Impact of Economic Reforms

Indian Economic Reforms
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Indian Economic Reforms edited by Raghabendra Jha is a sincere attempt to bring academic rigour and intellectual insight to analyse the multidimensional character of the reform process. The book enriched with contributions from academia, practioners and policy-makers goes beyond a routine treatment of the subjects considered, to theoretical conceptualisation and empirical assessment of the underlying hypotheses of them. Though the volume has technical information built into most of its chapters, it has something to offer the technical novice too. The pieces by Jha, Chand and Sharma on 'The Fiscal Constraint on India's Economic Growth' especially brings out succintly and in a non-technical manner the perils of a burgeoning fiscal deficit. The authors have gone to the extent of saying, "Indeed success or failure in this area may well dictate the prospects for success of the reforms themselves" (p 162). Again in the chapter on, 'A Perspective on Saving, Investment and Macroeconomic Policies in India in the 1990s', Mridul Saggar provides a perfect blend of empiricism and analytical rigour. The section on measurement problems and estimates of saving and investment estimates in India is quite informative and provides conceptual clarity to the readers.

The book has twenty chapters organised into four parts, apart from an introduction to the volume by the editor. Each part in the volume deals with a particular sector of the economy. Broadly they are: financial sector developments, the industrial sector, India's exposure to the global economy and sectoral and regional issues.

The first section of the book consists of seven papers on monetary and financial sector developments in the aftermath of the reforms. The chapter 'Monetary Regimes in India' by Warwick McKibbin and Kanhaiya Singh argues that an important issue currently facing India is the choice of an appropriate regime for conducting monetary policy. As the authors put it, "the problem facing the monetary authorities is to choose an appropriate instrument and intermediate target/targets, and a rule defining their interrelationship. This is what constitutes the regime of monetary policy" (pp 18-19). The chapter summarises the state of the current policy debate on selecting a monetary regime for India, and presents estimates of the impact of alternative monetary regimes, in the face of a variety of shocks. The authors use the Indian version 44M of the MSG2 multi-country model developed by McKibbin and Singh. The MSG2 is a "fully specified dynamic intertemporal general equilibrium model (DIGEM) with careful treatment of stock-flow relations such as the accumulation of investment into capital stocks and accumulation of fiscal deficits into net asset stocks" (p 22). Under three alternative policy regimes, viz, a money target, inflation target and nominal income target, the impact of shocks to aggregate demand, supply and risk perceptions has been studied. The authors' finding while considering adjustment to shock is: "the inflation target regime works quite poorly in terms of output volatility for permanent demand shocks, both permanent and temporary supply shocks and shock to risk perceptions which is quite instructive from a policy perspective" (p 47).

The chapter, 'On the Endogenity of the Money Multiplier in India' by Raghabendra Jha and Deba Prasad Rath is a pioneering attempt to study the money multiplier along the post-Keynesian tradition. The authors question the heroic assumptions that justify the stability and predictability of the money multiplier, especially in a deregulated financial structure where interest rates are free from the shackles of administrative fiat. They argue that the endogenous money multiplier framework is best suited to analyse the money supply process in India. Employing sophisticated econometric techniques to the theoretical construct, the authors conclude, "Money multipliers in India have been endogenous particularly since the reforms".

Amitava Sarkar, Kalyan Roy and Soumitra Mallick, in their chapter ‘Financial Fragility in Indian Stock Markets: The Decade of the Nineties’, study the long-term properties of the Indian stock market on two counts: First how stock prices are related to fundamentals and second the estimation of the extent to which bubbles are present in stock market data. The authors use cointegration techniques to model the behaviour of Indian stock markets in the aftermath of the reforms. Apart from structural modelling, the chapter examines the financial fragility of Indian stock markets and attempts to identify periods of crises in stock markets. The study reveals that stock price is an important consideration in making corporate decisions. The authors conclude, “Planned competition has been responsible in preventing markets from crashing more often, and in changing the overall structure of the interplay between price formation, history and expectations along with it”.

