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CHAPTER 1 - INDIAN ECONOMY ON THE EVE OF INDEPENDENCE

The structure of India's present-day economy has its roots steeped in history, when India was under British rule. The British rule lasted for almost two centuries before India finally won its independence on 15 August 1947.

Sole purpose of the British colonial rule in India: was to reduce the country to being a raw material supplier for Great Britain's own rapidly expanding modern industrial base.

Economic development under the colonial rule

- In Indian economy, agriculture was the main source of livelihood for most people.
- India was well known for its handicraft industries in the fields of cotton and silk textiles, metal and precious stone works etc. These possessed its fine quality and high standards of craftsmanship, hence they enjoyed worldwide market.

Changes brought by the economic policies of the colonial government in the structure of the Indian economy were:

It transformed the country into

- supplier of raw materials
- consumer of finished industrial products from Britain

Most studies found the country's growth of aggregate real output during the first half of the twentieth century was **GDP Growth < 2%** and rise in **GDP/Capita < 0.5%.**

Agriculture Sector

- About 85% of the country's population derived livelihood directly or indirectly from agriculture.
- Despite this the agricultural sector continued to experience stagnation and unusual deterioration because of the various systems of land settlement that were introduced by the colonial government particularly the zamindari system.
- Low levels of technology, lack of irrigation facilities and negligible use of fertilisers, all added up to aggravate the plight of the farmers and contributed to the dismal level of agricultural productivity.
- Due to commercialisation of agriculture, there were some evidences of relatively higher yield of cash crops, but this did not improve the farmers' economic condition.
- Instead of producing food crops, now farmers were producing cash crops which were to be ultimately used by British industries back home.
- India's agriculture was starved of investment in terracing, flood-control, drainage and desalination of soil.
- A large section of tenants, small farmers and sharecroppers neither had resources and technology nor had incentive to invest in agriculture.

Industrial Sector

- India could not develop a sound industrial base under the colonial rule.
- The country's world-famous handicraft industries declined resulting in massive unemployment and created demand in the Indian market which was fulfilled by imports of cheap manufactured goods from Britain.
- In the second half of nineteenth century, modern industries began to take root in India but were confined to the setting up of cotton (western parts), jute textile mills (eastern parts)
- Iron and steel industries began in the beginning of the twentieth century, the Tata Iron and Steel Company (TISCO) was incorporated in 1907.
- Few other industries in the fields of sugar, cement, paper etc. came up after the Second World War.
- There was hardly any capital goods industry (which can produce machine tools used for producing articles for current consumption) to help promote further industrialisation in India.
- The contribution of Industrial sector to the Gross Domestic Product (GDP) or Gross Value Added remained very small.

- The area of operation of the public sector was very limited under the new industrial sector. It remained confined only to the railways, power generation, communications, ports and some other departmental undertakings.

Foreign Trade

- The restrictive policies of commodity production, trade and tariff pursued by the colonial government adversely affected the structure, composition and volume of India's foreign trade.
- Britain maintained a monopoly control over India's exports and imports. More than half of India's foreign trade was restricted to Britain while the rest was allowed with a few other countries like China, Ceylon (Sri Lanka) and Persia (Iran).
- Large export surplus was generated which was used to make payments for the expenses incurred by an office set up by the colonial government in Britain, expenses on war and the import of invisible items.

Demographic Condition

- First census in British India was conducted in 1881 (carried out in every ten year thereafter). It revealed the unevenness in India's population growth.
- The overall literacy level was less than 16 per cent. Out of this, the female literacy level was at a negligible low of about seven per cent.
- Public health facilities were either unavailable or, when available, were highly inadequate.
- The overall mortality rate was very high and particularly, the infant mortality rate was quite alarming (about 218 per thousand).
- Life expectancy was also very low (44 year).

Occupational structure

- The agricultural sector accounted for the largest share of workforce i.e 70-75%, while the manufacturing and the services sectors accounted for only 10 and 15-20% respectively.
- There was growing regional variation like Madras Presidency, Bombay and Bengal witnessed a decline workforce in the agricultural sector and increase in the manufacturing and the services sectors.

Infrastructure

- Under the colonial regime, basic infrastructure, such as railways, ports, water transport, posts and telegraphs developed. The real motive behind this development was to subserve various colonial interests.
- The roads that were built primarily served the purposes of mobilising the army within India and drawing out raw materials from the countryside to the nearest railway station or the port to send these to far away England or other lucrative foreign destinations.
- The British introduced the railways in India in 1850 and it is considered as one of their most important contributions and affected the structure of the Indian economy in two important ways, one it enabled people to undertake long distance travel and thereby break geographical and cultural barrier, second it fostered commercialisation of Indian agriculture which adversely affected the self-sufficiency of the village economies in India
- They (Colonial Government) also took measures for developing the inland trade and sea lanes but they also proved uneconomical and failed to compete with the railways, and had to be ultimately abandoned.
- The postal services served a useful public purpose but remained all through inadequate.

