Thursday, 3 December 2020

Backstage

Prologue

- In a country with a history of over 3000 years, there is always a danger of overestimating the importance of individual events. Nevertheless, I believe the acceleration of economic growth that occurred in India between the early 1990s and the late 2000s was of crucial importance. India's GDP grew at over 7 percent per annum in real terms from 1993-94 to 2011-12 and poverty declined from 37 percent in 2004-05 to 22 percent in 2011-12
- From the late 1960s through the '70s, the growth performance of the Indian economy deteriorated while other countries in Southeast Asia fared much better. And yet, surprisingly, there were no voices in India advocating or demanding change - not civil servants, not academics, not the press, and not even Indian industry. They all saw that economic performance was not satisfactory but they did not view this as a consequence of the strategy deployed. They knew the public sector was performing very poorly and soaking up a lot of resources instead of generating surpluses for investment, but they saw the solution as pushing the government to somehow make the public sector more efficient. They could see that export performance was consistently falling short of targets, but they did not see the link between poor export performance and the import substitution strategy. That strategy raised the domestic cost structure and created an environment in which businesses would lobby for more protection from import competition rather than strive to lower costs to build export competitiveness
- In 2010, India moved out of the group of low-income countries as classified by the World Bank and into the group of middle-income countries, albeit at the bottom end

Development in Practice

- Turkey and Malaysia were two developing countries with a much higher level of per capita income than India. Both were significantly more open economies with much lower levels of trade protection and a policy of welcoming FDI. Both had governments that were proactive but encouraged private sector activity much more than we did. Both countries also had a much better economic performance than India in the 1970s
- A significant positive development in the late 1960s and early 1970s was the Green Revolution, which enabled India to become self-sufficient in foodgrains.

This was recognized globally as a major achievement, disproving the forecasts of the Club of Rome that India would not be able to feed herself and was too large to be fed by the rest of the world. The political credit for the success of the Green Revolution must go in large measure to Mrs Gandhi, who took bold decisions in the late 1960s to make it happen

- While the country's success in achieving food self-sufficiency was applauded, its failure to reconfigure policy for the industrial sector remained a point of criticism. This was widely used to explain India's poor growth compared to other countries. The original East Asian 'Gang of Four' (Korea, Taiwan, Hong Kong and Singapore) experienced rapid growth in the 1960s, at about 9 per cent per annum. By the 1970s, the Southeast Asian countries were also taking off. Growth in Malaysia, Indonesia and Thailand accelerated from an average rate of 5.9 percent in the 1960s to an average of 7.6 percent in the 1970s, but India's growth decelerated from 4.2 percent in the 1960s to 2.9 percent in the 1970s

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Coming Home

- Young people today are used to a variety of cars on offer, with easy financing and manageable monthly payments. In 1979, there were only two choices: the bulky-looking Ambassador, an updated version of the old British Morris Oxford of the mid-1950s, produced by Hindustan Motors; and the smaller and sleeker Padmini, based on the Italian Fiat Millecento of the late 1950s, produced by Premier Automobiles
- The extent of overstaffing was a culture shock. I had a personal assistant, or PA, who took phone calls, typed and managed my appointments, an office clerk who assisted him, and a peon who performed miscellaneous functions such as carrying files from office to office and carting my briefcase to and from my car to the office
- India's initial growth experience in the Nehruvian period from 1950 to 1965 at 4.1 percent per annum was much better than the 1-1.5 percent growth experienced in pre-Independence times, although it was below the target of 5 percent. It is during the period after Nehru, from 1965-66 to 1979-80, that growth slowed down to an average of only 2.9 percent. This was not only lower than in the earlier period but much worse than what was being achieved by many other developing countries in the 1960s and 1970s. In retrospect, the failure to rethink policies to identify the reasons for low growth was a major mistake. China had started to rethink its policies with agricultural reforms of 1978. We should have had a similar rethink. Mrs Gandhi did that for agriculture with great success with the Green Revolution, but not for industry

