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## FOREIGN POLICY OF ECONOMIC REFORMS AND GROWTH IN PUBLIC SECTOR, FINANCIAL SECTOR AND TRADE POLICY

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### ABSTRACT:

*More apparently, the question of understanding the trajectory of changing preferences in economic foreign policy of India in this liberalised world becomes essential. In the era of Globalisation, Indian foreign policy has enmeshed itself in liberal ideology paradigm. It has led Indian foreign policy makers to take specific domestic reforms at the domestic level and to compete itself in the global market. Essentially these economic reforms became a part of its economic diplomacy to pursue the economic growth of the country. This paper is looking into the process of India's economic diplomacy in post liberalization era.*



**KEYWORDS:** *Foreign Policy, Liberal Ideology, Public Sector, Financial Sector, Trade Policy.*

### INTRODUCTION :

Ideational liberalism claims that particular dominant ideologies prevail continuously throughout the history of the world. These dominant ideologies always stand opposite to each other's premises of thought. For example, Nolt (1990) and Barkin (1990) pointed out that much of the Peloponnesian war, has been explained by Thucydides as the conflict between two different ideologies - oligarchs and democrats. Seventeenth and eighteenth centuries witnessed the struggle of absolutist kings for their dynastic claim as against democratic reforms. The twentieth century is the century of struggle and conflict between Fascism, Communism and liberal ideology. More recently it can be seen as a clash of religious cultural identity and with a group of developed countries. (Russet 1993:30-38). In a way, the discourse of different ideologies are dominant and remains significant in international politics. In International Politics, Kehone and Nye has proposed a theory of complex interdependence. They point out that military force is becoming less useful among interdependent states. Transnational actors are going to become more important. Three characteristics have been shown by the authors. These characteristics are multiple channels connecting societies; absence of hierarchy among issues in relations of different states; and decline in the use of military force by the governments if within the region conditions of complex interdependence are existing (Kehone and Nye 2001: 20-32). In present time the logic of liberal ideology is quite noteworthy. In fact, maximum countries in the present time are driving their economic force of national development. The strategic policy thinking that underlies this change is based on the fact that external economic relations create relations of economic interdependence that contributes to a more stable global economic order (Baru 2006: 115).

## Tracing the Foreign Policy of Economic Reforms and Growth in Public Sector, Financial Sector and Trade Policy

**Public Sector Reforms:** The main objective of the reforms was to reduce the activities of public sector specially related with loss making divisions in the public sector. It was done to reduce the load on exchequer. It was emphasized that the public sector should focus only on those sectors which are important from the security and strategic point of view and are an integral part of the essential infrastructure. The government started a restricted process of disinvestment of government equity in public sector companies, with government holding 51% of the equity and also managing mechanism. Economic liberalisation created new terms on which bureaucracy started doing its work. The interaction between the private and government sector became the theme of strengthening the economy in positive way. The Federation of Indian Chambers of Commerce and Industry (FICCI), Confederation of Indian Industry (CII) and the role of the Associated Chambers of Commerce and Industry of India (ASSOCHAM) played a major role in facilitating globalizing of Indian economy and reforming the public sector (Singh 1991:1). FICCI has played an important role in articulating private sector's views on foreign trade policy. It mainly worked to enhance efficiency and global competitiveness of Indian industry. It expands the opportunities for domestic players both in foreign as well as in domestic markets through a specific range of global linkages. Indian private business groups were more concerned with domestic liberalization than with the losses and gains India sustained at the multilateral level (Sinha 2010: 467).

**Financial Sector Reforms and Exchange Rate Policy:** Under the liberalization process, restrictions and regulatory controls over financial institutions were removed. In financial sector, interest rates were deregulated. Accessing credit was made easier, banking was encouraged to expand and capital market deregulated (Ogden 2014:58). The objective of the financial sector reform is stated to be improved profit ability of the state retained commercial banking system and better working of the domestic capital market. Under liberalization it is supposed that the discipline of market will make both banking system and capital market well-organised. The concrete reduction in the statutory liquidity ratio and the cash reserve ratio are destined to remove financial limitations for the private sector. In a parallel move, the interest rates on securities of government have been raised close to the market levels. In general the philosophy of deregulation has been followed by government and the Reserve Bank of India. Beside these domestic changes, Indian Government in its economic foreign policy liberalised economic transactions on the current and capital accounts. While current account transactions have been fully liberalised during the initial years of liberalisation in India, the capital account has been liberalised gradually. It has encouraged the Indian professionals and corporates to increase their transactions with the rest of the world (Baru 2006:116). The current global scenario is providing the opportunities for strengthening the business environment and attracting the foreign direct investment. But along with the financial sectors, e-commerce is providing greater leap to compete at par with other world economies and is expanding in a better way on technological bases (External Affairs Ministry Report 2014: 32). Indian economic policy has succeeded in integrating its financial sector in global world economy which is helpful for expanding the economy of India.

