# Indian Economy

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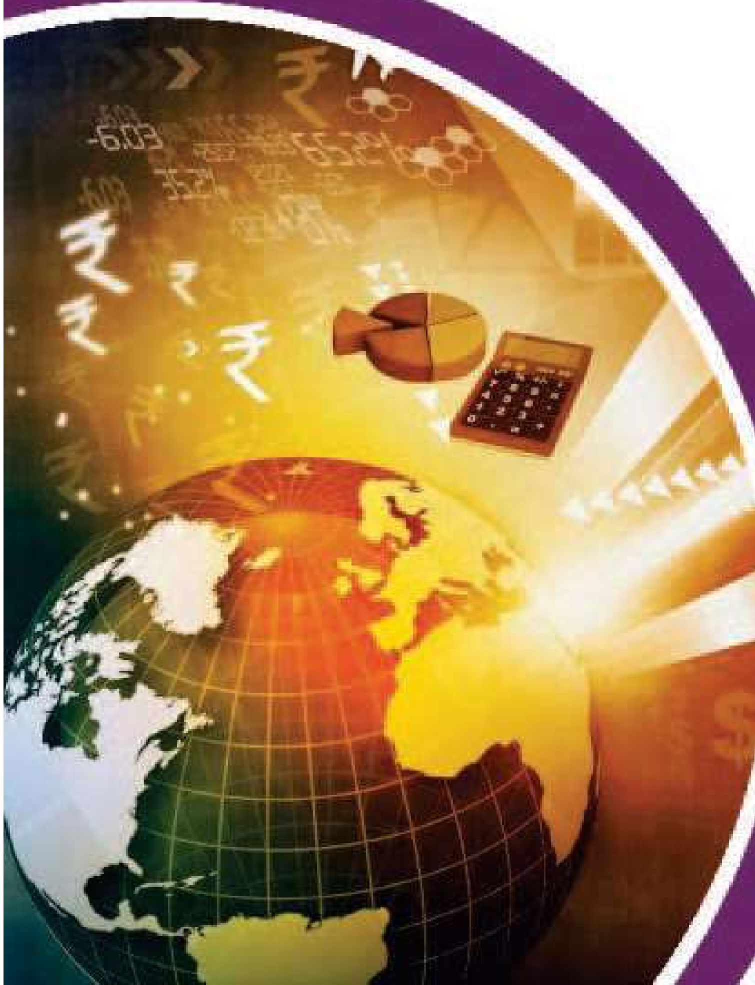

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# Contents

# 1 CHAPTER Indian Economy: An Introduction

## BACKGROUND OF INDIAN ECONOMY

Every economy in the world has its own characteristics or features by which it is known or identified. The economic conditions of India before the British came around the middle of 19th century were almost similar to these which prevailed in other countries at a comparable stage of industrial development. The agricultural sector as also the industrial sector was in a high degree of development. While trade and transport sectors were just satisfactory, banking was quite a developed sector. India was predominantly an agricultural country. According to the 1871 census, 56.2% of the adult male population was engaged in agriculture. To these may be added another 12.3 percent classified as general labourers. Agriculture was quite advanced as Indians cultivated wheat centuries before the English did.

| Features of the economic conditions of India before the British period |
|---|
| – Self-sufficiency and isolation |
| – Subsistence farming |
| – Lack of specialisation |
| – Dominance of customs and traditions |
| – Highly immobile labour |

**Colonial Exploitation: Forms and Consequences**

Under the colonial dispensation, the economic policies of the government were concerned more with the protection and promotion of British economic interests than with the need to develop the economic condition of the colonised country and its people. The agricultural sector continued to experience stagnation and incremental deterioration despite the fact that the largest section of Indian population depended on it for sustenance.

The exploitation by the British can be studied in three phases of their rule.

- **The first phase -** The period of merchant capital covers the period of 100 years from 1757 to 1857. During this phase, the East India Company had its sway. Its loot of the country's wealth was like that of a bandit who openly robs a house at gunpoint.
- **The second phase -** The period of industrial capital- starting from the beginning of nineteenth century and continuing till the end of this century and
- **The final phase -** The period of finance capital starting from the late nineteenth century and continuing till the independence.

## INDIAN ECONOMY ON THE EVE OF INDEPENDENCE

In 1947-48, per capita income was just Rs. 230. The population of India was nearly 36 crore, including 82% as illiterate. Nearly 72% of the country's population was engaged in agriculture.

Industrially too, the Indian economy was equally backward. In 1947, the total production of steel was merely 13 lakh tonnes. The rate of capital formation was hardly 6.8 per cent of the net domestic product of the total capital formation; public sector contributed nearly 20% while 80% belonged to the private sector. The period of the British rule was one of ill fortune for the Indian economy. The British rule made Indian economy under-developed and lop-sided.