- Other countries also had public sector enterprises but did not view the private sector with great suspicion. They also had a much more promotional approach to exports, looking out for sectors with export potential and encouraging them to exploit export markets. While we were a large economy in terms of population, the size of our domestic market in most industrial products was quite small. Production aimed at the domestic market would not permit economies of scale
- We also had major deficiencies in human resource development but I was less conscious of these at the time. They came to be widely recognized as a weakness from the late 1980s onwards, thanks to the energetic work of Amartya Sen. The problem had been highlighted even earlier in 1955 by Milton Friedman of Chicago University when he visited India as part of a programme in which distinguished foreign scholars came to India to advise the Government. Friedman had observed that we gave too much importance to the deficiency of capital and not enough to the deficiency of human skills. His memorandum to the Government of India emphasized that 'the fundamental problem of India is the improvement of the physical and technical quality of her people… the weakening of rigid social and economic arrangements, the introduction of flexibility of institutions and mobility of people, the opening up of the social and economic ladder to people of all kinds and classes'. All these issues came on to the policy agenda with great force only much later

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Indira Gandhi Returns to Power

- A new Industrial Policy was announced in July 1980, which reaffirmed the Industrial Policy Resolution of 1956 and the Government's commitment to the public sector. The sense that nothing had changed was intensified by the fact that six private sector banks that had grown in size were nationalized in 1980. It looked like we were back to 1969, when 14 large private banks were nationalized
- The establishment of Maruti Udyog Ltd (MUL) in the public sector was a significant - and fortuitous - development that helped change attitudes on many important aspects of industrial policy. MUL was established because Mrs Gandhi wanted to set up a public sector company to realize Sanjay's dream of producing an affordable people's car
- Several aspects of the MUL experience had implications for industrial policy as it evolved. One was the need to be realistic about the scope for indigenous design. Krishnamurthy made it plain to Mrs Gandhi that we could manufacture the car indigenously, but not design it. She accepted his advice and he began looking for collaborators. This also opened the door to a more relaxed approach to the import of foreign technology in other sectors

- Suzuki initially preferred a licencing agreement with parts being supplied from Japan. Krishnamurthy insisted on 26 percent equity, with an option to go up to 40 percent later, because he felt that only a substantial equity stake would ensure Suzuki's long-term interest in the JV. The partnership agreement was also structured so that some key decisions could only be taken with the consent of the foreign partner. Krishnamurthy later told me that he did this explicitly to insulate the company from whimsical political interference, a perennial danger for a public sector company

- The experience with Maruti also highlighted the inflexibility of import licencing. When MUL moved from assembling cars based on completely knocked-down imports to indigenous production under a phased manufacturing programme, they needed to put equipment in place for the next stage of manufacturing. When they asked for a licence to import the equipment to machine the engine block, Hindustan Machine Tools, another public sector company, persuaded the Directorate General for Technical Development (DGTD) that the import licence should be denied as they could supply the machines needed, just as they had done for the engine block for Bajaj scooters. The matter had to be resolved by Minister of Industries N.D. Tiwari in a meeting R.C. Bhargava, managing director of MUL, later told me he had arranged to physically bring the engine block of a Bajaj two-wheeler and the engine block of the Maruti car into the room to let everyone see how different the two products were! MUL finally got the licence, but the episode illustrates the arbitrariness inherent in the system. The flexibility shown here helped the case for a more relaxed administration of the regime

- MUL succeeded beyond expectations. The first car rolled out in 1983 and was an instant success, clearly out-competing the Ambassador and the Premier Padmini. It also went on to usher a revolution in component development, producing an impressive component supplier base that was later able to export auto components and meet the demands of new automobile manufacturers that entered the market in the 1990s

- The licencing system was as complex as could be. Imports of finished consumer goods were completely banned, except when brought in as baggage by returning travellers. It was a familiar sight to see long queues at the customs counter at the airport, of returning Indians declaring eletronic goods including TVs, tape and video players, air-conditioners and even electronic calculators! The ban on imports meant domestic producers of those consumer goods enjoyed near-infinite protection. Consumers were obviously the major victims, paying high prices for low-quality consumer goods

