

# **Economic Reforms in India: A Macro-Theoretic Study**

## **Synopsis**

### **1. Introduction**

The objective of my Ph.D. thesis is to examine the macroeconomic implications of economic reforms in India. The distinguishing feature of this thesis is that it is based on the hypothesis that a capitalist economy is completely under the control of the capitalists. They dictate all the policies and regulate all the macroeconomic phenomena such as the growth rate, the rate of inflation and employment. This is in sharp contrast with the position of mainstream macroeconomics (comprising the neoclassical macroeconomics and the Keynesian macroeconomics), which assumes that a capitalist economy does not have a driver. It is driven by impersonal market forces and the objective of economics is to examine how these forces work and what outcome they produce.

The thesis has three core chapters: Chapters 2, 3 and 4. Using a macro model it develops, Chapter 2 shows how reforms in the financial sector and deregulation of investment and prices benefit the capitalists at the expense of the masses. Using the same model, Chapter 3 shows how the reforms in the monetary policy recommended by the New Economic Policy (NEP) adopted in India in 1991 impoverishes the masses and makes the capitalists richer. Finally, Chapter 3 focuses on the reforms undertaken in the realm of fiscal policies and shows how they heap riches on the capitalist at the expenses of the masses. In what follows, we will present in brief the contents of all these three chapters.

### **2. Chapter 2: Economic Reforms and the Common Man in India**

India adopted the New Economic Policy (NEP) in 1991 replacing the Nehru-Mahalanobis Strategy (NMS) of economic development. The NEP is being implemented in India since 1991 through a series of Economic Reforms. The objective of the NEP is to privatize all the public sector enterprises and to establish free market by removing all kinds of restrictions and regulations of the NMS era. In other words, the objective of the NEP is to handover all the capital and natural resources of the country to the capitalists (the giant businessmen who control India's corporate sector) and to give them a free hand in running and managing their businesses. We will examine here the implications of some of the Economic Reforms for the capitalists and the common man through their impacts on the organized and the unorganized sectors in India. The question that naturally emerges here is why the Government of India is implementing the NEP and why the political parties in India have accepted the NEP. This is surprising because India is a democratic country. In a democracy, more than one party compete for State Power. Every adult citizen of a democratic country has one vote irrespective of his economic condition. Thus, democracy grants political equality. A general election is held every four or five years. The political party that gets the majority of the votes gets to exercise State Power until the next general election is held. In these circumstances, one would expect every political party to work for the masses who wield

more than ninety-nine percent of the votes. If the political parties work for the masses, the political party in power should confiscate all the wealth of the capitalists and distribute them among the masses. It should nationalize the entire business empire of the capitalists and run it in the interest of the masses so that the masses get all the incomes and benefits from them. Thus, the political equality granted by democracy should eliminate economic inequality and establish an equal society overnight. Therefore, capitalists and capitalism cannot survive democracy. However, this never happens. Democracy does not threaten the capitalists or capitalism in any manner. In fact, the political parties in a democracy behave exactly in the opposite manner. They forcibly take away the land of the poor and give it away to the capitalists free of cost. This is definitely a mystery. Obviously, it is necessary to resolve this mystery in order to gain an understanding of how a capitalist society in general and India in particular work. We try to do it below.

A political party in a capitalist country does not have any source of income of its own. However, to set up and run a political party, an enormous amount of fund is needed. A political party requires a nation-wide network of dedicated workers, access to all kinds of media etc. The larger the amount of fund at the disposal of a political party, the greater is its competitive strength. Accordingly, only the wealthiest of the people can set up and run political parties. Thus, only the capitalists have the resources to set up and run political parties and they do so like their other country-wide or world-wide enterprises and, thereby, usurp State Power. Using the State Power, they keep the masses under control and secure their enormous wealth and business empire from the masses.

In a capitalist country, therefore, just like all the basic necessities of life and justice, the State Power is also an object of purchase and sale and it gets sold-off to the highest bidder.

Democracy is, therefore, a sham and the actual rulers of a capitalist country get themselves hidden behind an elaborate facade of political parties and the government. The capitalists love this camouflage so much that they call their countries not capitalist countries but democracies. Why do the capitalists, the actual rulers of the capitalist countries, get themselves hidden? They do so in order that the anger of the people due to the misery and suffering a capitalist society perpetrates on them get directed not towards the capitalists but towards the leaders of the political party in power, whom the people have themselves chosen as their ruler. Democracy also gives the people a way of giving vent to their anger. They do so by voting out the political party in power and bringing in another political party. The question that emerges is why capitalist societies make people's lives miserable. We will answer this question below.

If the workers have substantial bargaining strength, they can force the capitalists to raise their wage rates to such high levels that the capitalists may even suffer losses. Hence, the capitalists seek to ruin the bargaining strength of the workers by creating large scale unemployment through different means. They invest on a massive scale in R&D to innovate technologies that make the production process more automatic. They continuously incorporate these technologies in the production process to reduce labour requirement of production. They also keep the growth rate of aggregate production on the average at such a low level that the rate of growth of jobs falls short of the rate

of growth of the labour force. In these ways, the capitalists create large scale and growing unemployment to destroy the bargaining strength of the workers. (For details of the view presented above, go through Ghosh and Ghosh (2019<sup>a</sup>, 2019<sup>b</sup>)). From the above it is clear why all the political parties who come to power in India try to implement the NEP, which seeks to hand over the country to the capitalists at an enormous cost to the masses.