During the early years of India's Independence, the economy's growth rate was lower but comparable to India's emerging market peers. The early phase of Indian economic planning, led by Jawaharlal Nehru was moderately successful in raising growth. Like the economist-turned-lawyer B.R. Ambedkar, Nehru believed that rapid industrialisation driven by the state was the most effective way to abolish mass poverty. These leaders' views in fact echoed those of the titans of Indian industry at that time, articulated in the Bombay Plan of 1944-45.

The post-Nehru era, however, saw India's growth rate slip below those of her peers. At a time when other controlled economies such as South Korea were opening up their economies and turning their industrial hubs into export powerhouses, Indian economic policy continued to be inward-looking. The license -permit raj gained in strength, leading to corruption, and cramping economic growth. The shackles on Indian businesses began to be loosened around the 1980s, and the Indian economy started growing at rates never experienced before. Since then, the growth rate of the Indian economy has eclipsed that of most of the country's peers.

# EXERCISE

1. Which one of the following is not a feature of a developing economy?
   (a) High rate of population growth
   (b) High rate of unemployment
   (c) Mass poverty
   (d) High rate of capital formation
2. Mixed economy envisages
   (a) Co-existence of capitalists and labourers
   (b) Integrated economic development
   (c) Development of agriculture and industry simultaneously
   (c) Private and Public Sectors
3. "Socialist Pattern" comes through
   (a) Free economy (b) Mixed economy
   (c) Public sector (d) None of the above
4. The predominant activity in the non-agricultural sector at the end of British rule was
   (a) Industry (b) Services
   (c) Both (a) and (b) (d) None of the above
5. Economic causes of under-development of India is/are
   (a) Market imperfections (b) Vicious circle of poverty
   (c) International forces (d) All of these
6. What are out the economic factors responsible for the under-development of the Indian economy.
   1. Shortage of capital
   2. Technological backwardness
   3. Lack of skilled manpower
   4. Low geographical mobility due to attachment to land.
   (a) 1 & 2 (b) 1, 3 & 4
   (c) 1, 2 & 4 (d) 1, 2 & 3
7. Who wrote a book describing the theory of economic drain of India during British rule?
   (a) Dadabhai Naoroji (b) Lala Lajpat Rai
   (c) Mahatma Gandhi (d) Jawaharlal Nehru
8. Which of the following is not a characteristic common to most LDCs?
   (a) A high rate of population growth
   (b) Large land area
   (c) Low proportion of adult literacy
   (d) Heavy reliance on one or a few items for export
9. What is Broad Money?
   (a) M1 (b) M2 (c) M3 (d) M4
10. In India, present trend of rapid urbanisation is due to:
   (a) Influence of cinema and electronic media
   (b) Lack of employment opportunities in rural areas
   (c) Break-up of joint family system
   (d) Abolition of zamindari system
11. Which of the following are the main causes of a slow rate of growth of per capita income in India?
   1. High rate of capital formation
   2. High level of fiscal deficits
   3. High rate of growth of population
   4. High capital output ratio
   (a) 1, 2 & 3 (b) 3 & 4
   (c) 1, 2, 3 & 4 (d) 2 & 4
12. Which of the following is not a flow concept?
   (a) Consumption (b) Spending
   (c) Investment (d) Capital
13. A "closed economy" is an economy in which
   (a) the money supply is fully controlled
   (b) deficit financing takes place
   (c) only exports take place
   (d) neither exports nor imports take place
14. Under the British rule, Indian economy became a poor and dependent economy because of :
   (a) Decline in crafts
   (b) Commercialization of agriculture
   (c) Change in occupational structure and foreign trade
   (d) Food scarcity and famines
15. Economic development has been retarded in India mainly due to:
   (a) Haphazard industrialisation
   (b) Westernised social attitudes
   (c) Poor infrastructural facilities
   (d) Inefficient agrarian system
16. In a free economy inequalities of income are mainly due to:
   (a) Free competition
   (b) Private property only
   (c) Private property and inheritance
   (d) Difference in the marginal productivity of labour.
17. Which among the following was not a characteristic of Indian economy at the time of independence?
   1. India was importing capital and consumer goods
   2. India exported primary commodities and industrial materials
   3. India was exporting food products
   4. India was importing food products
   (a) all of these
   (b) 2
   (c) 1, 4
   (d) 3
18. Which of the following is the cause of economic insecurity?
   (a) Poverty
   (b) Unemployment
   (c) Fall in real wages
   (d) All of the above
19. In 1991 India met with an economic crisis. Which of the following can be quoted as a reason for the same?
   1. The high level of external debt.
   2. High level of foreign exchange reserve.
   3. Rising prices of essential goods.
   4. Import substitution policy of India.
   5. Political instability.
   **Code:**
   (a) 1 and 2 (b) Only 1
   (c) 2, 3 and 4 (d) All the above

20. Consider the following statements about India's approach in dealing with 1991 crisis.
    1. India approached the international bank for reconstruction and development popularly known as IMF for loan to manage the crisis.
    2. India came up with new economic policies which were based on the conditionality of international institutions.
    3. Conditionality of international institutions was not as a punishment but were towards creating more competitive environment in the economy.

