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Economic Planning

Indian Development Strategy: From Planning to Reforms

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The first four decades of development strategy in India was characterized by the heavy regulation of the economy by the government. It was believed that the private sector in the economy either did not have the resources or the capacity and will to take on the big development projects needed to initiate development in a stagnant economy in the 1950s. However, by the late 1980s it was realized that the policies were not working and like many other countries India too switched gears from a Planned economic model to a one based on the primacy of the Markets and the private sector. The government, since the 8th Five Year Plan to the 12th Five Year Plan moved from a heavy-handed economic planning to an Indicative Planning. The centrality of the growth process is now well established in the development literature and the policy circles. Economic growth is now considered to be the primary driver of the development process with the state playing a redefined in the economy since the 1990s. The current development strategy combines a fine balance between the state and the market.

Keywords: indian development, economic planning, economic growth, economic reforms

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1. Introduction

Before the launch of economic reforms in 1991 the State was involved in various sectors of the economy. We had a largely controlled economy where the State played a crucial role not just in regulating the economy but also in producing goods and services. The private sector remained heavily regulated. The Industrial Policy 1956 defined the operational areas of the public and the private sectors. However, with the launch of market-oriented economic reforms in 1991 the private sector was allowed greater space and more freedom for its operation. The State remains an important force in the economy however it acts more as a facilitator than a direct producer of goods and services. Over the years the market economies have become increasingly complex – more interdependent, more interconnected and more sophisticated. Any development strategy uses both the state and the market to achieve the societal goals. When India achieved independence and started its conscious journey towards development with justice it called upon both the state and the market to act in unison to attain the desired goals. However, during the initial years it was the State that played a dominant role in the economy. The private sector was given a limited role particularly in the industrialization process. Economic planning was the main tool to affect the policies of the state. India had a poor industrial base at the time of independence. Millions of her rural people suffered under the weight of a traditional agrarian structure. A long period of economic stagnation, against the background of increasing pressure of population, followed by the burdens of the Second World War, had weakened the Indian economy. There was widespread poverty and want. This required a massive drive towards industrialization. The Second Five Year Plan provided an impetus to the accelerated development of the economy. However, after three decades of planning and well into the 1980s India failed to realize its economic potential. The country faced an economic crisis in the early 1990s. To stabilize the economy and speed up the tempo of accelerated change it adopted a set of policy measures called the economic reforms programme. These structural changes in policies provided a new foundation for economic development in the country.

2. Development and Economic Transformation

Development is often viewed as the transformation of the society. In modern economic literature development has been seen as synonymous with industrialization. Development has been defined as movement away from traditional modes of production, consumption and exchange to a more modern system characterized by advanced culture. Development a movement away from the traditional modes of existence to a more modern relation in production, exchange and consumption. Development brings about structural transformation in the economy. It changes the occupational structure in the economy with the rise of modern sectors that employ millions in various kinds of jobs and occupations. The transformation of a society requires a vision and a strategy which may differ in various stages of development. The experience of the past fifty years has demonstrated that development is possible, but it requires consistent effort to achieve and sustain it. It requires resources and their judicious application in desired channels of production and institution building (Stiglitz, 1998).

In his book,*Development as Freedom,*Amartya Sen defines development as the enhancement of freedoms that allow people to lead lives that they have reason to value. He says that development cannot be seen only as a sustained rise in per capita income of the population. He views development as expansion of freedoms and an increased investment in education and health to enlarge well-being of masses. He offers a critique of emphasizing development as extension of economic growth without corresponding improvement in the lives of the poor. He has given the capabilities approach to development and offers a more human development centric strategy of development (Sen, 1999).

We find that countries often move from a low industrial and economic base to a higher per-capita income through sustained growth of the economy. Getting economic growth is not easy. In the first three decades the Indian economy could grow only by 3.5 percent per annum. It was quite low compared to the expectations of Indian policy makers had set in the 1950s. after the launch of economic reforms in the 1990s the economy took off and registered an annual average per annum growth in excess of 6 percent signifying the success of the changed development strategy.

