And They Call These Reforms!

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In view of the fast deteriorating economic situation in India the government has launched a number of measures which it claimed are harbingers of economic reforms and, therefore, prosperity. The two most important of these measures relate first to petroleum products such as diesel and LPG and second to permitting Foreign Direct Investment (FDI) in certain sectors. The price of diesel has been substantially increased by approximately fifteen percent and so far has LPG is concerned, it has been decided that six cylinders per year will be made available at a subsidised price and that any quantity above this will be charged at a price which approximates to the market cost and would be about double the subsidised price. FDI is to be permitted in retail trade and in the civil aviation sector. There has been widespread public objection to these measures but government has gone ahead despite opposition.

Diesel is the fuel for prime movers in the transport sector, for agricultural machinery, pump sets for lifting water and small generator sets for power generation. The railways use a large quantity of diesel for locomotives and it is also the major fuel for marine propulsion. An increase in the price of diesel would automatically adversely impact the fishing community whose mechanised boats and trawler are diesel propelled. A very small percentage, say five to six percent, is used for private transport. A substantial increase in diesel would have such an adverse impact on the transport sector that it would push up all commodity prices, be they agricultural, industrial, consumer goods, pharmaceuticals, in fact the entire gamut of trade. In the field of agriculture an increase in the price of diesel would force a cultivator to spend more for his normal operations and this would cut sharply into any surplus he might earn in agriculture. The increase in commodity prices will hit the average consumer very hard indeed.

In the matter of LPG, this fuel has been encouraged because it is clean, relatively pollution free and is a substitute for such fossil fuels as coal and for biomass, such as firewood. In fact government promoted the extension of gas in cylinders in hill areas and tribal areas so that the felling of trees for fuel wood could be reduced. That is why a subsidy was given and against the loss to the exchequer one could set off the benefits flowing from the saving of trees and reduction of pollution while burning a clean fuel, both of which would reduce the carbon foot print. Now with LPG being priced beyond the means of the average Indian those at the lower end of the economic spectrum will undoubtedly resort to alternative fuels and if these take the form of firewood, God save our forests.

The tragedy is that government, in the name of reforms, instead of looking at the subsidy regime in totality, has decided to take measures in bits and pieces and in an ad hoc manner. Subsidies are of various kinds. One set of subsidies is given in order to kick start a particular set of activities. For example, concessions and subsidies given to new starts in industry or in designated industrial areas are justified on the grounds of encouraging industrial activity and creating employment opportunities. Another set of subsidies is given for the promotion of welfare of such groups as under-nourished children, people living below the poverty line and those who cannot afford even essentials, the totally landless and those who are unemployed. The mid-day meal programme in Tamil Nadu, as also the provision of cheap rice to those below the poverty line, are welfare measures to tackle malnutrition in children and hunger amongst the poor. These subsidies are fully justified because it is the duty of the State to promote the welfare of the people. Then we have a whole set of totally populist subsidies, such as free electricity to slum dwellers and farmers, which need an immediate review and, perhaps a quick phasing out. I am prepared to lay a wager that it is populist subsidies which will survive, despite the fact that they not are justified on any grounds.

Moving to FDI, China decided immediately after the revolution that it would encourage manufacture of goods, including capital goods and for this purpose adopted a very aggressive industrialisation policy. Right from the backyard furnace for making low quality pig iron upto the most modern factories, China went all out to inculcate a culture of manufacture and today China is a virtual power house of industry. To sustain such industrial growth China also had to build the support infrastructure, including roads, railways and huge power houses for generating electricity; these include the Three Gorges Dam, which is the largest hydro electric project in the world. By contrast India followed the tertiary sector model of development, in which the service industry grew but there were no parallel growth of manufacture. That is why whereas in software development in the IT sector India has done extremely well, in the matter of hardware it is the Chinese made Lenovo laptop which is the fastest selling laptop computer in the world today. In the field of manufacture China is far ahead of India.

Ultimately it is only a country with a strong secondary sector which can develop fast. India will have to pay a heavy price for its neglect of manufacture. This has led to slow growth of infrastructure, poor research and development and stagnation in the manufacturing sector. That is why whereas in China a great deal of manufacturing capability of America is off-shored, in India our government opens the retail market to foreign chains of stores such as Sainsbury, Walmart and Tesco. It also opens the civil aviation industry to foreign investment. However, in terms of investment in the manufacture of aircraft or factories for producing air-conditioning equipment for the agricultural storage industry our policy is inimical to such investment. We do not need foreign investment in retail – what we need is massive investment in creating physical infrastructure and in creating a powerful secondary sector which will make India a major producer of capital goods, as also manufactured goods for consumption. One cannot help but feel that we are a nation of traders and, therefore, to expect government to push us into the world of manufacture as the Chinese have done is perhaps expecting too much of it.

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