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Reforms need to reach the needy

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  To reduce the poverty ratio substantially and to improve our performance on other social parameters, the country needs to grow faster in a sustained way. Photo shows a child picking up rags along the Vaigai river in Madurai, Tamil Nadu. Photo: R.Ashok

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Though reforms are aimed at increasing the efficiency through enhanced competition, they do not automatically result in growth. Neither does economic growth by itself translate into better social sector outcomes. A definite policy paradigm that prioritises social welfare is needed

Reforms are on everyone's lips. Whenever growth slows down, it is blamed on the slowdown in the implementation of reforms. Despite the enormous noise made about reforms, there is no clarity on what constitutes reforms and what the impact of reforms is on growth and social sector spending.

Looking back, 1991 is an important landmark in the post-Independence economic history of our country. The country then faced an acute economic crisis, triggered by a severe balance of payments problem. But the crisis was converted into an opportunity to bring about fundamental changes in the content and approach to economic policy.

Until the end of the 1970s, and to a large extent even in the 1980s, development was state-directed and state-driven. The government subscribed to the theory of 'commanding heights' which meant that key sectors of the economy were to be under state control. The private sector was kept in check through an elaborate scheme of licences and controls. In foreign trade, 'import substitution' was the guiding principle and this meant quantitative controls on imports and high import tariffs.

Efficiency and equity

A fundamental shift from this perception to one supporting a liberalised economy occurred in the early 1990s. There is a common thread running through the various measures introduced since July 1991 — the objective of improving the productivity and efficiency of the economy by injecting a greater element of competition. This is sought to be achieved by removing the barriers to entry and growth. This has led to the dismantling of various controls and licences. Many areas which were exclusively reserved for the state are now open to the private sector. As a consequence, the role of the state as a producer of marketable goods and services has gone down.

However, simultaneously, its role as a regulator and as a provider for public goods and services has increased, even though with respect to the provision of public goods, several mixed models are available. The touchstone of reforms is, therefore, improved efficiency which comes from improved competition. The emphasis on efficiency, however, does not exclude considerations of equity. If improved efficiency can lead to faster growth, that itself can generate larger surpluses in the hands of the government which can be utilised to increase social sector expenditures and provide better social safety nets. Much, therefore, depends on the rate of growth and how the surpluses generated are utilised.

What has been the record of India in terms of economic growth and social development in the post-liberalisation period? In the post reform period beginning 1992-93, the economy has grown at an average rate of 6.8 per cent. In the more recent period, the growth rate has been even higher. Over the decade beginning 2004-05, the average annual growth rate has been 7.6 per cent. Between 2005-06 and 2010-11, the growth rate was 8.7 per cent. Contrast this with the annual growth rate of 3.5 per cent between 1952 and 1980.

Poverty reduction

It is true that the Indian economy grew between 1980 and 1990 at 5.6 per cent. But the economy faced its worst crisis in 1991-92 and the growth rate fell to 1.0 per cent. It is extremely doubtful if, without a change in the strategy of development, growth would have picked up again.

Social development has many dimensions. One composite indicator is the behaviour of the poverty ratio. However, over years, there have been some changes in the methodology for measuring poverty. That growth has a favourable impact on the poverty ratio is seen even from recent data. The annual rate of growth of per capita income in the period between 1993-94 and 2004-05 was 4.3 per cent and the growth rate for the period between 2004-05 and 2011-12 was 6.7 per cent. The annual decline in the poverty ratio in percentage points (according to the Suresh Tendulkar committee's methodology) was 0.74 in the first period and 2.18 in the second period. In fact, the finding that the decline in poverty was much faster in the latter period is valid irrespective of where the poverty line is drawn. Between 2009-10 and 2011-12, according to the Tendulkar Committee's methodology, the reduction in poverty ratio was 7.9 points. According to the Rangarajan Committee's methodology, it was 8.7 points.

Without doubt, the poverty ratio still remains high. However, what is important to note is that the faster the growth, the greater the reduction in the poverty ratio. To reduce the poverty ratio substantially and to improve our performance on other social parameters, the country needs to grow faster in a sustained way. Leaving aside these data, it is the high growth phase which witnessed the induction of several far-reaching social development programmes such as the rural employment guarantee scheme and extended food security scheme. Social and community service expenditures of the central and State governments, taken together, increased from 5.3 per cent of GDP in 1990-91 to 7 per cent of GDP in 2013-14.

GST, reforms in agriculture

Given the favourable impact of reforms on growth, what should be the focus of reforms in the coming years? The objective of reforms is to improve efficiency through enhanced competition. The introduction of the Goods and Services Tax (GST) will be a step in the right direction, as it will help in enhancing efficiency. 'Acquisition' is against the spirit of competition and the reach of any Land Acquisition Act must therefore, be limited. At the same time, we should avoid fixing the price of land. Farmers have become fully conscious of the value of their land. They are unlikely to sell them at throwaway prices.

There are still some segments of the industry which are subject to a number of controls of the pre-1991 type. A typical example is the sugar industry. Molasses are subject to a type of control which results in a subsidisation of the liquor industry. The basic principle underlying liberalisation is of the need to create competitive markets with minimal barriers to entry and should be extended to all sectors. Pricing of natural resources has become an issue. In the absence of competition, transparent mechanisms for fixing the prices must be followed which will be fair to both the producers and the end users.

Among the sectors that have remained untouched by reforms, the most important is agriculture. Even as much remains to be done to improve agricultural productivity through scientific research and improved dissemination of knowledge, there are areas like marketing where reforms are badly needed. The present marketing arrangements, particularly with respect to vegetables, are archaic. Barriers to movement of trade across the country must be brought to an end.

Reforms do not necessarily translate into growth. The policy framework that gave our country an annual growth rate exceeding 9 percent between 2005 and 2008 was very much in place when our economy witnessed a substantial slowdown post 2011. Reforms are at best a necessary condition for growth. They are not sufficient. The investment sentiment must be carefully nurtured. The investment climate is a function of several factors. We should not forget that non-economic factors also play a key role.

Equally, growth does not automatically result in increased social sector expenditures. There has to be a definite policy focus. Social sector expenditure must be prioritised to reflect the needs of the society. The administrative framework and delivering systems must be such as to maximise benefits. Efficiency in the use of resources is critically important. This is where good governance comes in.

Reforms, to be credible, must not only result in higher growth but also benefit all sections of society. Government must therefore, pursue a two-fold strategy: of accelerating growth through an appropriate reform agenda and deploying the surpluses generated through growth to augment social welfare.

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