3. Economic Planning, State and the Market

India adopted a planned model of development in the early 1950s. In all it implemented twelve Five Year Plans. The last FYP ended in 2017 after which economic planning as practiced since early 1950s was officially discontinued. During the initial years after independence it was thought that the task before an underdeveloped country was not merely to get better results within the existing framework of economic and social institutions but to mould and refashion these so that they contribute effectively to the realization of wider and deeper social values. These values or basic objectives were summed up in the phrase *'socialist pattern of society'*. Essentially, this meant that the basic criterion for determining the lines of advance must not be private profit but social gain, and that the pattern of development and the structure of socio-economic relations should be so planned that they result not only in appreciable increases in national income and employment but also in greater equality in incomes and wealth. Major decisions regarding production, distribution, consumption and investment—and in fact all significant socio-economic relationships—must be made by agencies informed by social purpose.

The question facing the Indian planners was in what manner and how quickly the rate of capital formation in India can be stepped up, consistently with other objectives, from about 5 per cent of the national income to, say, about 20 per cent. The answer depended upon the rate at which the national income increased as development proceeded and the proportions of this increase which could be ploughed back into investment. The larger the proportion of the increments to national income that can thus be ploughed back into investment, the greater is the pace at which development can be accelerated and opportunities for further investments created (Lewis, 2013).

The Second Five Year Plan (1956-61) stated that whether one thinks of the problem of capital formation or of the introduction of new techniques or of the extension of social services or of the over-all re-alignment of the productive forces and class relationships within society, one comes inevitably to the conclusion that a rapid expansion of the economic and social responsibilities of the State will alone be capable of satisfying the legitimate expectations of the people. This need not involve complete nationalization of the means of production or elimination of private agencies in agriculture or business and industry. It does mean, however, a progressive widening of the public sector and a re-orientation of the private sector to the needs of a planned economy.

The First Five-Year Plan (1951-1956**)** made it clear that the role of private profit was at best limited. It stated the concept of private enterprise, as, indeed, of private property, is undergoing rapid change, and the view that private enterprise can function only on the basis of unregulated profits is already an anachronism. The process of reorientation should and is certain to continue and gather speed, and the problem is to see that the transition is smooth and orderly. Already, in certain spheres of industry, units owned publicly and units under private enterprise were functioning side by side. The points of interaction between private and public enterprise are multiplied rapidly. In the maintenance of industrial peace and the promotion of a cooperative outlook between capital and labour, the State has necessarily to play a vital role. All these indicated that the private and the public sectors cannot be looked upon as anything like two separate entities; they are and must function as parts of a single organism.

The Third Five Year Plan (1961-66) stated the growth of the corporate private sector over the past decade had brought to the fore the question of the means by which economic growth will be secured without concentration of economic power and the emergence of monopolistic tendencies. As a rule, the process of rapid economic development tends to enlarge opportunities for well-established firms to expand their size and enter new fields of enterprise. As compared to new undertakings or to smaller enterprises, they enjoy advantages in organization and expertise, in access to the capital market and ability to secure foreign collaboration and, generally, in the resources which they are in a position to deploy. The fact that a significant proportion of the resources available for investment in industry arises within the corporate sector itself is another factor which makes it easier for an existing unit to expand than for a new one to come into being and take firm root. In several industries technological considerations favour the setting up of large-scale units with resultant savings in capital cost and in the cost of production.

Consequently, certain difficult problems arise. On the one hand, to the extent to which large existing enterprises undertake development in accordance with the priorities set in the Five-Year Plans and avail of essential economies of scale, they assist the growth of the economy. On the other, excessive economic power in relatively few hands and the uses to which it may be put, disturb the balance of power in a democracy, expose the social structure to new strains and tensions, and come in the way of diffusion of economic opportunities.