The point to note in this context is that the capitalists who control India are not the Indian capitalists, but the capitalists of Western Europe and the USA, which are the leading capitalist countries of the world and colonized almost the whole of the rest of the world by the time the First World War had begun. The reason we say this is the following. The most important feature of India at the present is that it is completely dependent on the Western European countries and the US for knowledge and technology. Let us illustrate this claim with an example. Think of the case of teaching economics in India. All the text books we refer to are imported from the Western European countries and the US. All the journals we refer to are imported from the Western European countries and the US. All the computers and also all the software we use are bought from the companies of the US or West European origin. This is true of not only economics but also all other subjects. Thus, to set up an educational institute in India, all the knowledge inputs and all the hi-tech inputs have to be imported. This is applicable not only to the educational institutes but also to all the modern production facilities in India. Thus, to set up a bank in India, for example, all the computers, software and high-tech machines have to be imported from the US or Western European countries. India, therefore, has to import on a large scale to sustain its production and investment. However, to import from the Western Europe and the US, India requires currencies of these countries. To earn these currencies, India has to sell its products to these countries. Since India produces its goods and services with imported knowledge and technology, which are never state-of-the-art, India's ability to compete in the world market is virtually nil. Therefore, India cannot get itself going. How does it survive then? The only plausible hypothesis seems to be that the Western capitalists, that is, the capitalists of the US and Western Europe, who have in their control almost all the enterprises and the governments of these countries, get India going by placing export orders with it and by buying India's bonds and stocks on a very large scale (see in this context Chapter 8 of Ghosh and Ghosh (2016) for evidential support) providing India with the requisite amount of foreign currency. Accordingly, India has to abide by the dictates of the Western capitalists at every step. Therefore, India is independent only on paper. It is virtually a colony of the Western capitalists. Since Indian capitalists do not have any independent base of knowledge and technology, they have no competitive strength vis-à-vis the Western capitalists and cannot survive as capitalists on their own. They are, therefore, one may safely presume, merely the representatives of the Western capitalists managing their businesses in India. Thus, the political parties in India are also owned and run by the Western capitalists. Hence, it is the Western capitalists who rule India and run all the large businesses in India. But, at the present, they do so not directly as in the colonial days but indirectly through their Indian representatives. To show how the capitalists rule India, we divide India into two sectors: the organized sector and the unorganized sector. The former consists of the corporate sector, public

sector enterprises and large unincorporated private enterprises. The unorganized sector consists of small enterprises including small farming units and cottage and village industries. We will delineate the relevant main features of the two sectors below:

### The Organized Sector

Following Keynes(1936), we assume that aggregate output in the organized sector is demand determined and the prices are set by the capitalists and the government. We will not try to explain in this model how capitalists and the government set the prices of their products and simply assume the average price in the organized sector to be given. We will denote the output and the price of the organized sector by  $Y$  and  $P_Y$  respectively. From the data given in Tables 2.1 and 2.2 in Chapter 2, we find that the share of the organized sector in GDP has grown steadily in the post-reform period. This means that the output of the organized sector has grown at a higher rate than the GDP in the post-reform period. However, even though the organized sector has grown at a high rate in the post-reform period, employment in the organized sector remained more or less fixed. This implies that along with growth in output, there has been taking place continuously labour saving technological and managerial changes enabling the producers to expand their output without generating any employment. Hence, we will assume the employment level in the organized sector to be fixed. We will denote this fixed level of employment in the organized sector by  $\bar{N}$ . (Note that the recent data on employment, which are, of course, not comparable to the data referred to above, have shown that the employment in the organized sector has grown with its output. Note that, even if we make employment in the organized sector an increasing function of its output, all our results will go through.) Given these assumptions, the equilibrium condition of the organized sector may be written as follows:

$$Y = c_c \cdot \left( Y - \frac{W}{P_Y} \bar{N} - \frac{Br_0}{P_Y} \right) + c_w \cdot \alpha \left( \frac{P_X}{P_Y}, R \right) \cdot \left( \frac{W}{P_Y} \bar{N} + \frac{Br_0}{P_Y} \right) + I + a\tilde{X} \quad (2.1)$$

Let us now explain (2.1). The expression on the RHS represents aggregate demand for  $Y$ . We have divided the people who take part in the production of  $Y$  into two classes: the capitalists and workers. The capitalists earn profit and we have denoted their fixed average and marginal propensities to consume by  $c_c$ .  $W$  denotes money wage rate. Workers are under the compulsion to save to tide over periods of unemployment, illness and old age. They hold their entire saving, by assumption, in the form of bank deposits.  $B$  denotes the stock of bank deposits of the workers outstanding at the beginning of the given period under consideration and  $r_0$  denotes the average interest rate applicable to  $B$  and it is, obviously, given in the given period.  $Br_0$  is the interest income of the workers in the given period. Workers' fixed average and marginal propensity to consume is  $c_w$ . As workers are much poorer than the capitalists, it is standard to assume that  $c_w$  is larger than  $c_c$ . However, the workers allocate their consumption spending between the outputs of the organized sector and the unorganized sector. Consumption goods produced by the two sectors are substitutes. Note that the unorganized sector compete with the organized sector almost in every area such as food, clothing, shelter, repair and servicing, education and healthcare. We assume that the workers

