

## A Remarkable Milestone

*India's economic transformation over the past quarter century has brought unprecedented progress and advanced its rise in the world order*

by Ambassador Hemant Krishan Singh, Director General, Delhi Policy Group



Milestones matter, even when they (mostly) pass silently by. The 25th anniversary of India's 1991 economic reforms has just gone by without much fanfare. Nonetheless, there is broad consensus among economists and analysts alike that the liberalization era has transformed the Indian economy from a backwater into a dynamic, entrepreneurship and private sector led, democratic free market economy. By bringing about unprecedented growth and wider prosperity, liberalisation has also balanced the demands of economic efficiency with the greater imperative of social equity, which together constitute India's political economy binary. Hundreds of millions have been lifted out of extreme poverty as the nominal per capita GDP has tripled to \$1,800. Far from collapsing under foreign competition as some had feared in 1991, India's private sector-led industry is today more strong, resilient, productive and globally competitive across several sectors, from services to manufacturing. Openness has propelled exponential growth of the IT sector. With a 7% share in the world economy (PPP) and a trade to GDP ratio of 49%, India is now both economically significant and integrated with the world<sup>1</sup>.

Of course, more could have been done and much did not happen. After the initial burst of industrial delicensing, lifting of import controls, move to a market exchange rate, lowering of tariffs and opening up of the Indian market to both FDI and FII, the reformist impulse gradually faded and finally lost political traction after 2004. Industrial expansion has largely been capital and technology intensive. Absence of backing for labour market reforms has imposed a heavy price on formal sector employment and manufacturing growth<sup>2</sup>. Unsurprisingly, as in 1991, 90% of India works informally<sup>3</sup>. From banking reforms to PSU disinvestment, pricing reforms to populist subsidies, failure to follow through with the 1991 reform surge has held back economic performance. Land markets have tightened after the Land Acquisition Act of 2013, denting prospects for industry and urban infrastructure<sup>4</sup>. The low wage advantage and manufacturing for export model has largely passed India by, with its exporters facing mainly domestic challenges, from de facto labour

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costs to logistics and quality infrastructure. Tariff protections have rendered our trade negotiators unable to negotiate meaningful trade instruments which can trigger domestic reform and boost export and economic competitiveness<sup>5</sup>.

This adverse trend has been decisively reversed since May 2014, with Prime Minister Narendra Modi ushering in a new era of economic aspiration and the vision of a globally competitive India as an attractive destination for foreign investment, drawing capital, technology and knowhow essential for India's economic rise.

*“The Indian government’s policy-making since 2014 has been consistently forward looking as PM Modi has pursued his nation building vision...”*

The success of India’s 1991 economic reforms was ensured by the extraordinary coherence of policy making in a crisis situation. Similarly, the Indian government’s policy-making since 2014

has been consistently forward looking as PM Modi has pursued his nation building vision of energized and transparent governance, incremental structural reform, FDI liberalization and cooperative federalism, while also advancing several national schemes and initiatives to give Indian states a policy direction. India’s Prime Minister is market pragmatic rather than market liberal, reflecting the demands of the political economy, but he is unquestionably an inspired reformer of government, society and economic conditions. He has sought to overcome old mindsets and challenged our nation to think: how long will India remain a struggling developing country? When will we finally be developed? Can India dare to succeed?

PM Modi has been a developmental nationalist not only at home but also abroad, through his multi-directional engagement of foreign powers and the pragmatic pursuit of India’s economic and security interests, together with the key partnerships which serve them. He has boldly asserted India’s aspiration to become a “leading power”.

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Identifying with the masses, PM Modi has been perceptive in his management of public expectations. His pursuit of “astute politics, sound economics” creates greater room for reform legislation. The government’s prioritisation of infrastructure investment in roads, power and railways has been commendable. So has its redirected focus on rural

revival, the financial inclusion initiative, the rationalisation of gas subsidies and the statutory backing for Aadhaar to provide more targeted social welfare benefits. The improving quality of government expenditures and continuing fiscal consolidation have added to India’s macro-economic stability.