- Machinery or capital goods not produced in India were on the 'open general licence' (OGL) list and could be freely imported without a licence, but those

produced in India were on a restricted list and needed an imported licence. Some raw materials (metals, ores, crude oil, petroleum products, fertilizers etc.) could be imported only by state agencies, which then supplied the materials to the users. Other raw materials, intermediate inputs and components either on OGL and therefore freely importable or on a 'restricted' list requiring an import licence. Further, licences were given only to 'actual users', not traders

- The DGTD based its advice on two key considerations: the indigenous availability angle, i.e. whether the item was available from a domestic producer, and the essentially angle, i.e. whether it was really needed. There was a high degree of arbitrariness in the decisions. A manufacturer of electronic irons wanted to import a particular grade of stainless steel. Domestically produced steel sheets were too thick and would make the iron too heavy. Import of thinner sheets would have been readily allowed if the production of electric irons was for exports, where quality was acknowledged to be paramount, but it was felt the domestic consumer could make do with a heavy iron. No one seemed bothered that the domestic producer would never gain credibility to market his product internationally if his general production line was deemed substandard!

- Imports cleared from the indigenous angle could still be rejected because they were not essential. For example, import of sophisticated instrumentation equipment not produced domestically could be deemed to be not essential because the DGTD 'felt' it would not lead to much improvement in the quality of the output. The system was highly non-transparent with enormous scope to get a favourable ruling from the DGTD. Having got licenses for import of raw material, many producers found it more profitable to sell the material in the black market than use it as input in their production

- The system was particularly unsuitable for areas where technology was changing rapidly. N.R. Narayana Murthy, the iconic co-founder of Infosys, told me of his personal experience in 1983, when Infosys wanted to import a Data General MV / 8000 computer, with three removable disk drives with a capacity of 200 MB each. They had to make several trips to New Delhi to get the import licence. By the time they got the licence, a new disk drive with a capacity of 300 MB had become available, 30 percent cheaper. Naturally, they wanted to import the latest model. However, the original licence specified the model number and several additional visits to Delhi had to be made to modify the licence. In an area where technology was changing rapidly and timely delivery of export orders was crucial, long delays in getting equipment was fatal for exporters

- The Swraj Paul episode revealed a fault line in Indian capitalism because families were controlling large industrial empires with very little equity stake. The fact that they were able to refuse to register changes in ownership of shares with impunity

also revealed weakness in the regulatory framework of the capital market. These weaknesses were finally addressed 10 years later, when an independent statutory regulator of the capital markets was established and the markets opened up to foreign institutional investors (FIIs)

- I had underestimated the professional satisfaction I would get from working in my own country. While there was frustration at the slow pace, I had a much better appreciation of the difficulty in bringing about change in a large and highly diverse country working within a democratic environment

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Reaching for the 21st Century

- Unlike his senior cabinet colleagues who were full-time politicians and had never held a regular job, Rajiv Gandhi had worked as commercial pilot in Indian Airlines. I thought this gave him a better understanding of how to work with professionals. He respected technical expertise and was aware of the importance of new technology and the need for training. He was licenced to fly Fokker aircraft and was about to start training to fly jets when he left his job and joined politics
- It was after the Kalahandi visit that Rajiv made his much quoted remark that out of every rupee spent by the Government to help the rural poor, only 15 paise actually reaches them. Many journalists assumed his statement was based on inputs provided by me but it was based entirely on his personal impressions. A few years later, Kirit Parikh, a distinguished economist who later served as a member of the Planning Commission, carried out an empirical study of the Public Distribution System (PDS) to work out how much actually reached the poor. His estimate was 22 paise out of every rupee spent, not far from the PM's off-the-cuff assessment!
- The first two Budgets of 1985-86 and 1986-87 saw significant progress in tax reforms. The maximum rate of personal income tax was reduced from 62.5 percent (including surcharge) to 50 percent. While the trend for reduction in tax rates had begun some years ago, the reduction was much sharper this time. The corporate tax rate had stayed at 55 percent for many years and was now reduced to 50 percent. These rates were still high compared to the maximum marginal rates in other countries, but they signalled a new turn
- Indian industry's attitude to liberalization was self-serving. They wanted reduced controls over private investment but were ambivalent on import liberalization. They wanted liberalization of imports of machinery and inputs for their own production but not of imports that would compete with what they produced
- As an experiment, top private sector managers were brought in to run public sector companies. Rajan Jetley was brought in from ITC to run Air India, and