If it is analysed critically, it is found that the contribution of FDI in the labour intensive industries is not significant. It is found that nature of capital flow in FDI is more in infrastructure than manufacturing. Trade and FDI flows have not shifted to labour intensive commodities in which India has a comparative advantage. The kind of liberalization India has pursued is based on the free access to capital goods and labour intensity in manufacturing sector which declined progressively. The Indian economy has shown reorientation towards more capital intensive nature of production. But at the same time, Indian foreign policy on trade and foreign direct investment has succeeded to increase the efficiency in manufacturing. It can be argued that economic reforms are gradual in nature. Each of the successive governments have supported these economic changes which were grounded on the ideology of market liberalisation. Despite late starter of economic reforms course, India can be perceived to have accomplished reasonably well in globalizing the economy and finds a good place in global economy. India's higher economic growth in this reform era is placing India as an important player in

international system. India has got more credibility in term of international leadership (Mohan 2014). India has got its credibility on the basis of economic growth in the reform era. India is expanding its weight on the basis of its economic strength.

**Trade Reforms and Indian Foreign Policy:** India had been following very strict rules and regulation in foreign trade for about four decades after independence. Earlier import and exchange rates were totally under direct control of the state. The import and exchange rate rules stipulated that there was complete control over foreign exchange utilization, vast dependence on quotas (Bhagwati and Srinivasan 1975). In 1991, import licencing of goods were divided into limited permissible, banned, and restricted and subject to Open General Licensing (OGL). Under the category of open general licensing, imported goods into India did not require a licence provided they fall and come within the scope of open and general licencing. For that reason, open general licensing was understood liberal and was confined to 30% of imports. The imports were also subject to disproportionately high tariffs. The highest rate was 400%. 60% of tariff lines were subjected to fluctuating tariffs from 110 to 150 percent. Only 4% of the tariff charges were under 60%. In capital and current account transactions severe exchange controls were applied (Pangaria 2001:2). In 1992, this procedure was amended to do away with Open General License by allowing imports and exports of all things without a license excluding those specified in a small negative list. The distribution of import license were grounded on two major principles; essentiality and indigenous non-availability (Sen 2002:318-319). It was the time when the whole world was rushing towards liberalisation. India had the no option but to join the race in this economic scenario and increase its exports to tide over the imports. It was necessary to make its presence felt in global trade. Import control ended with tariffs and duties reduced from 200% to 50% (Ogden 2014:58). As a result, the government proclaimed several export promotion actions. Along with it laws were designed to streamline the procedure. These laws aimed to expand the India's trade. The export and import program 1992-1997 can be perceived as innovative in India's economic past. To double the share of global trade and its thrust to employment was the important objective of Indian foreign trade policy (Handbook on Foreign Trade Policy to Export and Import 2008: 2). In the 1992-1997 policy, the list of restricted items contained 11 categories. In the first five year of trade policy, India heralded new changes in its trade policy. It was recognized that trade can flourish in a regime of substantial freedom. New policy stated that all goods could be freely imported unless particularly restricted through a negative list of imports. Going through such kind of vision, the negative list was kept as small as possible. Indian government pruned the list from time to time as the economy gained the strength. The quota was diluted in April 2001 when the balance of payments complications had eased. The constraints are now well-suited to the obligations undertaken by India under the agreement of the WTO.

