-projects expenditure.

As regards purposewise distributon of aid, it was noted that more than 60 percent of the authorised assistance was for industrial purposes of which more than half was utilized upto the end the Third Plan. For infrastructure development, the largest utilization was the case of reilways. (Table 5.14)

However,at the same time, it was observed that though gross aid inflow increased overtime, net availability of aid deteriorated when amortization and interest payments on past aid are taken into account. The net aid flow situation showed a less dramatic improvement in the aid situation than is actually indicated in Table 5.13A. In fact, there was even a decline in the level of net aid after 1965-66 and amortization, and interest payments increased to over one-fourth of export earnings by 1967-68. Thus, as regards the question as to whether India has been over-aidedin relation to developing countries on the average, it is argued that if suitable deflated measures, such as aid per head, were taken, than India would in fact be a grossly under-aided country [4].

The success of development in India greatly increased its capacity to utilize additional resources more effectively. The US aid, in fact, helped India to finance the Green Revolution to a considerable extent by making available rapid increases in supply of fertilizers, pumps for irrigation, better seeds and pesticides and technical expertise. Food aid, as a form of additional resource, allowed India to shift its own resources to other productive sectors of the economy.In other words, food aid freed India's foreign exchange for developmental needs. Moreover, it was widely recognised that liberal PL-480 imports made India realize the needs of agricultural development.

So far as the efficiency of the Indian aid programme was concerned, it had been characterised by an unusually long lag between authorization and utilization of aid. This has obvious implications for its efficiency. A major variety of domestic factors that accounted for the delays in utilization of aid have their roots in India's planning procedures which put heavy reliance on comprehensive controls in `virtually all important spheres of economic' activity. Experience in India had showed that foreign aid solved balance-of-payments crisis only temporarily, but aggravated later. This was particularly the case

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4. The point has been noted by Streeten & Hill in `Aid to India' in P.Streeten and M.Lipton (eds.),` The Crisis of Indian Planning', that India received US$ 1.8 on an average between 1962 and 1963 as compared to Brazil ($2.5), Argentina ($4.2), Pakistan ($4.4), China ($6.3), S.Korea ($9.2) and Chile ($17.9).

when aid was increasingly sought not to build permanent assets but for current consumption (mostly non-essential ones) as was the case with India mainly due to the so-called non-project aid. The idea behind this was to finance the import of spares and components (maintenance imports) instead of complete plants. This became necessary after the machine building industry started coming up in the country. Below are presented three tables which give three different overall views of the foreign aid and external debt position of India in the mid-80s. Table 5.15 shows the overall external assistance utilized by India upto 1985-86. Table 5.16 gives the debt-service position for a period of about three and a half decades. Table 5.17 gives comparable estimates of debt-service and export growth for developing countries.

At the same time, criticisms of foreign aid have been widespread. Intellectuals assail foreign aid as the major factor which has permitted India to indulge in public sector expansion and inefficient, bureaucratic policies, since aid withdrawal would have forced the planners into pursuing more efficient policies involving greater reliance on the private sector and price mechanism. Owing to such criticism, it began to be generally felt that dependence on aid should be reduced gradually. External assistance without conditionalities was accepted. But then, if foreign aid was refused totally, the objective of raising the standard of living of the people of India would be a herculean task to achieve. In the years that foreign aid was considerable redeced, particularly 1975-78 (See Table 5.15), the economy had been virtually stagnant. As a re-

Table 5.15

Overall External Assistance (Utilization) (Rs. Crores)

Period	Grand Total
Up to end of Fourth Plan	11922.1
1974-75	1314.3
1975-76	1840.5
1976-77	1598.9
1977-78	1290.0
1978-79	1215.6
1979-80	1353 %
1980-81	2161.7
1981-82	1869.9
1982-83	2249.8
1983-84	2267.6
1984-85	2353.7
1985-86	2938.1
Total	34375.3

Source : Desai, S.S.M. (1988)

Table 5.17

Growth of Debt Serivce and Exports:Developing Countries (%)

Country	Debt Service Ratio		Debt Service		Exports	
	1967	1973	1967-70	1970-73	1967-70	1970-73
			(Annual Growth Rates)			
India	24.9	20.1	10.9	4.9	6.7	17.2
Brazil	16.0	13.9	16.9	26.3	18.7	30.1
36 Developing Countries[a]	9.5	9.4	15.7	20.9	13.4	23.8

a = according to World Bank Report 1975 classification.
Source : Banerjee B.N.(1977).