Sudhir Mulji of Great Eastern Shipping Company to run the State Trading Corporation of India. Jetley improved the financial performance of the airline but returned to the private sector after three years. Mulji resigned in two years. Mulji told me that as a businessman, he found it impossible to function given the many controls exercised by the ministries

- Five years is too short a period to bring about major structural reforms

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The Crisis of 1990

- The installation of a National Front government at the end of 1989 marked a significant change - the country went from five years under a Congress government with a large majority in Parliament to a minority government dependent on outside support from the Left and the BJP. The Front itself was a coalition of several parties, held together only by a common anti-Congress sentiment. The arrangement had all the ingredients for political instability and could certainly not handle an economy sliding towards a BOP crisis. Political developments occupied centre-stage throughout the year and as politics usually eats economics for breakfast, economic management was neglected. Problems that should have been tackled almost immediately were neglected. In less than a year, the Government was overwhelmed when the Gulf War in August 1990 triggered a full-blown BOP crisis
- Damning an idea by putting an IMF or World Bank label on it was common practice. I would not have minded criticism of the substance of my proposals because these could be examined rationally, but being criticized just because what I was saying had some resemblance to what the World Bank was also saying was both irrational and irritating
- In May 1991, Finance Minister Yashwant Sinha authorized the State Bank of India to sell 20 tonnes of gold from the Government's stock of confiscated gold to the Union Bank of Switzerland with a provision for repurchase within six months. He also authorized negotiations for pledging 47 tonnes of gold from the gold reserves as collateral for a loan of $600 million from the Bank of England and the Bank of Japan. The actual transaction, however, was completed after the new government took office. Though the Chandra Shekhar government was criticized for 'selling the family jewels', these were actually bold decisions indicating that the Government was willing to take unpopular steps to stave off default. Dr Singh later went out of his way to praise Sinha for this action because it created credibility that India could take tough action if necessary. The Bank of England and the Bank of Japan, somewhat humiliatingly, insisted that the gold pledged with them should be physically shipped to the Bank of England vaults in London! The RBI was one of the authorized depositories for holding some of the IMF's

gold. Years later, Camdessus told me he was advised that perhaps the small part of the IMF's gold that was held with the RBI should be withdrawn. To his credit, he turned down the suggestion as he felt it would send the wrong signal

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1991: Seizing the Opportunity

- The first step in responding to the crisis was the announcement on 1 July 1991 that the rupee was devalued by 9 percent. As commerce secretary, I was not in the loop about the decision. But I had no doubt it was the right step, though 9 percent seemed too little. Two days later, a second devaluation took the cumulative depreciation to about 19 percent - a much more reasonable adjustment to deal with the BOP crisis
- Devaluation was a politically sensitive decision in most countries in the days of fixed exchange rates because the value of the currency in foreign exchange was often confused in the public mind with national honour. This was particularly so in India, given the unhappy experience of 1966. The situation in 1991 was very different. For one thing, unlike in 1966, when the exchange rate had been rigidly fixed for many years, the rupee had been depreciating gradually year after year. Between 1988 and 1991, for example, it had depreciated by 48 percent against the dollar. However, a gradual depreciation is one thing, a sudden large devaluation quite another
- One of the reasons devaluation was highly controversial was that most people did not understand the role it played in dealing with an external payments crisis. They understood that the problem arose because the country was 'living beyond its means'. With more demand in the system than available supply, the excess demand split over to create a current account deficit in the BOP. They also understood that to reduce the current account deficit, it was necessary to curtail total demand in the economy and this involved some 'belt-tightening'. This justified reducing the fiscal deficit, which involved either cutting government expenditure or increasing taxes. Cutting government expenditure cuts demand directly. And raising taxes reduces income in the hands of the consumers, thereby reducing private consumption
- However, it was not immediately obvious to most people why devaluation had to be part of the package of reducing the current account deficit. Devaluation raises the price of tradeables (exports and imports) relative to non-tradeables. This shifts domestic demand away from tradeables towards non-tradeables and this 'expenditure switching effect' increases exports and reduces imports. The effect of this relative price change on the composition of demand reduces the extent of the belt-tightening that might otherwise be needed to bring the current account deficit under control