spend  $\alpha$  fraction of their total consumption spending on  $Y$  and  $\alpha$  is an increasing function of  $\frac{P_X}{P_Y}$ , where  $P_X$  denotes the price of the output of the unorganized sector. During the Nehru-Mahalanobis era, a number of sectors such as textiles, agriculture, arricultural trade, retail etc, were reserved for the small producers only. However, the NEP through the process of economic reforms is gradually removing these restrictions. We denote the level of these restrictions by  $R$ . A fall in  $R$  indicates a decline in these restrictions. Obviously,  $\alpha$  is a decreasing function of  $R$ .  $I$  denotes investment of the organized sector. The standard assumption regarding  $I$  in the mainstream economics is that it is a decreasing function of the interest rate. However, as we have argued above, in a capitalist country, the capitalists have in their complete control all the prices and interest rates. In such circumstances, we consider it reasonable to postulate that the capitalists raise  $I$  to the maximum possible level so that  $Y$  is at its full capacity level, denoted  $\bar{Y}$ . This they do to maximize their command and use of produced goods and services so that they can use the maximum possible amount of produced goods and services to set up facilities for producing newer varieties of luxury consumption goods, better varieties of existing consumer goods and for making production less labour intensive. We divide the output of the unorganized sector, which we denote by  $X$ , into two parts. One part is produced without using any intermediate input bought from the organized sector. We denote this part of the output by  $\bar{X}$ . The other part of its output, which is produced with intermediate inputs bought from the organized sector is denoted by  $\tilde{X}$ . Finally,  $a$  denotes the requirement of  $Y$  per unit of production of  $\tilde{X}$ . Since it is not relevant for our purpose at the present, we have not incorporated taxes and government consumption in (2.1). We will incorporate them shortly. Substituting  $\bar{Y}$  for  $Y$  in (2.1), we rewrite it as follows:

$$\bar{Y} = c_c \cdot \left( \bar{Y} - \frac{W}{P_Y} \bar{N} - \frac{Br_0}{P_Y} \right) + c_w \cdot \alpha \left( \frac{P_X}{P_Y}, R \right) \cdot \left( \frac{W}{P_Y} \bar{N} + \frac{Br_0}{P_Y} \right) + I + a\tilde{X} \quad (2.2)$$

### The Unorganized Sector

We assume that the producers in the unorganized sector are credit constrained. They need loans to buy the essential intermediate inputs from the organized sector. As they have little collateral to offer, they are able to secure only a small amount of loan, which does not enable them to fully utilize the labour, capital and land they have in their command. They produce the output using only family labour. We denote the given amount of loan they are able to secure by  $L_X$ . Hence, the amount of  $X$  they are able to produce with the loan is given by  $\frac{L_X}{aP_{YX}}$ , where  $P_{YX}$  is the average price of the intermediate inputs. We also assume that even if the producers fail to secure any credit and buy any input from the organized sector, they are able to produce a given amount of output, which we denote by  $\bar{X}$ . If they can secure loan, they can utilize their land and capital more intensively and raise their output above  $\bar{X}$ . (For example, farmers can produce some crop in their land using traditional technology and inputs, which they themselves produce. Similarly, weavers and handlooms can produce some clothing without using inputs of the organized sector.) We further assume that the producers of the unorganized sector keep aside  $\beta$  fraction of their output for self-

consumption and investment and sell the rest in the market. Denoting the market supply of X by  $X^S$ , we get

$$X^S = \left(1 - \beta \left(\bar{X} + \frac{L_X}{P_{YX}} \frac{1}{a}\right)\right) \left[\bar{X} + \frac{L_X}{P_{YX}} \frac{1}{a}\right] \quad (2.3)$$

Let us explain (2.3). Quite a large part of the output of the unorganized sector consists of the basic necessities of life such as food, clothing, shelter etc. Since small and marginal farmers cultivate about 85 percent of India's arable land (see NAABARD (2021)), almost the whole of agriculture is a part of the unorganized sector and it is by far the largest segment of the unorganized sector. Since producers are heterogeneous in terms of their command over land and capital, we consider it reasonable to assume that the larger the X, the greater is the fraction of the producers who will be able to produce more than their subsistence requirement. Hence, we make  $\beta$  a decreasing function of X. The implication of this assumption is that many producers require loans to produce even the subsistence level of their output and if  $L_X$  falls below a certain minimum level, many producers may not be able to pay back their loans and may, thereby, lose their land and capital.

We assume that demand for X in the market comes only from the workers of the organized sector. Denoting it by  $X^D$ , we get

$$X^D = c_w \cdot \left(1 - \alpha \left(\frac{P_X}{P_Y}, R\right)\right) \cdot \left[\frac{W \cdot \bar{N} + Br_0}{P_X}\right] \quad (2.4)$$

Therefore, the unorganized sector is in equilibrium when the following equation is satisfied:

$$c_w \cdot \left(1 - \alpha \left(\frac{P_X}{P_Y}\right)\right) \cdot \left[\frac{W \cdot \bar{N} + Br_0}{P_X}\right] = \left(1 - \beta \left(\bar{X} + \frac{L_X}{P_{YX}} \frac{1}{a}\right)\right) \left[\bar{X} + \frac{L_X}{P_{YX}} \frac{1}{a}\right] \quad (2.5)$$

We assume that the producers of the unorganized sector use the sales revenue to pay back their loans along with interest. They save the excess of the sales revenue, if any, over the debt service charges in the form of currency to tide over emergencies such as sudden illness, natural calamities, repairing of implements, treatment of animals etc. Since these producers are semiliterate or illiterate and since the bank branches may be located in far off places, the transaction cost of holding their small savings as bank deposits may be prohibitive. We make this assumption for analytical simplicity. Our results will go through even under more general assumptions. Normally, most of these producers are too poor to make any saving. Hence, it is unlikely to cause much harm, if we ignore their saving.

Regarding investment in the unorganized sector, we make the following observation. Most of the small investments made by the unorganized sector producers are produced in the unorganized sector and are included in the  $\beta$  fraction of output kept aside for self-use. Government supplies the unorganized sector with infrastructure inputs such as water, power, drainage, roads etc.

Our specification of the unorganized sector is complete.