The five year exim (export and import) policy 2002-2007 was modified in 2004 and was combined into the new five year trade policy started for the time period of 2004-2009. New trade foreign policy in 2004 seems to be built on the ongoing liberalization efforts by decreasing tariffs; unchaining controls and streamlining procedures; bringing down transaction charges; wide use of duty reductions and immunities to neutralise all levies and duties on inputs used in export products; forming export processing zones, the so called special economic zones to increase export and tie together FDI into infrastructure building. India has a comparative advantages in certain sections of the services area. The decreasing trade taxes patterns show continuing commitment to trade liberalisation. Over the period tariff reduction has been noted and gone deeper in manufacturing merchandise in comparison to agricultural sector. The growth of foreign trade which was accounted for 17% of GDP in 1991, was 44% by the end of 2005 (Dash and Sharma 2011: 237). Indian exports saw considerable development to touch US\$168 billion in 2008-2009 from 63 US billion dollars in 2003-2004. The portion of global trade was 0.83% in 2003 and it rose to 1.45% in 2008 as per WTO assessments (Report of Foreign Trade Policy 2009-2014: 2014: 6).

There is the rapid rise in service exports. These service exports have grown faster than merchandise trade in recent years. The overall annual growth rate in service sector increased from 6.9% during 1981-91 to 8.1% during 1991 to 2001 (Pangaria 2007: 16). It is a noteworthy aspect of

India's trade profile. India can be seen as an emerging exporter on the global scene along with China, Ireland and Korea. India's service exports in 1991 was 4.9 billion dollars in 1992 and it rose 25 billion dollars in 2003. India's trade performance can be seen in the context of its merchandise trade and total account of goods and services exports. WTO's International Trade Statistics 2010 stated that, in merchandise trade, India is the 20<sup>th</sup> leading exporter in the world with a portion of 1.4% and the 13<sup>th</sup> biggest importer with a portion of 2.1% in 2010. In India's full account of exports of goods and services, services exports account for 40%. As per the objective of foreign trade policy 2004-09, the Indian export accounted to grow from US \$ 83.5 Billion in 2004-2005 to US\$ 185.3 Billion in 2008-2009. It registered the annual growth rate of 24 %.( Outcome Budget Report of India 2014:46).

The short time goal of foreign trade strategy 2009-2014 was to reverse the trend of exports. The plan was to promote to those sectors which were hit severely because of the financial crisis in the advanced world. This sector provides employment to many million people. India's export is related with mainly IT and IT aided sectors, transport and financial sector. The main places of destinations are United State and European Union and other advanced countries in 2008. The most severely affected sectors were banking and financial service sector, infrastructure and information technology sector. The long term goal aims to double India's exports of goods and services (Outcome Budget Report of India 2014: 47 and Annual Report 2009-2010).

As per WTO's International Trade Statistics, 2012, in merchandise trade India mounted to 19<sup>th</sup> position of major exporter in the world with a portion of 1.7% and 12<sup>th</sup> import terms with a portion of 2.5% in 2012. In same way, India rose to 8<sup>th</sup> largest exporter with a share of 3.3% in world exports and 7<sup>th</sup> biggest with 3.1% of the share of imports (Outcome Budget Report of India 2014:90). India's merchandise export was USD 83.5 billion in 2004-2005. It increased to USD314.4 billion in 2013-2014. India's two way merchandise trade registered USD 760 billion in 2013-2014. It is around 44.1 percent of the GDP (Foreign Trade Policy 2015-2020: 8, 9). In the year of 2013-2014, India's service export stood at USD151.5 billion. It is a significant increase in share of services in India's total services exports (Financial Express, 4 April 2015).

India's performance on economic growth has shifted the perceptions of its power and potentiality in economic sphere. It has fueled its acceptance on the global stage. This type of acceptance is working as the major driver of advancing its foreign policy in present time. The Indian foreign economic policy has shifted from economic self-reliance to trade orientation strategy. Trade has contributed to India's high economic growth. India's economic strategy in favour of trade economic liberalisation at the domestic level has led India to a substantial economic integration with the world economy. The purpose of trade strategy reform executed so far in India has been to eliminate the unrestricted bureaucratic controls generally on imports. Sen points that India's growth acceleration in its early phase was primarily based on the statist model of development. But the later, the phase of economic reforms brought down the price of capital goods accessible to Indian firms (Sen 2009: 372). The trade growth of India has accelerated in terms of its share in GDP in India. Mainly, economic expansion is based on the increasing growth of India's trade in merchandise and services.

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