    Select the correct ones.
    (a) All the above (b) 2 and 3
    (c) 1 and 2 (d) 1 and 3
21. Which of the following is not a part of changes in industrial sector post 1991 reform?
    1. Industrial licensing under which every entrepreneur had to get permission from government officials to start a firm was abolished except in some sector.
    2. Private sector was allowed in many industries.
    3. Some goods could be produced only in small scale industries.
    4. Controls on price fixation and distribution of selected industrial products.

    **Code:**
    (a) 1, 3 and 4 (b) 1, 2, 3 and 4
    (c) 1 and 4 (d) 3 and 4
22. There are many ways to categorize poverty. Consider the following statements in this regard.
    1. 'The people who are always poor' and those whose are usually poor but who may sometimes have a little more money are called chronic poor.
    2. The people who regularly move in and out of poverty are called churning poor.
    3. People who are rich most of the time but may sometimes have a patch of bad luck are called occasionally poor.

    Select the correct ones.
    (a) 1 and 2 (b) 2 and 3
    (c) All the above (d) 1 and 3
23. Most of the economies including India are mixed economies. Consider the following statements.
    1. In mixed economies government and the market together answer what and how to produce and how to distribute what to produce.
    2. The government will provide whatever goods and services it can produce well.
    3. The market will produce to the goods and services the government fails to do.

    Select the correct ones.
    (a) Only 1 (b) 1 and 3
    (c) All the above (d) 2 and 3
24. India followed a planned economy from the time of independence. Consider the following statements.
    1. India's plans were of five years and lacked a perspective approach.
    2. Directive principles of Indian constitution reflect the planned outlook of India.
    3. Our five year plans do not spell out how much of each and every good and service is to be produced.

    Select the correct statements using codes below.
    (a) Only 2 (b) 2 and 3
    (c) 1 and 3 (d) All the above
25. In case of India we have unemployment in rural and urban areas. Consider the following statements about types of unemployment in India.
    1. Disguised unemployment happens when people are not able to find jobs during some months of the year due to agricultural patterns.
    2. Educated unemployment is a result of improper management of Human resources.
    3. In case of India, statistically, the unemployment rate is low.

    Select the correct statements using codes below.
    (a) 1 and 2 (b) 1 and 3
    (c) 2 and 3 (d) All of the above

## Answer Keys

| | | | | | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1 | (d) | 2 | (d) | 3 | (b) | 4 | (c) | 5 | (d) | 6 | (d) | 7 | (a) | 8 | (b) | 9 | (c) | 10 | (b) |
| 11 | (b) | 12 | (d) | 13 | (d) | 14 | (c) | 15 | (c) | 16 | (c) | 17 | (d) | 18 | (d) | 19 | (b) | 20 | (b) |
| 21 | (a) | 22 | (c) | 23 | (a) | 24 | (b) | 25 | (c) | | | | | | | | | | |

# 2

CHAPTER

# Underdevelopment, Development and Economic Growth

In economic terms, development has been understood as achieving sustainable rates of growth of income per capita to enable the nation to expand its output faster than the population. This definition fails to take into consideration problems of poverty, discrimination, unemployment and income distribution; the assumption being that increased output or economic growth would deal with these issues. The distinction between underdeveloped and developed countries is rather loose and also arbitrary to a certain extent.

## UNDERDEVELOPED ECONOMY

- The term 'underdeveloped countries' is relative. In general, those countries which have real per capita incomes less than a quarter of the per capita income of the United States are underdeveloped countries.
- More recently, instead of referring to these economies as underdeveloped, the UN publications prefer to describe them as 'developing economies'.
- The term 'developing economies' signifies that though still underdeveloped, the process of development has been initiated in these countries. Thus, we have 'developing economies' and 'developed economies'.
- According to the United Nations definition, an underdeveloped country is one which has a real per capita income that is lower in relation to the real per capita income of the USA, Canada, Australia and Western Europe.
- Emphasis here is on the low income level relative to the advanced countries and lack of any perceptible success in making substantial improvements in quality of life of the masses.
- In simple words, underdeveloped country is just another name by which a poor backward country is known.

## WORLD BANK'S CLASSIFICATION

The World Bank assigns the world's economies to four income groups—low, lower-middle, upper-middle, and high-income countries. The classifications are updated each year on July 1 and are based on GNI per capita in current USD.