Table 5.16
External Debt Servicing (Rs. Crores)

Period	Total Debt Serviving (Amortisation & Interest)
First Plan	23.8
Second Plan	119.4
Third Plan	542.6
1966-67	274.5
1967-68	333.0
1968-69	375.0
1969-70	412.5
1970-71	450.0
1971-72	479.3
1972-73	507.4
1973-74	595.8
1974-75	626.0
1975-76	600.7
1976-77	653.9
1977-78	729.1
1978-79	796.0
1979-80	800.7
1980-81	803.9
1981-82	849.1
1982-83	947.5
1983-84	1032.5
1984-85	1176.2
1985-86	1366.6
1986-87	1600.4

Source : Same as Table 5.15

sult, the years thereafter experienced a steady increase in external assistance not undermining its significance for a growing and developing economy like India. Over the years, the trend began to move upwards.

By the late 1980s, India was able to achieve an excellent credit rating in international capital markets. However, its debt-service ratio increased form about 8% in 1981-82 to over 19% in 1986-87 reflecting the growing share of commercial borrowing in India's debt. The corresponding figures, if IMF repayments and interest are included, are 8.1% and 24.4%. Through the 1960s and 1970s, capital inflows were tightly controlled and whenever foreign exchange reserves declined substantially, the government tended to restrict imports and sacrifice growth, rather than accumulate high-cost debt. The objective of restricting the inflow of short-term high-cost funds, which needed approval of the government, was to check that the external indebtedness of the country is not duly extended. The foreign borrowing that did take place was mainly on concessional terms (aid). In 1978-80, less than 1% of India's outstanding debt was owed to private financial institutions. In recent years, however, limitations on foreign borrowing have been relaxed in order to accelerate economic growth. Owing to such relaxation , in 1985-86, 40% of India's total foreign loan commitments and 50% of the disbursements were accounted for by foreign commercial loans. By the end of 1986-87, about 22% of India's total outstanding debt was owed to private creditors. Moreover, concessional aid continued to play an increasingly important role in the succeeding years in order that debt service on commercial borrowing remained manageable given the mangitude of external capital requirements. On the other hand, aid availability also allowed India to implement policy reforms without depriving the economy of the investment funds needed to sustain growth.

Table 5.18 gives data with respect to approvals of external commercial borrowings since 1980-81. These approvals do not necessarily indicate their utilization.

If one takes an overall view of the last three decades reagrding foreign capital inflows to India one would observe that the structure of capital account in India has undergone considerable changes. In the sixties and seventies, as noted earlier, the main sources of financing the current account deficits were official loans on concessional terms. In 1980 nearly 90% of India's outstanding debt was to official creditors and 85% of that was on concessional terms. The picture however, changes dramatically by 1989 and official loans accounted for 61% of the total outstanding debt, which was a decline of 29%. The proportion of concessional loans had fallen to 47%. This decline in concessional assistance was almost entirely due to change in the composition of lending to India by the World Bank group. Being the poorest among developing countries, India definitely is justified in its claim for concessional assistance. However, the World Bank has reduced such flows. (See table 5.19A). Moreover, total interest payments in dollar terms have been increasing at a much faster rate than exports- 21.7% p.a. (compound rate) in the 1980s as compared to 7.8% p.a. growth in exports. Table 5.19B shows that at the beginning of the 90s, debt-export ratio had crossed 300% which is comparable to the 17 heavily-indebted Latin

Table 5.19

A. Structure of India's Long-term debt 1970-89 (in US $ million)

	1970	1980	1989
1. Total Debt Outstanding	7837	18322	54776
2. Total official debt, of which concessional	7507	16315	33371
3. Total Private debt	330	2007	21405

B. Debt Relations in heavily-indebted countries and India

	India	17 heavily-indebted countries	
	1989	1982	1987
Debt/GNP	21.5	45.6	58.0
Debt/Exports	303.5	254.6	317.9
Debt Service/GNP	1.9	7.9	6.2
Debt Service/Exports	29.3	43.9	34.1
Interest/GNP	1.1	4.8	3.9
Interest/Exports	17.8	26.9	21.4

Source : adapted from Jalan, Bimal (ed.) (1992) - "The Indian Economy : Problems and Prospects", Viking, Penguin Books India (P) Ltd., New Delhi, Pp. 181-182.