- Those who realized that devaluation made our exports cheaper in dollar terms and therefore, more competitive often saw it as a policy that only helped exporters, including high-profile software exporters like Infosys, Wipro and TCS. It was not sufficiently appreciated that all domestic producers competing with imports would also benefit because the higher price of imports would make their products more competitive. Many also did not realize that a large part of the higher incomes earned in the export sector would be spent on domestically produced commodities and services, hotels, restaurants, domestic tourism etc thereby adding to employment
- The speed with which trade policy reforms were approved in July 1991 throws up some important lessons for the future. First, the response to a crisis must be speedy, but well considered. Second, it is not always possible to get everyone to agree
- Industrial licencing was abolished for all but a handful of industries and the rules affecting FDI were greatly liberalized. The MRTP Act was effectively abolished and the list of industries reserved for the public sector reduced from 18 to eight
- What made Manmohan Singh's Budget Speech of 1991-92 historic was that he used it to present a masterly explanation of why the wide-ranging reforms were being attempted and how the various components fitted together. He explained that we needed to go beyond crisis management towards structural reforms, including liberalization of both industrial policy and trade policy as a means of unleashing the animal spirits of India's private sector. The opening to imports and foreign investment was necessary to subject the economy to competitive pressure
- The public sector was meant to be an engine of growth but had become an 'absorber of national savings'; this problem needed to be addressed. While there was to be no privatization - the 'P' word was politically unacceptable - 20 percent of equity in selected PSUs would be offered to mutual funds. Further, loss-making PSUs would referred to the Board for Industrial and Financial Reconstruction to see if they could be revived; if not, they would be closed. The interests of workers would be fully protected. In this context, a National Renewal Fund would be established to finance programmes to support training and rehabilitation of retrenched workers

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The Road to Reforms

- The insistence on secrecy meant all the Budget documents had to be printed in an internal press located in the basement of the Ministry of Finance. Some 80-odd individuals were locked in for seven days and let out only after the speech

was over. They were provided dormitory-style accommodation and their meals were provided by caterers and served inside. Only a few senior officers of the ministry had special passes to go in and out to make last minute changes. Spirits in the basement were generally high as those present felt they were performing a very special function

- Highlights of Tax Measures: 1992-93
  - Reduce number of tax slabs of personal income tax from four to three
  - Abolish wealth tax on financial assets
  - Reduce maximum customs duty from 150 percent to 110 percent
  - Reduce customs duty for new projects and general machinery from 80 percent to 55 percent
- In his budget speech of 1993-94, Finance Minister Manmohan Singh stated that he broadly accepted the approach of moving to a regime of moderate rates of direct taxation, broadening the tax base, low to moderate customs duties, a simpler system of excise duties with fewer rates, and a long-term aim of a VAT system. Much was done in this direction in the following three years. The maximum rate of personal income tax was (including surcharge) was reduced from 56 percent in 1990-91 to 44.8 percent in 1992-93, and then to 40 percent by 1994-95. Corporate tax rates had been raised to 45 percent in the first Budget but were brought down to 40 percent in 1994-95
- Reducing import duties was part of the strategy of opening up the economy and increasing its competitiveness and we were able to reduce duty rates faster than envisaged by the Chelliah Committee. By 1995-96, the last year of the Rao government, the maximum rate of duty was down to 50 percent and the duty on capital goods and machinery was lowered to 25 percent. This brought India's average import duties down to 36.6 percent by 1995-96, but it was still much higher than 20.4 percent for Indonesia, 13.7 percent for the Philippines, 7.8 percent for Malaysia and 6.9 percent for Thailand
- A potentially important recommendation that was not accepted was that supervision of the banks should be taken out of the RBI and entrusted to a separate quasi-autonomous Banking Supervisory Board. The Harshad Mehta scam had just broken out and the RBI felt taking supervision out of its purview would look like an expression of lack of confidence in the RBI. A new department for supervision of banks was created within the RBI, presided over by a Board of Financial Supervision chaired by the governor and including all deputy governors. Had we created a separate Banking Supervisory at that time, we might have avoided some of the problems with bank lending that surfaced much later

