

Examining the Role of World Bank in Shaping the Industrial Policy in India

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Abstract: *Ever since India got independence in 1947 the World Bank has played a critical role in framing various policies of economic development ranging from agriculture to industrial sectors in India. The World Bank policies in Indian industrial sector started taking shape in 1953, when a three-man mission sponsored by US government and the World Bank mission visited India. On the basis of this commission's instructions to facilitate the close integration of private capital with foreign capital the government established the Industrial Credit and Investment Corporation of India (ICICI) in January, 1955. Since then in many ways in general and through Structural Adjustment Lending from 1980's in particular the World Bank has played a very critical role and the entire liberalisation of Indian economy in the post 1990's were seen by many economists, was based on the conditionalities and recommendations attached to the lending of the World Bank. The article examines the role played by the World Bank in the Industrial policies of India from post Independence period to the beginning of the economic liberalisation in India.*

Keywords: *The World Bank, Industrial policy of India, Aid India Consortium, IBRD, IDA*

1. INTRODUCTION

1.1. World Bank and Aid India Consortium

The World Bank is the largest donor to India. Through its Delhi Office and India specific staff in Washington head quarters, World Bank has many specialists with long term expertise position, policy responsibility on India. And an Indian Executive Director at the World Bank, usually a senior Civil Servant, strengthens and eases the Indo Bank relationship [1]

The policy advice and economic analysis mostly produced by resident mission staff in close consultation with government officials. Conditionality was used sparingly and common ground between the World Bank objectives and the government policies were continuously stressed [1].

From about 1963-64 onwards a rapidly increasing share of the Aid India Consortium aid to India came as non-project loans for general balance of payment support [2]. In 1965 Bell commission sent by World Bank to study the Indian economic development criticized the Indian government's development strategy and recommended greater liberalization, increased foreign assistance and currency devaluation.

Starting with the Bell Mission from the World Bank, the Indian government accepted and then implemented the required policy changes including the June 1966 rupee devaluation. But the results for trade and industry were unsatisfactory and the liberalization process was halted, the devaluation of rupee was seen as both externally imposed and ineffective and the promised aid failed to arrive. In any case, a reputation became increasingly less feasible as the relative importance of aid flows to the Indian economic sector fell in the 1970s [3]

The World Bank and the Aid India Consortium were seen by many Indians as linked with one over powering donor USA, both in seeking to influence Indian Macro policy excessively and ideologically and subsequently in not succeeding in mobilizing the aid promised. For example, in 1979, the Aid India Consortium meeting headed by World Bank, US in preparatory documents discussed at consortium meetings pressed for import liberalization, export development, and preference for private sector. The US mainly via World Bank encouraged India towards diversified private sector provision of contraceptives [4].

1.2. World Bank and Structural Adjustment Lending

The process of liberalization was especially started from 1980 onwards, when the World Bank's programme of structural adjustment lending was initiated. Loans were given only if appropriate programs were accepted and implemented by borrowers. These were the programs of stabilization by controlling the demand side of the economy, structural adjustment, supposedly designed to free the supply side by removing those macroeconomic market imperfections created largely by state intervention. The words, liberalization and stabilization/structural adjustment have become synonyms [5]. The difficulties of World Bank mediated policy dialogue are different and more fundamentals. The difficulty is the growing pressure upon the World Bank to remove increasing parts of aid to India from IDA, by arguing that the need of these IDA credits are essential for African countries, which cannot borrow commercially. This because the loan from IDA are so concessional as to be worth over 85 percent of a grant the same amount and far below commercial bank rates available to India [6].

Some measures to liberalize industrial policies were also taken in the early 1980's, but these gathered momentum only after 1990, when the external payments crisis raised and Indian government accepted the World Bank-IMF package of economic reforms. World Bank has played a central role in the experience-based criticism by continuously emphasizing the negative economic effects of exclusive state interventions. Regarding the involvement of the state in the procurement of material infrastructure, the establishment and running of communications systems and with respect to provision of public services like electricity, water supply, the World Bank emphasized that the public enterprises generally have a poor performance record. They have functioned ineffectively and inefficiently. The lack of infrastructure, financial resources technical capacity and bureaucracy have created problems for the private sector for example, many companies had to install backup diesel generators because of the frequent power cuts [7].