Conclusion

- By the time India won its independence, the impact of long British colonial rule was showing on all aspects of the Indian economy.
- The agricultural sector was already saddled with surplus labour and extremely low productivity.
- The industrial sector was crying for modernisation, diversification, capacity building and increased public investment.

- Foreign trade was oriented to feed the Industrial Revolution in Britain.
- Infrastructure facilities, including the famed railway network, needed upgradation, expansion and public orientation.
- Prevalence of rampant poverty and unemployment required welfare orientation of public economic policy.

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CHAPTER 2 - INDIAN ECONOMY 1950 – 1990

On 15 August 1947, after India got independence, the job of nation building was in our own hands.

The leaders of independent India had to decide the type of economic system most suitable for our nation, a system which would promote the welfare of all.

It was decided by our National leaders that India would be a socialist society with a strong public sector but also with private property and democracy.

The government would plan for the economy with the private sector being encouraged to be part of the plan effort.

The 'Industrial Policy Resolution' of 1948 and the Directive Principles of the Indian Constitution reflected this outlook.

In 1950, the Planning Commission was set up with the Prime Minister as its Chairperson. The era of five-year plans had begun.

Types of Economic system

1. **Capitalist Economy:** Only those consumer goods will be produced that are in demand. Goods produced are distributed among people not on the basis of what people need but on the basis of their Purchasing Power, i.e., goods that can be sold profitably either in the domestic or in the foreign markets.

2. **Socialist Economy:** The government decides what goods are to be produced in accordance with the needs of society and distribution under socialism is supposed to be based on what people need and not on what they can afford to purchase.

3. **Mixed economies:** Market will provide whatever goods and services it can produce well, and the government will provide essential goods and services which the market fails to do.

The goals of Five-Year plans

The goals of the five-year plans were: growth, modernisation, self-reliance and equity.

Due to limited resources, a choice has to be made in each plan about which of these goals is to be given primary importance and the policies of the plans do not contradict these four goals.

- **Growth:** It refers to increase in the country's capacity to produce the output of goods and services within the country which implies either a larger stock of productive capital, or a larger size of supporting services like transport and banking, or an increase in the efficiency of productive capital and services.

  A good indicator of economic growth is steady increase in the Gross Domestic Product (GDP)

  The GDP is the market value of all the goods and services produced in the country during a year.

  The GDP of a country is derived from the different sectors of the economy i.e. the agricultural sector, the industrial sector and the service sector.

- **Modernisation:** It refers to adoption of new technology to increase the production of goods and services.

  It also refers to changes in social outlook such as the recognition that women should have the same rights as men.

- **Self-reliance:** It refers to avoiding imports of those goods which could be produced in India itself.

  The first seven five year plans also gave importance to self-reliance. This policy was considered a necessity in order to reduce our dependence on foreign countries, especially for food.

- **Equity:** It refers to the benefits of economic prosperity reaches to all the section of the society instead of being enjoyed only by the few.

Every Indian should be able to meet his or her basic needs such as food, a decent house, education and health care and inequality in the distribution of wealth should be reduced.

Agriculture

During the colonial rule there was neither growth nor equity in the agricultural sector. The policy makers of independent India had to address these issues which they did through land reforms and promoting the use of 'High Yielding Variety' (HYV) seeds which ushered in a revolution in Indian agriculture.

- **Land Reforms:** It primarily referred to change in the ownership of landholdings. After independence, steps were taken to abolish intermediaries like zamindars, jagirdars and to make the tillers the owners of land.

  The idea behind this move was that ownership of land would give incentives to the tillers to invest in making improvements provided sufficient capital was made available to them.

- **Land ceiling:** It refers to fixing the maximum size of land which could be owned by an individual.

  The purpose of land ceiling was to reduce the concentration of land ownership in a few hands.

  This legislation faced hurdles, as the big landlords challenged the legislation in the courts, delaying its implementation. They used this delay to register their lands in the name of close relatives, thereby escaping from the legislation.

  Land reforms were successful in Kerala and West Bengal because these states had governments committed to the policy of land to the tiller.
- **The Green Revolution:** This refers to the large increase in production of food grains resulting from the use of high yielding variety (HYV) seeds especially for wheat and rice.
  The use of these seeds required the use of fertiliser and pesticide in the correct quantities as well as regular supply of water. The application of these inputs in correct proportions is vital.