4. Socialist Pattern of Society

The task before an underdeveloped country was not merely to get better results within the existing framework of economic and social institutions but to mould and refashion these so that they contribute effectively to the realization of wider and deeper social values. These values or basic objectives were summed up in the phrase 'socialist pattern of society'. Essentially, this meant that the basic criterion for determining the lines of advance must not be private profit but social gain, and that the pattern of development and the structure of socio-economic relations should be so planned that they result not only in appreciable increases in national income and employment but also in greater equality in incomes and wealth. Major decisions regarding production, distribution, consumption and investment—and in fact all significant socio-economic relationships—must be made by agencies informed by social purpose. The benefits of economic development should go to those who deserve the most. The under-privileged sections of society should be the first beneficiaries of the process of development. There should be a progressive reduction of the concentration of incomes, wealth and economic power. The challenge was to create a milieu in which the small man who has so far had little opportunity of perceiving and participating in the immense possibilities of growth through organized effort is enabled to put in his best in the interests of a higher standard of life for himself and increased prosperity for the country. The socialist pattern of society was not to be regarded as some fixed or rigid pattern. It was not rooted in any doctrine or dogma. Each country has to develop according to its own genius and traditions. Economic and social policy had to be shaped from time to time in the light of historical circumstances (Second Five Year Plan, 1956-61).

The Constitution of India, in its Preamble, and the Directive Principles of State Policy, has declared that it aims at securing for all its citizens justice in all its forms – political, economic and social; that the state through its policies must strive to ensure equality of opportunity and status; that the state should ensure the dignity and self-respect of individuals by creating a just social order. It should create livelihoods for all. The ownership of resources should be distributed in a way that ensures justice to all and avoids concentration of economic power. The state in India has been allocated a heavy role in the fulfillment of the social and economic objectives of the society.

5. Industrial Policy 1956

The IPR 1956 made changes in IPR 1948 and established the primacy of the State in guiding industrialization and promised to take the country towards establishing a 'socialist pattern of society.' It served as the cornerstone of India's development strategy. As the resolution put it, the adoption of the socialist pattern of society as the national objective, as well as the need for planned and rapid development, requires that all industries of basic and strategic importance, or in the nature of public utility services, should be in the public sector. Other industries which are essential and require investment on a scale which only the State, in present circumstances could provide have also to be in the public sector. The state has, therefore, to assume direct responsibility for the future development of industries over a wider area.

First, the Resolution classified industries into three categories. The **Schedule A**, consisted of industries the future development of which will be the exclusive responsibility of the State. The future development of these industries was reserved for the public sector. In this schedule 18 industries had been kept. They were of basic and strategic importance. Further, they needed enormous capital for their development. The government reserved special control on these industries. In **Schedule B**, were industries which were to be progressively state-owned and in which, therefore, the State will generally take the initiative in establishing new undertakings, but in which private enterprise will also be expected to supplement the effort of the State. There were 12 industries under this category.

The third category comprised all the remaining industries, the further development of which will, in general, be left to the initiative and enterprise of the private sector. the state would encourage the development of these industries. The prime consideration determining State policy over the whole industrial field was promotion of rapid development in keeping with the overall objectives defined. The public sector had to rapidly grow and the private sector had to conform to the requirements of the Plan.

Second, it was considered essential to accelerate the rate of economic growth and to speed up industrialization process to develop heavy and machine making industries to expand the public sector and to build up a large and growing co-operative sector. These provided the economic foundations for increasing opportunities for gainful employment and improving living standards and working conditions for the mass of the people. Equally, it was considered urgent, to reduce disparities in income and wealth and prevent private monopolies and the concentration of economic power in different fields of the economy. Accordingly, the State had to progressively assume a predominant and direct responsibility for setting up new industrial undertakings and for developing transport facilities. It also undertook State trading on an increasing scale. At the same time, as an agency for planned national development, in the context of the country's expanding economy, the private sector had the opportunity to develop and expand provided private interests did not collide with public interest. The adoption of the socialist pattern of society as the national objective, as well as the need for planned and rapid development, required that industrialization be guided by state. The State therefore assumed direct responsibility for the future development of industries over a wider area.

Third, the distinction between the public and the private sector was one of relative emphasis, explained the plans. The private enterprise should have a public purpose and there is no such thing under present conditions as completely unregulated and free private enterprise. Private enterprise was to function within the conditions created by the State. Apart from the general protection that the State gave by way of the maintenance of law and order and the preservation of the sanctity of contracts, there were various devices by which private enterprise derived support from the Government through general or special assistance by way of tariffs, fiscal concessions, and other direct assistance.