World Bank policy agenda for developing countries says that growth in the world economy will help the developing countries to industrialize, but for efficient industrialization their own domestic policies are much more important. In this regard trade policy reform is a top priority. The fundamental goal should be to increase competitiveness in world markets. World Bank says that the countries which adopted outward-oriented trade strategies have outperformed those that followed inward-oriented trade strategies-in income growth, export growth, employment, and savings. An outward oriented trade strategy means lowering trade barriers, replacing quantitative restrictions with tariffs, and adopting realistic exchange rates. The objectives are to improve resource allocation, to force domestic firms to become more efficient by having to compete with foreign firms, and to open the economy to new opportunities [8].

Replacing quantitative restrictions with tariffs is a useful first step. It lets firms operate in a less restrictive environment, allows them to buy imported inputs more easily, and removes the incentives for unproductive activities. The next step is to lower the level and variation of rates of protection. The simpler the scheme, the better. Getting off to a bold start seems to strengthen the credibility of reforms [9].

1.3. World Bank and Industrial Sector in India

Although agriculture is the main sector in Indian economy, the Industrial sector started occupying important position since second five-year plans, which started in 1956. In the early 1950's the textile industry dominated the industrial field. Iron and steel industry and coal production were limited and fertilizer production was virtually nonexistent [10].

The World Bank policies in Indian industrial sector started taking shape in 1953, when a three-men mission sponsored by US government and the World Bank mission visited India. On the basis of this commission's instructions to facilitate the close integration of private capital with foreign capital the government established the Industrial Credit and Investment Corporation of India (ICICI) in January, 1955. The primary purpose for which the ICICI makes available funds is for the purpose of capital assets in the form of land, building and machinery. The ICICI is a privately owned and managed corporation setup in 1954. It was established for assisting the growth of private industry in India [11]. Development finance companies play a vital role in the mobilization of capital for industrial and commercial development by providing loan or equity finance by under writing security issues, by serving as financial intermediaries between local and foreign businessmen and by providing locally established companies with managerial and technical advice.

On the advice of this mission, the government announced the Industrial policy in 1956. The 1956 policy marked the areas in which private sector can expand in an uninhibited manner.

Since 1956, among industrial investments particular emphasis was given to engineering industries. The IBRD has given \$ 176.9 million loans to assist the two private steel producers, the Indian Iron and Steel Company (IISCO) and the Tata Iron and Steel Company (TISCO), in expanding their output from 1.3 million tons in 1955 to 3.3 million tons of steel in 1965. This was the World Bank's first loan in the manufacturing field to be made directly to a private company with guarantee of the Indian Government [12].

At the request of the Nehru Government in 1960 the World Bank sent a mission composed of three members. On the basis of this mission's report, which suggested the forming of an investment center to advice collaboration ventures between the multinational corporations and Indian companies, in order to bring foreign investments to the Indian markets, in February, 1961 the Government of India inaugurated the Indian Investment Center. It was a autonomous body with branches in world capital markets such as New York, London and Tokyo [13].

In the beginning of 1960's, World Bank criticized the direction of Indian economic policy. In 1964, Bell commission sent by World Bank to study the Indian financial sector development issued a report calling for the devaluation of rupee and abolition of many of the foreign trade controls then in effect. It said, there is no particular evidence that the licensing system has in fact served any positive economic purposes. It has like the import control system, protected and preserved inefficiency by in effect, allotting market shares and restraining the growth of more efficient enterprises. Bell commission criticized the government's development strategy and recommended greater liberalization, increased foreign assistance and a currency devaluation [14].

Based on these recommendations, the Government of India announced the devaluation of rupee by 3.75 percent and the associated import liberalization measures in June 1966. To save from the foreign exchange problems, India received \$ 465 million from the World Bank [14].