American, Asian & African countries. If this trend continues, the future for India with respect to external indebtedness does not position too well.

The external financing gap was a consequence of the policies adopted in mid-80s. As a result of the aggressive import liberalization measures, the trade gap and current account deficit widened. Aid-donors refused to cover the deficit so that the government resourted to commercial borrowing abroad. Interest payments on successively larger annual borrowings burgeoned, expanding the deficit year after year. Nonetheless, India st uck to its import liberalization policies financed with foreign borrowings. There is very little scope in the years ahead to finance inward-looking investments through recourse to external debt. There is an urgent need to first, stabilise the debt-export ratio and then, during the 90s, reduce it to manageable levels.

Table 5.20 A & B summarizes India's external debt position as it was in the 50s and 60s (Table 5.20A) and the 1980s (5.20B). The capital account remained in surplus in 1986-87 but the surplus declined sharply compared to 1986-87.

5.3.2 **Direct Foreign Investment :**

The debate over private foreign investment in Indian industrialization pre-dates Independence in contrast to the role of foreign aid which received considerable attention only after the initiation of large scale inflow of official assistance in the Second Plan. Indian attitude, particularly, Indian business, towards foreign investment had steadily grown hostile until independence. In 1945, a critical resolution was adopted on the subject by the National Planning Committee of the Indian National

Table 5.20

A. India : Balance of Payments, 1950-67 (in $ million)

Year	Capital Account Govt. Transfers long-term loans (net)	Pvt. transfers & long-term loans of which, direct investment	Changes in Reserves etc.	Other Pvt short-ter
1950	14	7	-34	-17
1951	84	21	103	48
1952	136	20	127	-83
1953	34	26	-53	-22
1954	42	25	-48	44
1955	102	80	-77	-19
1956	149	114	421	34
1957	278	113	702	-36
1958	650	59	249	20
1959	591	86	-97	19
1960	710	138	67	24
1961	694	63	59	-32
1962	725	69	136	7
1963	852	120	-23	22
1964	1322	118	-25	-5
1965	1137	74	103	6
1966	969	186	11	-67
1967	1247	150	14	19

[contd.]

Table 5.20 (contd.)

B. India : Balance of Payments, Summary (in $ million)

	1980/81	1981/82	1982/83	1983/84	1984/85	1985/86	1986/87 (P)
Exports,f.o.b.	8332	8477	8386	8667	8746	8956	10249
Imports,c.i.f.	-15893	-15333	-14385	-14360	-14400	-16066	-15757
Trade Balance	-7561	-6856	-5999	-5693	-5654	-7110	-5509
Net non-factor services	1365	1002	935	1036	1039	1514	2114
Resource Balance	-6196	-5854	-5064	-4657	-4615	-5596	-3395
Net Factor Income	615	381	-293	-526	-838	-1009	-1198
Net Current Transfers	2771	2317	2505	2570	2526	254	2176
Current Balance	-2810	-3156	-2852	-2614	-2927	-3951	-2417
Direct Investment	8	10	65	63	62	160	209
Official Grant Aid	643	496	399	367	453	450	369
Net M&LT Loans	2013	1720	2115	2204	2600	2853	2609
Capital Flows NEI	-311	-1717	-1399	29	-264	1244	-79
Errors/Omissions	-200	-441	210	-474	272	-	-
Net Credit - IMF	312	689	1968	1306	67	-209	-540
Capital Balance	2465	758	3357	3495	3190	4498	2568
Change in Reserves (- = Increase)	345	2398	-505	-881	-263	-547	-151
End-Year Reserves (Gross)	6859	4461	4966	5847	6110	6657	6808

Source : A. Same as Table 5.6
B. Same as Fig. 5.1

Congress which proposed that even existing foreign capital should be eliminated from key industries and maintaining that foreign capital had twisted out of shape and stunted the nation's development. In April 1949 policy towards foreign investment was liberalized with a view to encourage new foreign capital into India. It was recognised that Indian capital had to be supplemented by foreign capital not only because it was necessary for rapid economic development but also because with it would accompany the scientific technical and industrial knowledge which was a prerequsite for the country's development. However, in the absence of any explicit safeguards to eliminate the threat of resulting foreign competition, the domestic entrepreneurs began to be unsympathetic to the liberalization. Nonetheless, the total foreign capital which stood at about Rs. 287.7 crores in June 1948, increased to Rs. 419.3 crores by December 1953 and to Rs.480 crores by December 1955. The additional business investment during the period of 1948 to 1953 was Rs. 132 crores. During 1954 and 1955 the increase was Rs. 61 crores. A major change in the pattern of investment during 1954 and 1955 was that although two-thirds of the total increase during the period went towards the petroleum industry, a major portion of it was in the manufacturing of petroleum rather than in its trading. The manufactures attracted one-fourth of the increase. Moreover, the major sources of foreign investment were the industrially advanced countries of the First World. An interesting point to be noted was that at the time foreign companies were earning a higher rate of profit as compared to the earnings by capital in their own countries.