The classifications change for two reasons:

In each country, factors such as economic growth, inflation, exchange rates, and population growth influence GNI per capita. Revisions to national accounts methods and data can also influence GNI per capita.

To keep the income classification thresholds fixed in real terms, they are adjusted annually for inflation. The Special Drawing Rights (SDR) deflator is used which is a weighted average of the GDP deflators of China, Japan, the United Kingdom, the United States, and the Euro Area. This year, the thresholds have moved up in line with this inflation measure. The new thresholds (to be compared with GNI per capita in current USD, Atlas method) are as follows:

| Group | July 1, 2020 (new) | July 1, 2019 (old) |
|---|---|---|
| High income | > 12,535 | > 12,375 |
| Low income | < 1,036 | < 1,026 |
| Lower-middle income | 1,036-4,045 | 1,026-3,995 |
| Upper-middle income | 4,046-12,535 | 3,996-12,375 |

*Source: www.worldbank.org*

- Income is measured using gross national income (GNI) per capita.
- Similar groupings had originally been introduced with the *World Development Report* in the late 1970s, but countries were not classified consistently.
- "Developing economies" were divided into low income and middle income; OECD membership was used to define "industrial" countries; and other economies were listed as "capital surplus oil exporters" and "centrally planned economies."

**Main Characteristics of Underdeveloped Countries**

- Low per capita income
- Low level of living
- High rate of population growth
- High levels of unemployment and underemployment
- Predominance of agriculture in the economy
- Low rate of capital formation
- Highly unequal distribution of wealth/Assets
- Low Levels of Productivity
- Technological Backwardness
- Lower Level of Welfare
- Insignificant Foreign Trade
- Export of primary products
- Weal infrastructure
- Poor quality of human capital
- Dualistic economy
- Low social indicators of development

## Developing Economy

A developing economy is defined to be an economy where the standard of living enjoyed by the people has not reached a high level but is rising. Again since per capita income is the usual measure of the standard of living, the definition can be stated in terms of per capita income: "A developing economy is an economy where per capita income is rising."

### UN Classification of Developed and Developing Economies

The UN classification on the basis of per capita income reveals three things:

(i) Presence of gross inequality of incomes between the rich and the poor countries;

(ii) gap in per capita income (and consequently in living standard) between the rich and the poor countries is even widening over the years—though recently the growth rate among low income countries is showing an increase and if this is sustained the gap may reduce over a period of time; and

(iii) All high income group countries are not developed countries-the oil exporting countries have high per capita income mainly due to their exports of oil, but in real sense they are not developed countries.

### Features of Developing Economy

- Gradual rise in per capita income from a low level.
- Gradual rise in per capita saving and capital formation.
- Gradual decline of the contribution of the agricultural sector towards national income.
- Gradual expansion of infrastructural facilities.
- Falling incidence of poverty, adult illiteracy, gender discrimination etc.
- Gradual shift in occupational structure in favour of industrial and service activities.
- Gradual improvement in the standard of living of common people.
- Gradual improvements in science and technology.

# ECONOMIC DEVELOPMENT

Economic development implies the process of securing levels of productivity in all sectors of economy and this, in turn is a function of the level of technology. Economic development is a process of stepping up the rate of capital formation. But economic development is, influenced by both economic and non-economic factors.

- The prominent economic factors are the available capital stock and the rate of its accumulation, capital-output ratio in various sectors, agricultural surplus, conditions in foreign trade and economic system.
- The non-economic factors are size and quality of human resources, political freedom, social organisation, technical know-how and absence of corruption etc. economic development means economic growth in a country where the growth process has not progressed very far.
- Development is to be pursued as a deliberate mechanism of deliverance of the masses from poverty and idleness in a relatively short period of time. Economic development is not only a process but also a level.

**Features of a Developed Economy**

- High Per Capita Income
- High Standard of Living
- High National Income
- Full Employment of Resources
- High Level of Technology
- Dominance of Industrial Sector
- High Industrialisation
- High Consumption Level
- Smooth Economic Growth
- High Level of Urbanisation
- Social Equity, Gender Equality and Low Levels of Poverty
- Political Stability and Good Governance

According to Amartya Kumar Sen, development is about creating freedom for people and removing obstacles to greater freedom. Greater freedom enables people to choose their own destiny. Obstacles to freedom, and hence to development, include poverty, lack of economic opportunities, corruption, poor governance, lack of education and lack of health.

# ECONOMIC GROWTH

Economic growth has been defined as "an increase in real terms of the output of goods and services that is sustained over a long period of time, measured in terms of value added". Economic growth is a dynamic concept and refers to continuous increase in output. A country's economic growth is usually measured by National Income, indicated by Gross Domestic Product (GDP). The GDP is the total monetary value of the goods and services produced by that country over a specific period of time, usually one year.