- A significant reform implemented in 1994 was to end the practice of automatic financing of the fiscal deficit by the RBI. This practice, first introduced in 1955, ensured that every time the Government's cash balance with the RBI went below a certain threshold, the RBI would top it up by issuing 'ad hoc' Treasury Bills at artificially low rates of interest. Governor Rangarajan had been arguing that this practice made monetary policy a hostage to fiscal policy and should be ended. There was resistance at the official level in the ministry because automatic financing made it easier for the officials to manage the fiscal deficit. I felt Rangarajan was right and backed him fully. We were happy when the finance minister decided the practice should stop. The Government would have to finance its deficit through open market borrowing at market interest rates
- Reforms of existing PSUs remained a distant dream. The Government initiated a process of selling minority stakes (less than 20 percent) in the equity of PSUs to mutual funds and public financial institutions, but this was driven primarily by the need to mobilize resources for the Budget. As long as the Government retains 51 percent of the equity and the power to appoint the management, no PSU management can afford to ignore the ministry controlling it. Besides, as long as the Government has 51 percent equity, the legal position of the PSU remains identical to the state and subject to all the restraints on decision-making that would normally apply to the government. This makes it impossible for public sector managers to act with the flexibility and commercial orientation available to private sector managers
- Interestingly, the GDP growth rate in the decade of the 1990s averaged only 5.8 percent, which is only marginally higher than the average of 5.6 percent in the 1980s. However, the decade includes the crisis year of 1991-92, when growth collapsed to 1.4 percent, as well as the year 1997-98, when the East Asian crisis lowered growth to 4.3 percent. If these two years are excluded, the average growth rate was 6.6 percent, much better than any eight-year period in the past. Moreover, the gradualist nature of the reforms meant that many of the measures had not begun to have their full impact. The impact was soon only in the next decade, when average growth reached 7.2 percent

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United Policies, Divided Politics

- Tax Measures in the 1996-97 and 1997-98 Budgets
  - The maximum rate of personal income tax was lowered from 40 percent to 30 percent in 1997-98, making the rate fairly comparable with most countries. A three-slab system was put in place, with tax rates of 10, 20 and 30 percent, respectively

- The corporate tax rate for domestic companies was reduced from 40 percent plus surcharge of 15 percent in 1996-97 to 35 percent with no surcharge in 1997-98
- A minimum alternate tax (MAT) was introduced in 1996-97 to counter the practice whereby companies were able to reduce their tax liability to zero by claiming investment-related incentives
- The rate of tax on long-term capital gains for domestic companies was reduced from 30 percent to 20 percent
- Dividends were exempted from tax in the hands of the recipient but a flat 10 percent tax was levied on dividends to be paid by the company before distribution
- Reduction of import duties was continued in the 1997-98 Budget with the peak duty reduced from 50 percent to 40 percent and the duties on capital goods from 25 percent to 20 percent. The 1996-97 Budget had made a commitment to move to four rates of excise duties over a period of three years. The 1997-98 Budget indicated that the four rates would be 8, 13, 15 and 18 percent in 1997-98, but several items remained outside the four-rate structure

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Continuity With Change

- It is worth noting that when imports of consumer goods were finally allowed in 2001, we did not find it necessary to raise tariffs as there was no unmanageable surge in imports. It illustrated how many of our positions taken in trade negotiations are based on irrational fears of a surge in imports with little acknowledgement of the capacity of domestic producers to adjust to competition
- In 1998, the Vajpayee government took a step back in liberalization of FDI in response to pressure from Indian investors in JV partnerships with foreign companies. When FDI limits were raised from 40 percent of equity to 51 percent in 1991, many foreign investors who had earlier accepted the 40 percent, now wanted to increase their share to 51 percent. If this was resisted by their Indian JV partners, the foreign partner would setup a new JV with other Indian partners willing to accept a minority stake. The Indian partners in the existing JVs lobbied that foreign investors should not be allowed to abandon existing partners to setup new JVs in the same sector. The Government conceded to this demand and introduced a condition that foreign investors with existing JVs would need a 'no-objection certificate' from their existing partners before they could setup another venture in the same sector. Foreign investors saw this as patently unfair as companies that had not entered India earlier when policies were more restrictive were now being allowed to setup majority-owned JVs, while those who had