Four, the policy endeavored to the development of the **Cottage and Small-Scale industries** by taking appropriate policy measures like restricting the volume of production in Large scale industries, cheap electricity, credit support, marketing facilities etc.

Five, a top priority of this industrial policy was to support the development of the industrial and agricultural sector in all the regions of India and work towards the **reduction in regional disparities** in development. To achieve this goal infrastructural and other support were pledged to the backward regions of the country.

Six, India remained committed to a closed-door policy towards **foreign capital** as it was seen as an extension of imperial power. It indeed collaborated with other countries for the development of power, steel and other plants but large scale foreign direct investment was disallowed and it was decided that domestic resource mobilization should ultimately provide the support to investment and capital accumulation.

The first four decades of economic planning in India led to the industrial diversification and infrastructural development. However, agriculture continued to serve as the mainstay for millions in need for jobs. The pace of change was slow and the economy could grow annually only at a modest rate of 4 percent per annum between 1950 and 1990. The manufacturing sector could contribute only in the range of 10-15 percent to the GDP. To combat poverty and regional backwardness India the government did take a lot of steps however poverty remained endemic and gainful employment limited to those skills and know-how.

Arvind Panagariya has argued that the policies failed to produce widespread development in the economy in the first four decades. In the same time period countries in Southeast Asia transformed from a rural economy to a more modern economy by benefitting from international trade and a more market-oriented economic policies.

By the late 1980s India was afflicted with twin crises – a widening fiscal deficit and a Balance of Payments (BoP) – which left India with no option to but to change of economic strategy.

6. Economic Reforms

The **economic reforms** programme had two components – **structural reforms** and the **stabilization policies**. The reforms were introduced in many sectors of the economy however the Industrial policy saw the biggest change. Licensing was abolished and attitude towards foreign capital became more benign. Many industries that were earlier reserved for the public sector dereserved and the private sector was allowed a much greater participation in the economy. The exchange rate policies were made more flexible whereas the tax rates were reduced. The stabilization policies attempted to control the high inflation and bring the widening fiscal deficit under control. The emphasis on the centrality of economic growth was accepted. It was finally realized that there could be no sustained welfare without accelerated economic growth. (Panagariya, 2008; Bhagwati and Panagariya, 2013)

The macroeconomic crisis had three aspects:
a. Fiscal imbalance
b. Fragile Balance of Payments situation
c. Inflationary pressures

The crisis made economic reforms necessary. It emphasized on demand and supply side measures-

A. Macroeconomic management – Demand Management
a. Control of Inflation
b. Fiscal adjustment
c. Balance of Payment adjustment

B. Structural Reforms – Supply-side Management
a. Industrial Deregulation
b. Trade and Capital flows reforms
c. Financial sector reforms
d. Public sector reforms and Disinvestment

7. The Triumph of Economic Growth

Growth rates differ substantially from nation to nation. Some societies achieve higher and faster economic transformation while others are trapped in vicious cycle of poverty.

The Southeast Asian nations like South Korea, Singapore, Hong Kong, Taiwan and lately China and India have registered sustained increase in their per-capita GDP and witnessed tremendous improvement in their living standards thanks to the positive effects of faster economic growth. These nations have moved from the ranks of being among the poorest in the world to being among the richest.

The experience over the past few centuries suggest that economic growth is the most powerful engine for generating long term prosperity and raising living standards. The fact of the matter is that the record of last quarter century demonstrates two points: Aggregate economic growth benefits most of the people most of the time; and it is usually associated with progress in other social dimensions of development (Stiglitz and Squire, 1998).

It has been argued using long term data on economic growth and development over the past few centuries the 20the century has been the most productive in terms of improvement in material welfare and raising the standard of living of the masses. The pace of economic growth has substantially lifted many people out of poverty. (Delong, 2000).