Substituting for  $X$  its value in (2.2), we rewrite it as follows:

$$\bar{Y} = c_c \cdot \left( \bar{Y} - \frac{W}{P_Y} \bar{N} - \frac{Br_0}{P_Y} \right) + c_w \cdot \alpha \left( \frac{P_X}{P_Y}, R \right) \cdot \left( \frac{W}{P_Y} \bar{N} + \frac{Br_0}{P_Y} \right) + I + \frac{L_X}{P_{YX}} \quad (2.6)$$

We will now delineate the financial sector.

### The Financial Sector

The financial sector consists of the RBI and the commercial banks only. We will henceforth refer to the latter as banks. Both the capitalists and the workers of the organized sector hold their savings as bank deposits. The banks hold a fraction  $\rho$  of their deposits as cash reserve and lend out the rest. We make  $\rho$  a decreasing function of the interest rate  $r$ . However, the monetary policy of the RBI consists in keeping  $r$  at a target level  $\bar{r}$ . Hence, the supply of new bank loans in the period under consideration, denoted  $L^S$  is given by

$$L^S = (1 - \rho(\bar{r})) \cdot \left[ (1 - c_c) \cdot \left( Y - \frac{W}{P_Y} \bar{N} - \frac{Br_0}{P_Y} \right) + (1 - c_w) \cdot \left( \frac{W}{P_Y} \bar{N} + \frac{Br_0}{P_Y} \right) \right] \quad (2.7)$$

The capitalists finance their entire investment of the corporate sector with new bank loans. The banks give a given  $L_X$  amount of new loans to the producers of the unorganized sector. Therefore, the equilibrium in the financial sector is given by the following equation:

$$(1 - \rho(\bar{r})) \cdot \left[ (1 - c_c) \cdot \left( Y - \frac{W}{P_Y} \bar{N} - \frac{Br_0}{P_Y} \right) + (1 - c_w) \cdot \left( \frac{W}{P_Y} \bar{N} + \frac{Br_0}{P_Y} \right) \right] + b = I + \frac{L_X}{P_{YX}} \quad (2.8)$$

In (2.8),  $b$  denotes the RBI's new lending to the banks in the period under consideration. It may be positive or negative. If at  $\bar{r}$ , there emerges an excess demand for new bank loans, the RBI lends to the banks so that they can meet the excess demand. In this case,  $b$  is positive. On the other hand, if there emerges an excess supply at  $\bar{r}$ , the banks lend out their excess supply of loans to the RBI. In this case,  $b$  is negative. This is how  $r$  is kept at  $\bar{r}$  by the RBI.

The specification of our model is now complete. It contains three key equations (2.5), (2.6) and (2.8) in three endogenous variables  $P_X, I$  and  $b$ . We can solve them for the equilibrium values of the three endogenous variables. We can use this simple model to show how the New Economic Policy (NEP), which is being implemented through the process of economic reforms, enables the capitalists to expand their businesses at the expense of the unorganized sector. This is extremely worrying since more than ninety percent of the labour force works in the unorganized sector and the fraction of the labour force engaged in the unorganized sector is also steadily rising. Clearly, therefore, if the organized sector expands at the expense of the unorganized sector, it will increase immensely the poverty and misery of the masses. We will first focus on the implication of financial sector liberalization in this respect.

## 2.1 Financial Sector Liberalization

The NEP came into force in 1991 replacing the Nehru-Mahanobis Strategy (NMS). Under the latter, the ownership and control of the financial sector rested solely with the government. The government administered all the interest rates and directed the financial institutions how much to lend to each of the different sectors so that the plan targets of production and investment were fulfilled. Through this directed credit programme, the government provided the unorganized sector with large amounts of loans at very low interest rates so that the unorganized sector could grow at a fast rate ensuring high rates of growth of both employment and supply of mass consumption goods. The government regarded the unorganized sector as the priority sector and specified the priority sector lending norm which made sure that the producers of the unorganized sector did not suffer any dearth of credit. Under the NMS, the financial institutions were not commercial organizations. They were social organizations and their purpose was to mobilize all the savings of the masses by providing them with completely safe and remunerative avenues of saving and to utilize this saving in such a manner that the plan targets of production and investment were fulfilled. The NEP, however, seeks to dismantle the directed credit programme, make the financial institutions profit driven and privatize the financial sector so that the market forces determine the allocation of resources. In other words, one of the objectives of the NEP is to transfer the ownership and control of the financial sector from the government to the capitalists enabling the latter to determine the interest rates and allocation of credit across different sectors, firms and individuals. The Government of India (GoI) is seeking to achieve this objective through the process of financial sector reforms. The reforms have already dismantled the directed credit programme diluted the priority sector lending norms substantially and made the financial institutions profit driven commercial organizations and given them the autonomy to set the interest rates and take their lending decisions. The government has also imposed on the banks lending norms that have made them extremely wary of lending to the risky borrowers. Moreover, in banks' parlance, the poorer a borrower the greater is the risk of lending to him. The government has also withdrawn its guarantee of bank deposits, which have made bank deposits unsafe and banks more cautious regarding their lending. We will denote all those factors that make banks more cautious regarding their lending by  $\gamma$ . Using our simple model, we will try to capture the implications of these changes. At the present, the imposition of Basel norms, which put great emphasis on the risk-weighted capital adequacy ratio, has made profit-driven financial institutions extremely cautious about lending to the small producers, who are financially weak. We, therefore, make  $L_X$  a decreasing function of  $\gamma$  and the degree of stringency of the Basel norms, which we denote by  $\emptyset$ . We also make it a decreasing function of the default rate of the small producers, which we denote by  $D$ . The analysis of chapter 2 shows that  $D$  is a decreasing function of  $X$  and  $R$  and an increasing function of  $r_X$ , where  $r_X$  is the interest rate at which the small producers receive loans. While the reason for  $D$  being a decreasing function of  $r_X$  is quite self-explanatory, the reasons why it is a decreasing function of  $X$  and  $R$  is not so. Let us, therefore, explain them briefly. If  $X$  goes up, given  $L_X$ , on account of a fall in  $a$  or  $P_{YX}$  or for some other reason, revenue of the small producers is found to go up lowering their default rate. Again, everything else remaining the same, if  $X$  rises

because of an increase in  $L_X$ , the revenue of the small producers is assumed to increase more than the debt service charges. This is said to be the boundary condition of the model. This lowers the default rate of the small producers. Again an increase in  $R$  lowers  $\alpha$  and it is found to increase the revenue of the small producers lowering their default rate.