invested earlier were denied the same flexibility. In many cases, the need for a no-objection certificate only led to existing domestic partners extracting a price for the no objection, vitiating the atmosphere. The no-objection requirement was finally removed in 2005 by the UPA government under Dr Manmohan Singh

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India Hits Peak Growth Under UPA

- Independence of the monetary authority is an excellent practice for normal times but, in a crisis, markets feel much more comfortable if all relevant wings of the Government are seen to be acting in concert
- GDP Growth: 2003-04: 8%; 2004-05: 7.1%; 2005-06: 9.5%; 2006-07: 9.6%; 2007-08: 9.3%; 2008-09: 6.7%; 2009-10: 8.6%; 2010-11: 8.9%; 2011-12: 6.7%; 2012-13: 5.4%; 2013-14: 6.1%
- The introduction of an Insolvency and Bankruptcy Code (IBC) was another extremely important proposal of the Rajan Committee, but work on this started only after the general election. The IBC Bill was introduced by the NDA government in December 2015 and passed in 2016. It is going through the usual teething problems, but is expected to fill an important gap in the financial system, strengthening the rights of secured creditors

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Inclusive Growth

- The percentage of the population in poverty had declined at an annual rate of 1.5 percent, from 37.2 percent in 2004-05 to 29.8 percent in 2009-10, almost twice as fast as in the pre-UPA period

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Epilogue

- The so-called ‘middle-income trap’ is relevant in our context. The concept derives from the proposition that in the initial stages of development, growth can be accelerated by carrying out reforms that remove key constraints on productivity. This can take a country out of the low-income category of per capita income below $1,000 to the middle income category from $1,000 to $12,000. However, once the economy gets into the middle-income range and attains a degree of complexity and sophistication, another set of ‘second-generation’ reforms are needed to ensure that rapid growth is sustained. These reforms include stronger institutions and much greater investment in human resources to help realize the full efficiency gains possible in a market economy

- The tax-to-GDP ratio of 2019-20 is estimated at 11.7 percent, and is projected to fall to 11.6 percent in the next two years. The recent reduction in the corporate tax rates after the Budget for 2019-20 will further reduce the tax ratio
- Internationally, majority government ownership is seen as inconsistent with sound commercial banking, but no part of the political spectrum in India shares this view
- Banking reform should include giving the RBI the same powers over public sector banks as it has over private sector banks, including the decision to approve the proposed appointment of a CEO in advance, based on 'fit and proper grounds', and the power to remove CEOs for non-performance. It is also necessary to implement reform in the RBI to improve its regulatory and supervisory capacity. The need for such improvement is evident from the way NPAs were allowed to build up in the public sector banks until the problem was finally revealed by the asset quality review initiated by Governor Raghuram Rajan in 2015. RBI regulation over the non-bank financial sector also needs to be strengthened as this part of the financial sector has also come under stress
- Those who resist privatization of existing public sector banks must remember that private banks are continuously innovating and inducting new technologies while government-controlled public sector banks have less flexibility and are losing their ability to complete. The result is already evident as the share of public sector banks in total advances fell from 76 percent in 2014 to 61 percent in 2019. At this rate, the share of the private sector could increase to over 50 percent in 10 years. Since the sector is being effectively privatized in this manner, the option of privatizing some individual public sector banks deserves consideration
- Good economics may not seem to be good politics in the short term, but wise political leaders will realize it is almost always the best politics in the long run. How to marry the two is, in some sense, the real test of political leadership. I remain an unrelenting optimist that our political system can resolve this conflict and that the India story of high growth and development will therefore continue