Some economists have argued that redistributive policies come after some growth has been achieved in the economy. There can be no redistribution without sufficient economic growth in the economy. The poor countries that aspire to remove poverty should focus first on getting growth going in the economy. Economic growth encourages poverty reduction two important ways: sustained economic growth pulls up the poor out of poverty be providing gainful employment; and second, higher economic growth generates revenues for the state that can be used for the operation of welfare schemes for the poor. (Bhagwati, 1998, 2007).

Adam Smith forcefully argued against the prevalent mercantilist folly and showed the merits of free exchange of goods to a society’s wellbeing. In his view consumption was the sole end of production, and ill-founded and counter-productive regulations checked the expansion of commerce and trade, so essential to raise living standards, thus reduced material prosperity. He further argued that the productive capacity rested on division of labor, and accumulation of capital facilitated the former. And that just as individuals gain from specialization so do nations so restrictions on international trade inevitably make both nations poorer.

Smith was no advocate of big government interventions in the economy but believed that market economies could prosper only when property right were secure and contracts honored, and when government acted as a facilitator by ensuring justice, maintaining peace and tranquility and, by undertaking public works to support markets. (Smith, 2002).

A society which is not growing is stagnant. A society which is on a higher growth path is more likely to raise the standard of living of its citizens, foster greater opportunities, generate greater resources for the government and, promote faster social mobility in contrast to a slowly growing economy. By increasing a nation's economic wealth, it enhances its potential for reducing poverty. Economic growth – meaning a sustained improvement in the standard of living for a clear majority of its citizens – has been the magic wand helping nations solve some of the most pressing socio-economic and political challenges of the day. Economic growth bears moral benefits as well. There is greater likelihood of promotion of political freedom and civil liberties in countries with rising income. (Friedman, 2006).

In the past quarter a century economic betterment has heralded an era of political progress. The number of democracies in the world is on the rise. In principle this is very much in consonance with the broader meaning of development which includes both economic and political progress. Therefore, it becomes important that when we discuss about the merits of liberal market friendly policies we consider these moral positives as well. The contention is that we must not measure the benefits of faster growth in purely economic terms but any accounting must also consider other political and social gains as well. Why do nation with rising income tend to gravitate towards democracy? The logic seems to be that with rising income level the ever-expanding middle class press for basic political freedom and civil liberties widely recognized and a fundamental element of advanced market democracies. The pressure on China to liberalize its control over its political institutions has been gaining ground. The Southeast Asian nations have moved towards openness and freedom, however slow that might have been.

8. Conclusion

The first four decades of development strategy in India was characterized by the heavy regulation of the economy by the government. There was an economic logic behind this line of economic reasoning in policy making. It was believed that the private sector in the economy either did not have the resources or the capacity and will to take on the big development projects needed to initiate development in a stagnant economy. However, by the late 1980s it was realized that the policies were not working and like many other countries India too switched gears from a Planned economic model to a one based on the primacy of the Markets and the private sector. The government, since the Eighth Five Year Plan to the Twelfth Five Year Plan moved from a heavy-handed economic planning to an *Indicative Planning*. The government today is more active in a different sense. The regulatory burden on the economy has been reduced. But the government runs plenty of welfare schemes for those who insufficiently benefit from the growth process. The centrality of the growth process is well established in the development literature and the policy circles. Economic growth is now considered to be the primary driver of the development process with the state playing a redefined and an active role. As feared in the 1990s the neoliberal policy regime – with its emphasis on private initiative and open economy - has not led to the withdrawal of the state from the economic sphere. After the Twelfth Five Year Plan economic planning has been completely discontinued. The current development strategy combines a relatively fine balance between the state and the market. We have witnessed accelerated development along many dimensions in the last few decades particularly since the early 1990s. The current development strategy with its emphasis on the private initiative and economic freedom has paid rich dividends. So far as acceleration in the pace of development is concerned it is working. The emphasis on private sector, foreign capital, outward-oriented trade policy which are the essential features of the current development strategy has come to the rescue of the Indian economy that faced a crisis in early 1990s. However, the country continues to underinvest in health and education. Likewise, job creation lags behind the number of entrants to the labour force creating a situation of persistent unemployment, and inequality is on the rise too. This calls for a rethink on our spending priorities and a more emphatic implementation of the pending economic reforms.

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