Table 5.21 gives the distribution of foreign capital and proportions of direct and portfolio investments therein, during the Second Five-Year Plan.

It was noted that portfolio investment, which was only a half of the directly controlled capital during 1956, doubled in 1957 and was considerably as higher in the next two years. However, in 1960, it again fell to half that of direct investments. In this year, a greater part of capital inflow came by reinvestment of profits and imports of machinery and equipment from aboard. An interesting point to note was that during the entire period of 1956-60 as a whole, portfolio investment came largely form the US while direct capital was preponderant in case of British firms.

Despite opposition from within the government against DFI as mentioned earlier, the policy of liberalization of foreign investment was to stay. In the early years of planning, policy measures towards this were accentuated. The relaxations concerning majority ownership, though on an ad hoc basis, were prompted by the thinking that India's industrial development required the influx of technical expertise and capital and that private foreign investment was an appropriate and possibly a major source for wuch scarce resources. However, as seen earlier, until the beginning of the Second Plan, relatively very few investors came. Thereafter, with the initiation of the Second Plan, the need for foreign capital was reinforced by the foreign-exchange shortage due to the crisis in 1956-57 and continued reliance on exchange and import controls that followed. These

Table 5.21

Kinds of foreign investment (Rs. Crores)

Year	Direct	Portfolio	Total
1956	24.2	12.7	36.9
1957	17.8	32.2	50.0
1958	3.5	26.1	29.6
1959	10.4	27.5	37.9
1960	53.6	26.4	80.0

Source : Khan, M.S. (1961).

Table 5.23

A.Growth of multinational corporations in India(1973/74 to 1978/89)

Country of Incorporation	No.of Companies		Assets (Rs.Crores)	
	1974-74	1978-79	1973-74	1978-79
1. United Kingdom	319	189	1239	1659
2. United States	88	64	381	535
3. Japan	21	17	24	64
4. Other	111	88	147	156
Total	539	358	1791	2401

B. Recent Collaboration Agreements

	1984	1985	1986
1. Foreign collaborations Approved (No.s)	752	1024	958
2. of which :			
a. Financial Collaborations (No.s)	151	238	242
b. Foreign Investment (Rs. Crores)	113.00	126.86	106.90

Source : Same as Table 5.15, derived

developments weakened the objections within the government to absorb foreign private capital. Moreover, the high rate of projected growth, lack of indigenous technological capibility and availability of World Bank and other foreign credits alongwith the foreign-exchange crisis, all led to an influx of foreign capital into a number of industries. Of course, though multinationals were knocking the doors, they were consciously kept out of several sectors. The protected markets which followed as a result, revived the hostile attitudes to foreign capital. The influx of foreign investment began to be seen essentially as a method by which the Indian entrepreneurs could acquire the know-how to produce in a more profitable and large domestic market and a way by which the government could be persuaded that the foreign exchange cost of the project was being met by the capital inflow itself. Thus, while regulations regarding foreign investment were liberalized, the changing business attitudes also led to a simultaneous stiffenting of other aspects of governmental policy in this area such as detailed scrutiny and approval of each act of foreign investment and sale of technical expertise. The industrial pattern of private foreign investment inflow also began to be regulated. This was the reason why several sectors were out of bounds for foreign investment as mentioned earlier-'key' industries such as steel (on political grounds) and inessential industries such as certain consumer goods, services and trade. The latter was the result of a definite tendency on economic grounds. Subject to such rules and regulations, criteria and meeting the terms and conditions approved by the licensing authorities, the overall policy inclination was generally towards encouragement of private foreign investment.

Over the years, two distinct types of foreign investment operations began to be characterized by the Indian experience - one, equity investment or direct foreign investment and another, purely technical collaborations. The latter was concerned with buying know-how. In actuality, there were, of course, a mixture of the two. Table 5.22 gives the position of the total financial foreign business investment as it stood at the end of 1961.