Under the NEP, the financial institutions consider it extremely risky to lend to the small producers. Hence, they charge a risk premium, denoted  $\varepsilon$ , on the loans given to the small producers. While the large producers face  $\bar{r}$ , the small ones get loans at

$$r_X = \bar{r} + \varepsilon \quad (2.9)$$

Using (2.3) and (2.9), we get

$$D = D(X, r_X, R) = D\left(\bar{X} + \frac{L_X}{P_{YX}} \frac{1}{a}, \bar{r} + \varepsilon, R\right); D_X < 0, D_{r_X} > 0, D_R > 0 \quad (2.10)$$

From the above it follows that

$$L_X = \bar{F}\left(D\left(\bar{X} + \frac{L_X}{P_{YX}} \frac{1}{a}, \bar{r} + \varepsilon\right), \Phi, \gamma\right) \equiv F(L_X, \bar{X}, P_{YX}, a, R, r_X, \Phi, \gamma); \frac{\partial F}{\partial L_X} > 0, \frac{\partial F}{\partial a} < 0, \frac{\partial F}{\partial P_{YX}} < 0, \frac{\partial F}{\partial R} > 0, \frac{\partial F}{\partial \gamma} < 0, \frac{\partial F}{\partial \Phi} < 0 \quad (2.14)$$

We assume that  $F(D(\bar{X}, \bar{r} + \varepsilon), \Phi, \gamma) > 0$  and  $0 < F_D D_X X_{L_X} \equiv \frac{\partial F}{\partial L_X} \equiv f < 1$ . Under these conditions, we can solve (2.14) for  $L_X$ . We show the solution of (2.14) in Figure 2.1 below:

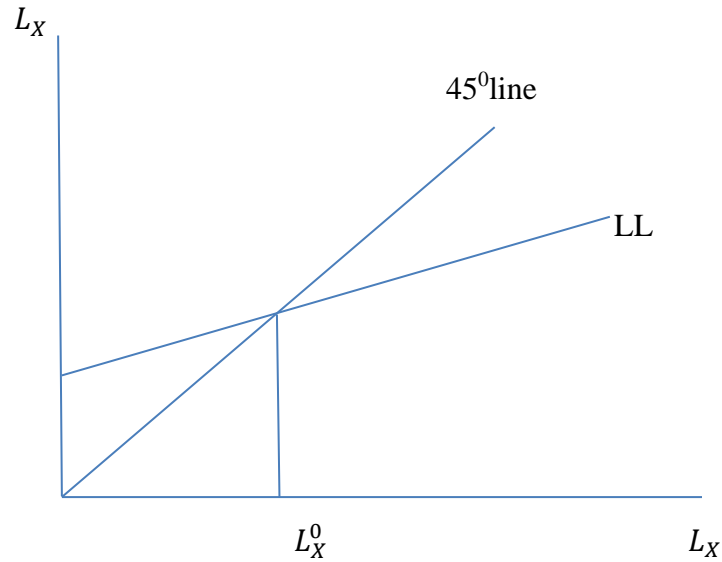


Figure 2.1

In Figure 2.1, LL represents (2.14) and the equilibrium  $L_X$  corresponds to the point of intersection of LL and the 45° line. The equilibrium  $L_X$  is denoted  $L_X^0$ . Putting this equilibrium value of  $L_X$  in

(2.3), we get the equilibrium value of  $X$ . Putting the equilibrium value of  $L_X$  or that of  $X$  in (2.5), we can solve it for the equilibrium value of  $P_X$ .

Using the model developed above, we have examined how an increase in  $\gamma$  and  $\emptyset$  affect  $X$  and  $I$ . We have also examined how withdrawal of government guarantee of bank deposits, bank fraud, price deregulation and relaxation of control on investment affect  $X$  and  $I$ . In other words, we have shown here how financial sector reforms, deregulation of investment and prices have benefited the capitalists at the expense of the masses.

### **Impact of Financial sector Reforms**

We have examined first how financial sector reforms are likely to impact the economy. They have made banks profit driven, imposed on the banks lending norms that have made the banks extremely wary of lending to the small borrowers. In other words, these reforms have substantially raised  $\gamma$  and  $\emptyset$  reducing on a large scale the supply of loans to the producers of the unorganized sector. This reduces  $X$  creating an excess demand for  $X$  at the initial equilibrium  $P_X$ . The increase in  $P_X$  restores equilibrium in the  $X$  market by inducing the workers of the organized sector to switch their spending from  $X$  to  $Y$ . The consequent decline in the revenue of the producers of  $X$  is, by assumption, larger than the fall in their debt service charges. Hence, their bankruptcy rate increases reducing loan supply to them further. Thus, there will take place a cumulative contraction in the output of the  $X$ -sector. The fall in demand for  $Y$  of the  $X$ -sector is likely to enable the capitalists to raise their investment despite the increase in the workers' consumption of  $Y$ . We, therefore, get the following proposition:

**Proposition 2.1:** Financial sector reforms are a weapon at the disposal of the capitalists to increase their market share at the expense of the unorganized sector creating mass unemployment and poverty. These reforms are also likely to allow the capitalists to grab a larger fraction of the GDP for their own use at the expense of the masses.