To cater the ever increasing demand for coal in industrial production, the Government took number of measures to allow private companies to expand production, including a system of subsidies for mines with difficult operating conditions, permissions to open new mines and an assurance of policies favourable to continued mining by private companies. The World Bank advanced in 1961, a loan of \$28.8 million to assist the private coal mining industry in expanding production. Private companies as a part of their programme, intended to expand existing facilities and open new mines to increase their annual production of coal from 44 million to 61 million tons. The loan provided foreign exchange required to import necessary equipment [15].

With the introduction of new agricultural policy viz., the Green Revolution, that emphasized the development and growth of high yielding seeds requiring irrigation and heavy applications of fertilizers, the demand for fertilizers went up dramatically. The World Bank helped to increase the fertilizer production through assisting loan of about \$ 100 million in January, 1975, to construct a plant in Phulpur (UP), to produce 900 tons of ammonia and 1,500 tons of urea per day [16].

In its Industrial Policy Statement, 1980, the Government felt that the productive capacity as endorsed in the original licenses may not reflect the full potential of the production unit and the productive capacity may have increased by increased Labour productivity and technological development. In 1988 Indira Gandhi Government decided to consider induction of advanced technology and permit creation of capacity, large enough to manage competitively in world markets provided substantial returns. This was the first step in the direction of liberalization advocated by World Bank [17].

In 1985, the Rajiv Gandhi Government undertook the industrial reforms further in industrial licensing and regulatory policies, like [18] de-licensing of 25 industries, despite the fact that other restrictions such as licensed import of equipment, clearance form Monopolies and Restrictive Trade Practices (MRTP) which was established in 1951, commission etc., continued, board banding of products which helped relaxation of restrictions on product diversification by a producer, the exemption limit for asset size qualifying for MRTP scrutiny was raised from Rs.20 crores to Rs.100 crores. There was other minor liberalization measures in respect of reservation to small-scale sector, entry of private sector in telecommunications equipment manufacturing. But the Indian economy basically continued to be a closed one, without ensuring competition either from within or from outside.

The new Industrial Policy of 1991 was prompted by the World Bank principles, which in a way were instrumental in bringing about radical departure from the earlier regulatory policies to liberalization of the economy. The new Industrial Policy was part of a package of economic policies, comprising, a part from the new industrial policy, the policy regarding import tariffs, direct taxation, inclusive of corporate taxes, reforms in the financial sector, inclusive of structural changes in the banking sector. The major components of Industrial policy are Industrial licensing was abolished for all industries except for eighteen, irrespective of level of investments. In order to get advantages of technology transfer marketing expertise, introduction of modern managerial techniques and promotion of exports. The new Industrial policy provides for automatic approval of foreign technology agreements and 51 percent foreign equity proposals in 34 high priority industries, which require large investment and advanced technology. Direct foreign investment in equity exceeding 51 percent would also be encouraged in high priority industries subject to approval by the Foreign Investment Promotion Board (FIPB), which was set up for that purpose [19].

The World Bank has made repeated references to institutional constraints coming in the way of effective implementation of liberalized economic policies, and in particular investment and Industrial policies. It says that, the legacy of India's developmental policies is embedded in sector level policies and institutional frame works, which do not support private investment, and recommends, "extending the reform process to sectoral ministries, the states, and public enterprises" [20].

2. CONCLUSION

Based on the observations on the association of World Bank in India's industrial policy, it is imperative to say that since India's second five year plan which emphasised on the Industrialisation, World Bank started playing a key role in not only involving in the process but also in shaping the policies in later decades. But only after the liberalisation such involvement strikingly met with huge criticism as its lending was more attached with policy prescriptions and guidance. As long as the government kept with it the liberty to shape the industrial policy before liberalisation such flexibility received a setback with the bank SAP approach by a section of people. In the later stages of liberalisation period government of India slowly started withdrawing from public sector and private participation in industrial activities has been encouraged on the lines of World Bank prescriptions "extending the reform process to sectoral ministries, the states, and public enterprises". As a result new set of standards, competition among players, including sectors and states been carried out. At states level various policies to attract private investment both domestic and foreign investments vehemently being designed and pursued as the development practice. A close analysis of this trend has further widened the gap between states which existed in the pre-liberalisation period as industrialised and non industrialised states, resulting further socio-economic-human relations and complexities.

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