Table 5.18

External Commercial Borrowings

(Rs.Crores)

1980-81	1981-82	1982-83	1983-84	1984-85	1985-86	1986-87	1987-88
1038	1204	2026	1085	1906	1700	1396	2654

Source : Economic survey, 1988-89, Government of India.

Table 5.22

Foreign Business Investment from Private Sources : Mid - 1948 to end 1961. (in Rs. crores)

Mid - 1948	End 1961	Percentage growth 1948-61
255.9	580.4	227

Sources : Derived from same source as Table 5.2

In 1972, a major step to attract foreign capital was initiated by India in that it permitted wholly-owned subsidaries of foerign companies, provided they undertook export of 100 percent of their production. In case the objective was not met, the extent of foreign capital permissible was decided by negotiations between the government and foreign companies. The enactment of the Foreign Exchange Regulation Act (FERA) in 1973, tightened equity shareholding policy bringing down foreign equity to a maximum of 40% except for export-oriented and high-tech companies where a higher controlling interest was allowed. The objective of FERA was to limit foreign exchange drain in the form of repatriation of divideds. Nonetheless, new foreign investment declined and flow of technology from parent companies reduced so that there had to be collaborations for relatively minor technology transfers. Thus, the BoP did not improve much.

Till 1980, the economy functioned normally as regards DFI. But by this time, another foreign-exchange crisis surafced and the then ruling government took a hugh loan from the IMF. The perception regarding foreign investment changed further and there were further policy liberalizations. The process was greatly accelerated in late 1984. In such a climate, the catchwords became efficiency, modernisation, technological upgradation and export-orientation. Foreign capital began to be welcomed into many areas hitherto closed, mainly in order to supplement domestic savings and the inflow multiplied manifold. Inspite of such a positive development, the government retained discretionary powers to decide each proposal by merit. It must be noted that DFI, in India, appeared to have concentrated in agriculture, trade and commerce. From 12 percent in 1973-74, its share in manufacturing declined to 6 percent in 1978-79. This was proof enough of the fact that foreign investors were not very much interested in the development of industries and technology transfer especially in the vital sector of industries.

Since 1984-85, DFI has been growing which may well reflect policy changes and improved investment climate but, nonetheless, it remains a relatively small item in India's GDP. Moreover, an important feature of foreign investment was that although policies have encouraged minority participation and outright purchases of technology, it has served to reduce the volume and quality of technology inflow. This was due to the fact that technology vendors generally sought a controlling equity stake or at least a sufficiently attractive payment terms to part with the latest know-how. Besides this, India's trade policy and efforts to conserve foreign exchange have also contributed to technology deficiencies such as ban on consumer-goods imports, eliminating the fear of foreign competition to modernize and upgrade quality, and protection of domestic capital goods which has adverse effects on investment goods technology. Thus, it seems that if that if the role of DFI is to increase significantly, India needs to review its current policies affecting it and take steps to remove the remaining barriers to joint ventures and to the flow of risk capital into India. The size of the country has meant that whatever considerable sums of aid it has received have nonetheless amounted to a significantly lower proportion of its GNP than in case of several other developing countries which have registered superior economic performance. Similar is the case with DFI. Even though India's policy is not entirely open-door, it is unconceivable that any DFI that flows in will be at any-where close to the percentage of GNP level that it has achieved in 'star' developing countries like S.Korea, Taiwan and Israel.

India's experience has a direct impact on the development strategy consisting of booming industrial investments by cutting off imports and offering sheltered markets indiscriminately. Such an approach negates the very definition of planning and leads to an indiscriminate growth of industries regardless of costs. Once such industries have taken root, it becomes extremely difficult to revert to efficient policies. A country cannot have growth first and efficiency next but these two processes have to go hand in hand. Indian experience highlights these lessons quite boldly. In 1939, Nehru had written "....India will always make a difference to the world.....when we fall, we fall low; when we rise, we inevitably play our part in the world drama,' and after independence, "leaving the USA, Soviet Union and China aside for a moment (though there are many advanced highly cultured countries)... if you peep into the future .... the obvious fourth country in the world is India"[5]. What a travesty of truth !

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5. Quoted from Suri k ,"India's Economy and the World", Vikas Publishing House, New Delhi, 1992,Pp 44.