In order to fully appreciate the implications of the cumulative contraction in the output of the unorganized sector following the financial sector reforms, one has to take into account the following facts. From the data given in Tables 2.1 – 2.4 in Chapter 2, we find that the organized sector employed only 6 percent of the work force in 2004-05. The employment in the organized sector had been virtually stagnant during 1994 – 2014, while the work force had been growing at the rate of more than 2 percent per year during 1999-00 to 2004-05. There is no reason to believe that these trends have reversed since then. Hence, it may be safe to say that close to 99 percent of the Indians derive their livelihood from the unorganized sector at the present and the percentage of people surviving on the unorganized sector is rising steadily. Under these circumstances the cumulative contraction in the output of the unorganized sector due to the financial sector reforms is a cause of major concern. It will lead to a substantial increase in the level of unemployment and poverty threatening the survival of the ordinary Indians.

### **Deregulation of Prices**

During the Nehru-Mahalanobis era, prices of all the essential industrial goods were administered by the government. The government also provided the small producers with inputs at highly

subsidized prices. Economic reforms under the New Economic Policy (NEP), however, have done away with price regulation and input subsidy. In the post-reform period, therefore,  $P_{YX}$  has gone up steeply. This reduces X creating an excess demand at the initial equilibrium  $P_X$ .  $P_X$ , therefore, increases lowering M ans raising VS until the two become equal at a lower value. The fall in revenue raises the default rate lowering the supply of loans to the small producers. Hence, X falls again. Thus, there takes place a cumulative fall in X enabling the capitalists to grab more of the market of the unorganized sector. The capitalists may also be able to raise their consumption and investment. This yields the following proposition:

**Proposition 2.3:**  $P_{YX}$  is an instrument of exploitation at the disposal of the capitalists. By raising it, they bring about a cumulative contraction in the output of the unorganized sector that produces for the masses and employs in India in all likelihood more than ninety-nine percent of the work force. This leads to a substantial increase in unemployment and poverty. The capitalists grab more of the market of the unorganized sector and may be able to use the resources released from the production of X to raise their consumption and investment.

## 2.5 Forcible Acquisition of Land of the Small Producers

**In the** post-reform period, laws have been passed to facilitate forcible acquisition of land of the small producers. This lowers the collateral of the small producers. As a result supply of loans to them falls leading to, through the process described in the earlier cases a cumulative fall in the output of the unorganized sector. This yields the following proposition:

**Proposition 2.4:** Forcible acquisition of land of the producers of the unorganized sector will lead to a cumulative decline in the output of the unorganized sector bringing about a substantial increase in unemployment and poverty. This will enable the capitalists to grab more of the market of the unorganized sector and may enable the capitalists to raise their investment on a large scale

## 2.6 Decline in Public Investment in Infrastructure for the Unorganized Sector

Mishra (2006), Godaraet. al.(2014)) show that public investment in agriculture, which is by far the largest segment of the unorganized sector, has declined steadily in the post-reform period. This steady fall in public investment may lead to deterioration in the quality of services provided by the already existing public infrastructure facilities. Hence, quality and quantity of the supply of power, water etc. may deteriorate; drainage and flood control facilities may lose gradually their efficiency. Hence, the producers of the unorganized sector may get less protection from the adverse impacts of drought, water logging, flooding etc. Hence, the productivity of the intermediate inputs they use may fall. In terms of our model, the fall in public investment in the area specified above may bring about an increase in  $a$ . This in turn, just as in the earlier cases, will lead to the following proposition:

**Proposition 2.5:** A decline in public investment in agriculture will bring about a cumulative contraction in the unorganized sector causing cumulative increase in unemployment and poverty. This will enable the capitalists to grab more of the market of the unorganized sector and may enable the capitalists to raise their investment on a large scale

## 2.7 Conclusion

This study is based on the hypothesis that at the present India is under the complete control of the capitalists. They are making the Government of India undertake a series of Economic Reforms to implement the New Economic Policy (NEP), whose objective is to establish a free market and transfer the ownership of all the capital and natural resources to the capitalists. In sum, the NEP seeks to handover India to the capitalists so that they can run and manage India in whatever way they want. Our study shows that economic reforms in the financial sector and deregulation of prices coupled with forcible acquisition of land from the small producers and decline in public investment in agriculture lead to a large and cumulative shrinkage in the output of the unorganized sector enabling the capitalists to grab the market of the unorganized sector and have in their command a larger part of the aggregate output of goods and services for consumption and investment.

Since about 99 percent of the people derive their livelihood from the unorganized sector and the organized sector grows without generating any employment, the shrinkage of the unorganized sector is a matter of grave concern. If the capitalists, through the process of economic reforms and other means, succeed in obliterating the unorganized sector grabbing its market and resources, most of the ordinary Indians will perish. Thus, in the absence of mass awareness of and strong mass movement against capitalistic exploitation, ordinary people in India might be extinct.