  The government provided loans at a low interest rate to small farmers and subsidised fertilisers so that small farmers could also have access to the needed inputs.

  The spread of green revolution technology enabled India to achieve self-sufficiency in food grains; India no longer had to be at the mercy of any other nation, for meeting its food requirements.

  The portion of agricultural produce which is sold in the market by the farmers is called marketed surplus. A good proportion of the rice and wheat produced during the green revolution period (available as marketed surplus) was sold by the farmers in the market.

  The green revolution enabled the government to procure sufficient amount of food grains to build a stock which could be used in times of food shortage.

Industry and trade

The five-year plans placed a lot of emphasis on industrial development because Industry provides employment which is more stable than the employment in agriculture; it promotes modernisation and overall prosperity.

At the time of independence, the variety of industries was very narrow — largely confined to cotton textiles and jute. There were two well-managed iron and steel firms — one in Jamshedpur and the other in Kolkata. We needed to expand the industrial base with a variety of industries if the economy was to grow.

- **Public and Private Sectors in Indian Industrial Development:** The erstwhile governments had to play an extensive role in promoting the industrial sector.

In addition, the decision to develop the Indian economy on socialist lines led to the policy of the government controlling the commanding heights of the economy, as the Second Five Year plan put it.

This meant that the government would have complete control of those industries that were vital for the economy.

The policies of the private sector would have to be complimentary to those of the public sector, with the public sector leading the way.

- **Industrial Policy Resolution 1956 (IPR 1956):** This resolution formed the basis of the Second Five Year Plan, the plan which tried to build the basis for a socialist pattern of society.

  This resolution classified industries into three categories.

  - **The first category** comprised industries which would be exclusively owned by the government.
  - **The second category** consisted of industries in which the private sector could supplement the efforts of the public sector, with the government taking the sole responsibility for starting new units.
  - **The third category** consisted of the remaining industries which were to be in the private sector.

    The private sector was kept under state control through a system of licenses. No new industry was allowed unless a license was obtained from the government. This policy was used for promoting industry in backward regions.

    It was easier to obtain a license if the industrial unit was established in an economically backward area and also were given certain concessions such as tax benefits and electricity at a lower tariff. The purpose of this policy was to promote regional equality.

- **Small-Scale Industry:** A 'small-scale industry' is defined with reference to the maximum investment allowed on the assets of a unit.

  In 1955, the Village and Small-Scale Industries Committee, also called the Karve Committee noted the possibility of using small-scale industries for promoting rural development.

  In 1950, a small-scale industrial unit was one which invested a maximum of rupees five lakh; at present the maximum investment allowed is rupees ten crores.

  To promote small scale industries, the production of a number of products was reserved for the small-scale industry.

  They were also given concessions such as lower excise duty and bank loans at lower interest rates.

Trade policy: import substitution
In the first seven plans, trade was characterised by an inward-looking trade strategy called import substitution. This policy aimed at replacing or substituting imports with domestic production.

Protection from imports took two forms: tariffs and quotas.

Tariffs are a tax on imported goods; they make imported goods more expensive and discourage their use.

Quotas specify the quantity of goods which can be imported.

The effect of tariffs and quotas is that they restrict imports and, therefore, protect the domestic firms from foreign competition.

Effect of Policies on Industrial Development:
The proportion of GDP contributed by the industrial sector increased in the period from 13 per cent in 1950-51 to 24.6 per cent in 1990-91.

The rise in the industry's share of GDP is an important indicator of development.

The industrial sector became well diversified by 1990, largely due to public sector.

Protection from foreign competition enabled the development of indigenous industries in the areas of electronics and automobile sectors which otherwise could not have developed.

Conclusion

The progress of the Indian economy during the first seven plans was impressive indeed.

- ✓ Our industries became far more diversified compared to the situation at independence.
- ✓ India became self- sufficient in food production thanks to the green revolution.
- ✓ Land reforms resulted in abolition of the hated zamindari system.
- ✓ In industrial sector, many economists became dissatisfied with the performance of many public sector enterprises. Excessive government regulation prevented growth of entrepreneurship.
- ✓ In the name of self-reliance, Indian producers were protected against foreign competition and this did not give them the incentive to improve the quality of goods that they produced.
- ✓ Indian policies were 'inward oriented' that failed to develop a strong export sector.

The need for reform of economic policy was widely felt in the context of changing global economic scenario, and the new economic policy was initiated in 1991 to make Indian economy more efficient.

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