In his chapter, ‘A Perspective on Saving, Investment and Macroeconomic Policies in India in the 1990s’, Mridul Saggar examines the behaviour of savings and investment aggregates for the Indian economy. The gains in private saving were largely the result of financial deepening. The author observes that the failure of fiscal reforms to keep pace with the wide-ranging reforms may have been largely responsible for limited gains in saving and investment. A sharp decline in the public saving rate during the reform period has contributed to a rise in the private saving rate, but the rise failed to fully compensate for the fall in the public saving rate resulting in a lower overall gross domestic savings rate than what have been the case if fiscal reforms had progressed at the desired pace.

In the chapter on ‘Macroeconomics of Credit: An Indian Perspective’ Deba Prasad Rath and Dhritidyuti Bose provide a credit model for India. The time series model estimated for the reform period shows that industrial output continues to exert a predominant influence on credit demand and supply. Credit-output relationship is shown to be bi-directional. The authors have revisited the debate surrounding the use of credit as an intermediate target for monetary policy. The empirical exercise in a VAR framework pursued by the authors drive them to the conclusion, “As, such usefulness of credit as an intermediate target seems to be rather limited”. The chapter concludes with the observation, “From the policy angle, credit turns out to be as weak a target variable as money”.

The second section of the book deals with the industrial sector of India. Using company level data for the engineering industry, in the chapter, ‘Technology Productivity and Export Growth of Engineering Industry in India’ Anita Kumari models the determinants of export performance. Using panel data techniques, the author finds that productivity growth had a positive impact on export growth in both periods, but that this was particularly so in the post-reform period. However, the use of as many as 13 variables as affecting exports goes against the fundamental principle of parsimony in econometric modelling. The use of a simultaneous framework would have had more intuitive appeal. The period of analysis has been confined to the year 1995 and, as such one gets only a brisk flavour of the impact of reforms and it is not certain whether the results would hold in subsequent years. The results obtained can be treated as early signals and need to be corroborated with an extended period of analysis.

The impact of structural adjustment programmes on corporate investment is a much discussed and debated topic in the public as well as policy circle. Prema-Chandra Athukorala and Kunal Sen, in their chapter ‘Liberalisation and Business Investment in India’, have addressed this issue by modelling business investment in India. The results suggest that the level of capital stock and rental cost of capital are important determinants of business investment, along with changes in output and public investment. A decline in the rental cost of capital and better growth performance could together negate the adverse impact of a decrease in real bank credit and the slowdown in the growth of public investment in the period 1991-95. The net impact of the reforms on corporate investment consequently is found to be positive. Though the analysis is quite enriching, the authors could have extended their analysis to the second half of the 1990s.This would have enabled one to discern the impact of growth fatigue of the late 1990s on corporate investment.

Bhagwn Dahiya and Desh Gupta in their chapter, ‘The Current State of Corporate Governance in India’, argue that India was slow in moving towards changes in corporate governance in the early part of the post reform period, despite a higher number of scandals. But starting from 1997, with the introduction of the SEBI Takeover Code, reforms have been introduced first through the CII’ Voluntary Code and then through the implementation of the recommendations of the KMB Committee. These have set in place a code of corporate governance moving India's corporate governance regime from one that is dominated and monitored by insiders, and towards the Anglo-Saxon model, which seeks an arm's length relationship. The conflicts of interest are clearly highlighted and an attempt is made to resolve them, but problems of corporate governance remain particularly in the area of implementation.

Rashmi Banga in her chapter 'Do Productivity Spillovers from Japanese and US Firms Differ?' undertakes a comparative assessment of the impacts of FDI from Japan and the US on the Indian economy. The chapter is built on certain hypotheses of the impact of FDI and the author draws her inferences from empirically testing them. The chapter is a must read with a number of insights which may come handy while formulating a strategy to attract FDI. The most important one is that Japanese equity has a significant positive impact on the total factor productivity growth of domestic firms but US equity has no significant effect.

The next section deals with sectoral and regional issues and consists of four chapters. In their chapter, 'Growth in India's State Economies before and with Reforms: Shares and Determinants', Shashanka Bhide and Ric Shand describe the characteristics of economic growth for 14 major states of India, during the period 1993 to 1999. The chapter discovers patterns in such growth and argues that the behaviour of determinants of economic growth across these states is broadly consistent with the observed pattern of growth in their state domestic products. The chapter also examines the role of various constraints such as the fiscal deficit, quality of infrastructure in economic growth at the state level. However, the chapter is silent on the dynamics of income inequality across the states as is the case in a number of other studies.