### **3. Chapter 3: Monetary Policy in the Post-Reform Period and the Common Man in India**

During the Nehru-Mahalanobis era, monetary policy consisted in a credit policy. The financial sector became the exclusive preserve of the government. The government administered all the interest rates and determined the total volume of credit to be disbursed by the financial institutions and dictated the allocation of the total amount of credit across different sectors and economic agents. The financial institutions had to abide by the dictates of the government. The objective of the credit policy delineated above was to make sure that all the sectoral production and investment targets specified in the Five Year Plans were fulfilled and no leakage of credit took place in non-planned areas. The financial institutions were social organizations whose objective was not to make profit but to provide the people with fully safe avenues of saving and disburse credit in accordance with plan targets at interest rates administered by the government. The prices of all the non-agricultural essential goods and services were administered by the government. The financial sector and the credit policy were subservient to planning.

The New Economic Policy (NEP) that the Government of India adopted gave up planning and along with it the directed credit programme. It has opened up the financial sector to the private entrepreneurs, made the public financial institutions autonomous commercial organizations that are free to decide whom to lend, how much to lend and at what interest rates. The RBI under the NEP seeks to regulate the interest rates indirectly through policies such as open market operations (OMO), liquidity adjustment facility (LAF) etc. The RBI's monetary policy under the NEP consists in adoption of measures to reduce nominal interest rates to counter recession and to raise nominal interest rates to lower inflation rate when it goes beyond a tolerable level. The objective of this chapter is to subject this monetary policy to close scrutiny to unravel its ulterior motive.

We have used the model developed in the previous chapter for our purpose. We have based our study, as before, on the hypothesis that the capitalists drive a capitalist economy. It is they who create recession and inflation to exploit the masses. We will show here that the monetary policy delineated above instead of countering the recession reinforces them and, thereby, facilitates the process of exploitation. It is subservient to the objective of the capitalists.

### **3.1 Counter-Recessionary Monetary Policy**

As we have already pointed out, the monetary policy of the RBI consists in keeping the interest rate at a target level through policies such as the OMO, LAF etc. In times of recession, it cuts the interest rate to a low level. If that happens, workers' interest income in our model will fall. Hence, their spending on the output of the unorganized sector will fall. This will lower the revenue of the small producers raising their default rate. Loan supply to them will, therefore, fall reducing their output. This will set in motion, for reasons explained in the previous chapter, a cumulative process of decline in the output of the unorganized sector enabling the capitalists to grab the market of the small producers and, in all likelihood, raise their investment. This yields the following proposition:

**Proposition 3.1:** A cut in the interest rate brings about a cumulative contraction in the output of the unorganized sector and, thereby, deepens recession. It, therefore, brings about a cumulative increase in unemployment and poverty. It enables the capitalists to capture a part of the market of the unorganized sector. It is also highly likely that the capitalists will be able to use a larger part of the output of the organized sector for their own use.

### **3.2 An increase in $\emptyset$ or $\gamma$ and the Monetary Policy**

We will show here how the counter recessionary monetary policy deepens the recession generated by a change made by the capitalists in the value of an instrument of exploitation. Thus, the counter recessionary monetary policy facilitates the capitalists' plan of reducing the unorganized sector. We will establish this claim by considering the example where the capitalists using the State Power bring about an increase in  $\emptyset$ . Since  $\bar{r}$  is cut to counter recession, it should be a decreasing function of the output gap defined as the excess of the potential real GDP and the actual real GDP. In our perception, the recession remains confined to the unorganized sector. Hence, we will make  $\bar{r}$  an increasing function of  $X$ , since the potential level of  $X$  is given. Thus, following a tightening of Basel norms, as we have shown in the previous chapter, there will take place a cumulative contraction in the output of the unorganized sector widening the output gap. This will induce the RBI to lower the interest rate. This will lead to, as shown above, a further cumulative contraction in  $X$ . This process will continue until a new equilibrium is achieved. This yields the following proposition:

**Proposition 3.2:** A tightening of Basel norms brings about a cumulative contraction in the output of the unorganized sector. This contraction is magnified significantly by the counter recessionary policy of the RBI. The capitalists, through the tightening of Basel norms, grab not only a large part of the market of the unorganized sector but also, in all likelihood, a larger part of the aggregate output of the organized sector for their own use.

The tightening of the Basel norms is just an example to show how the counter recessionary monetary policy deepens the recession in the unorganized sector caused by a change in a policy instrument of the capitalist aimed at reducing the output of the unorganized sector. Thus, a fall in

$\bar{N}$  brought about by the capitalists by bringing about more automation in production or a capitalist induced worsening of attitude of the banks towards the unorganized sector will lead to a shrinkage of the unorganized sector and this process of shrinkage will be facilitated greatly by the counter recessionary monetary policy. We will discuss another example where the banks raise  $r_X$ .

### 3.3 The Effect of an Increase in $r_X$

As we have pointed out earlier, we regard  $r_X$  as an instrument of the capitalists to exploit the small producers.  $r_X$  is independent of  $\bar{r}$ , the interest rate at which the capitalists secure loans for financing investment. In fact, in times of recession,  $r_X$  often goes up despite the fall in  $\bar{r}$ . This happens because in times of recession, banks become more cautious regarding their lending and in their perception the risk of lending to the small producers increases phenomenally. Thus, the risk premium that they charge on loans given to the small producers increases steeply in times of recession. This was in evidence in the USA (see Bernanke (1983), Bernanke, Gertler and Gilchrist (1996) and Mishkin (2009)). The capitalists by exercising State Power in India can make banks raise  $r_X$ . We will derive its impact mathematically now.

A ceteris paribus increase in  $r_X$  should increase the default rate of the small producers inducing the banks to reduce loan supply to the small producers. This, just as in the earlier cases, will lead to a cumulative contraction in the output of the unorganized sector, which will be aggravated considerably by the counter-recessionary monetary policy and the increase in the risk premium with the deepening of the recession. This yields the following proposition:

**Proposition 3.3:** An increase in  $r_X$  brings about a cumulative contraction in the output of the organized sector. This contraction is magnified significantly by the counter recessionary monetary policy of the RBI. The capitalists, by raising  $r_X$ , grab not only a large part of the market of the unorganized sector but also, in all likelihood, a larger part of the aggregate output of the organized sector for their own use.