*Commuters interact with Prime Minister Narendra Modi in the Delhi Metro, September 6, 2015 (Source: PTI)*

*“However, the economic liberalization process initiated in 1991 remains a work in progress.”*

However, the economic liberalization process initiated in 1991 remains a work in progress. An efficient “Make in India” manufacturing sector

which produces trading strength in goods requires deeper and wider domestic reform, not lingering barriers to trade. The complexities and frequent changes of our FDI regime, from single to multi-brand retail, food processing to e-commerce, still make India’s market both difficult and unpredictable. This hurts deeper integration with global value chains, particularly at a time when our leading partners in East Asia are moving towards trade liberalisation instruments which benchmark higher rules for enhanced business activity. India can benefit from a predictable policy environment that makes its economy more open, more competitive and more inclusive<sup>7</sup>. The government must also continue to address both the ease and the cost of doing business in India.

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Domestically, the Goods and Services Tax (GST) legislation pending in Parliament remains the ultimate symbol of unfulfilled economic potential. The NCAER predicts that the GST can boost India’s economic output by some 1.7%.

A unified national market will augment seamless national supply chains, improve productivity, benefit both consumers and producers while also boosting employment<sup>8</sup>.



Prime Minister Narendra Modi with Silicon Valley CEOs in San Jose, September 26, 2015 (Source: MEA)

As frequently transpires with democratic polities in transformation, much work also lies ahead in the comprehensive improvement of basic government services, the rule of law and access to judicial remedy, education and health<sup>9</sup>. India needs stronger institutions that are independent but complementary in meeting public expectations for more effective democratic governance.

*“India is not insulated from the turbulent trends that the global political and economic order is traversing.”*

India is not insulated from the turbulent trends that the global political and economic order is traversing. Twenty five years after the triumph of liberal democracy and globalised free markets in

1991, economic decline and growing public insecurity are changing the political discourse in several advanced western nations towards isolationism, protectionism and economic populism. We are witnessing contradictory trends, where elements of globalization are under challenge and the liberal trading order is under pressure, at a time when the world economy is much more integrated than 25 years ago. Building protectionist walls and retreating from the world is hardly the solution<sup>10</sup>. As India’s own experience and practice with political economy impulses shows, leaders and decision makers must invariably respect democratic processes in policy making and pursue responsive governance to avoid a popular backlash.

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In the midst of adverse global trends, India has emerged as the world’s fastest growing major economy, having gained from global tailwinds as a commodity importer and its relatively lower trade and economic exposure to China<sup>11</sup>. Potentially, India is destined to be the world’s largest market place for goods and services given the sheer magnitude of its growing consumer market and favourable demographic trends. With several major emerging economies deep in negative territory, it is hard for global business to ignore the India opportunity today.

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Keeping faith with the reformist policies which have helped transform India in less than a generation will put India even more firmly on track to become a powerful growth engine of the

world economy in the years ahead. In PM Modi's own words, "India cannot wait for incremental change. We need transformational change and that comes only with drastic policy reform"<sup>12</sup>. This is a 25 year old success story that awaits new chapters of achievement, which in the coming decades will decisively reposition India's place in the world order.

*“In PM Modi's own words, "India cannot wait for incremental change. We need transformational change and that comes only with drastic policy reform.”*



*“India cannot wait for incremental change. We need transformational change and that comes only with drastic policy reform”*: Prime Minister Narendra Modi addresses Niti Aayog in New Delhi, July 28, 2016 (Source: PTI)

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**Endnotes:**

- <sup>1</sup> Sadanand Dhume, "India's Half-done Reforms", *The Times of India*, July 27, 2016.
- <sup>2</sup> Shaji Vikraman, "Our demographic dividend could become a nightmare if we don't focus on labour reforms: Shankar Acharya", *The Indian Express*, July 7, 2016.
- <sup>3</sup> Sachin Bansal, "India's Reverse Brexit", *The Times of India*, July 25, 2016.
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- <sup>5</sup> Hemant Krishan Singh, "Acting East: Aligning Economic and Strategic Goals", *Delhi Policy Group Policy Note*, Vol. I, Issue 1, July 6, 2016.
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- <sup>7</sup> Ashok Gulati, "From plate to plough: A thought for food", *The Indian Express*, July 18, 2016.
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- <sup>9</sup> SA Aiyar, "25 years on, the good, bad and ugly of reforms", *The Times of India*, July 17, 2016.
- <sup>10</sup> Daniel Twining, "Asia's reformist antidote to Western populism", *Nikkei Asian Review*, July 21, 2016.
- <sup>11</sup> Daniel Twining, "Waiting for a Modi Miracle", *The International Economy Magazine*, July 18, 2016.
- <sup>12</sup> Mahendra Singh, "Transformational change must: Modi", *The Times of India*, July 29, 2016.



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