Edgar Wilson's 'Testing Market Integration in Indian Agriculture' is an attempt to compare market integration in prices for selective agricultural commodities in the pre-reform and post-reform period. The author develops a simultaneous vector autoregressive model of non-stationary prices, which is estimated using Johansen's full information likelihood estimation techniques to derive efficient and consistent parameter estimates. The empirical findings suggest greater market integration in the post reform phase. The chapter also quantifies a short-run equilibrating price elasticity, which indicates the ability of individual markets to return to equilibrium when faced with short-term commodity price shocks.

In 'Indian Software Industry: Growth Patterns, Constraints and Government Initiatives', Chandana Chakraborty and Dilip Dutta discuss a host of issues like, the size and ownership of the Indian software industry, the degree of foreign participation and concentration without using much jargon. The export performance of this industry and national policy towards this strategic industry are also discussed in brief. The chapter also highlights some potential concerns like the negligible share of pre-packaged software in software exports and the underdeveloped domestic market for software. However, the authors are silent on charting out a possible course of action to overcome the present lacuna so as to improve India's competitive as well as comparative strength in software .

Raghabendra Jha and Prem Thapa in their chapter 'India's Infrastructure Sector' examine the spatial distribution of infrastructure services across India with a focus on the electricity sector. The chapter deliberates the association of output growth and the incidence of poverty with the availability of infrastructure facilities in major sates in the last two decades. The pricing of electricity across states and the problems faced by the State Electricity Boards (SEBs) has been dealt with in some detail by the authors. The authors, however, identify political compulsions as the true bottleneck for infrastructure reforms in India.

The final part of this book examines India's social sector and consists of three chapters. In their chapter 'Income Generation Programme and Empowerment of Women: A Case Study in India', P Basu and S Basu compare and contrast the effectiveness of NGOs and government organisations in programmes designed to generate income and empower women. They use a socio-economic case study in the district of 24 South Parganas in West Bengal involving a private NGO and a government organisation, both of whom were responsible for designing and implementing anti-poverty programmes. The findings reveal that "participation, partnership and member accountability", which characterised the NGO's development programmes have contributed to its greater success in empowering women as compared to the programme run by the government organisation. The study has the policy implication of further encouraging NGOs into development programmes and suitably designing government development programmes along more participatory lines.

In his chapter 'Are the Poor more Vulnerable to Income Shocks? An Analysis of Consumption Insurance in Rural India', Pushkar Maitra tests for insurance against income shocks in rural India. He examines the extent of consumption insurance against income risk by rural households in India. He estimates the effects of income changes on consumption, after controlling for aggregate shocks through changes in village level consumption and household size. Consumption regressions show that the null hypothesis of full insurance is rejected both for the population as a whole and for different land classes. Further, consumption tracks income more closely for poorer households, as compared to richer households. The analysis in this chapter is based on data obtained from the Additional Rural Income Survey conducted by the National Council of Applied Economic Research (NCAER) in three rounds for the years 1969, 1970 and 1971.The findings of the study, no doubt, are of practical relevance but are quite dated. To what extent the findings of the late 1960s should guide policy 30 years hence is debatable.

The book concludes with a piece by the editor on Rural Poverty in India. Apart from discussing poverty dynamics over the last five decades, it revisits the debate on the comparability of poverty estimates drawn from the 50th and 55th rounds of NSS data, which use different recall periods. In addition to intertemporal treatment, the chapter discusses the spatial variation in poverty and inequality over time. Apart from providing an occupational characterisation of the poor, it also discusses the socio-economic characteristics of the poor. There is a small but interesting section is on the reasons for the slowdown in poverty alleviation in the 1990s, in spite of better growth performance. More importantly, this chapter discusses the policy response to poverty reduction and provides the broad contours of a strategy for tackling rural poverty. Policy-makers can take a cue from the strategy outlined here while designing poverty reduction programmes.