### 3.4 Conclusion

This paper shows that the counter recessionary monetary policy is a part of the exploitative machinery of the capitalists. It brings about a large and cumulative contraction in the output of the unorganized sector and enables the capitalists to grab a large part of the market of the unorganized sector. The capitalists, in all likelihood, are also able to use a larger part of the output of the organized sector for their own use. The capitalists have many instruments at their disposal to bring about a shrinkage in the unorganized sector. The counter recessionary monetary policy deepens manifold the recession created by these instruments in the unorganized sector.

The scenario is obviously extremely scary in view of the fact that about 99 percent of the workforce derives their livelihood from the unorganized sector. The shrinkage of the unorganized sector raises unemployment and poverty significantly. If the capitalists swallow up the whole of the unorganized sector, the ordinary Indians will perish.

The interest rate is falling steadily since 2015 in India (see Table 3.6 in Chapter 3). The prices on the other hand are rising at an alarming rate (see Table 3.5 in Chapter 3). As a result, the real value of the savings of the workers and that of the interest income yielded by the savings are falling at a high rate benefiting the capitalists, who are net borrowers, and making the lives of the workers precarious. The central banks all across the capitalist world and its satellites such as India are

carrying on with this extremely unjust monetary policy in the name of fighting recession, which the capitalists create to reduce the unorganized sector.

Clearly, unless the ordinary people become aware of the real cause of their plight, unless they become united, form their own party and grab the State Power, they are likely to become extinct. However, the spontaneous farmers' movement against the reforms in agriculture keeps the hopes for the ordinary people alive.

#### **4. Chapter 4: Monetary Policy, Financial Sector Reform, Fiscal Policy and Land Grab in India**

At the present, the monetary policy all across the capitalist world including India consists in pushing down the interest rates to the lowest possible level. Prices on the other hand increase continuously all across the capitalist world including India. As a result, both the principal amount of a loan and the interest income from it fall in real value continuously. This makes loans or financial assets such as bank deposits or bonds unattractive as instruments of saving. Again, the financial sector reforms undertaken in recent years such as the withdrawal of government guarantee of bank deposits and **the bank frauds that are rising at an alarming rate in India** at the present have contributed to the vulnerability of the financial assets. Under these conditions, the savers get induced to divert their savings from the financial assets to real estate. This makes it profitable for the capitalists to appoint land sharks to force the small producers to part with their land. The capitalists sell this land to the savers and, thereby, make a huge profit. The capitalists are able to do so because, as we have explained in Chapters 2 and 3, they own all the political parties and wield the State Power. Obviously, the land lost by the small producers gets locked in unproductive uses, while the output of food and other mass consumption goods falls impoverishing the poor substantially.

The government's fiscal policy these days consists in switching from direct taxes to indirect ones so much so that the fraction of the total tax revenue contributed by the indirect taxes has been rising steadily of late and at the present the major part of the total tax revenue comes from the indirect taxes (see Table 4.1 of Chapter 4). We have shown here that a fall in the direct tax rates will also raise demand for land making it profitable for the capitalists to take away more land from the small producers impoverishing the poor. A hike in indirect tax rate will also, as we show here, will bring about a cumulative fall in the small producers' output substantially increasing the poverty of the masses.

The NEP has drastically cut down the direct tax rates. Even though the government has hiked indirect tax rates to make up for the shortfall in revenue, there are limits to such hikes as they produce strong inflationary forces. The NEP has also put stringent restrictions on government's fiscal deficit. As a result, the government has become subject to acute fund shortage and there has taken place drastic fall in public investment in infrastructure that caters to the needs of the small

producers and the poor (see in this context Mishra (2006) and Godara et. al.(2014)). **The fund shortage also induces the government not to rescue the troubles financial institutions making them more fragile in popular parlance.** We have shown here how this decline in government expenditure will lead to unproductive real estate development at the cost of the land and output of the small producers substantially impoverishing the poor.

## 5. Conclusion

After gaining independence, India adopted the Soviet model of planned economic development. It modified the strategy a bit and drew up the Nehru-Mahalanobis Strategy of economic development. The objective of this strategy was to establish socialism. With this end in view, the government nationalized all natural resources and financial institutions. All the essential industrial sectors were made exclusive preserves of the government. The government played the major role in developing industry, agriculture and the financial sector of India. The capitalists were not allowed to invest in most sectors. To generate employment, quite a large number of sectors of production and distribution were reserved only for the small producers. All the prices and interest rates were under the control of the government. Through a system of licensing, the government used to regulate production, investment, import and export of the private sector. On the basis of the support received from the Soviet Union, India could adopt and carry on with this strategy of socialist development. However, with the weakening of the Soviet Union since the mid-eighties, the western capitalists finally succeeded in forcing India to give up the Nehru-Mahalanobis Programme and adopt the NEP in its place in 1991(see Ghosh and Ghosh (2016), (2019<sup>a</sup>, 2019<sup>b</sup>). The objective of the NEP is to remove all kinds of government restrictions and regulations on economic activities of the capitalists, to sell of all government enterprises and natural resources to the capitalists and to do away with all restrictions on cross-border trade of goods, services and capital. In other words, the objective of the NEP is to hand over India to the capitalists so that they can run and manage India the way they want to. The NEP is being implemented through a series of economic reforms. This thesis shows how the process of economic reforms is benefiting the capitalists causing immense misery and suffering to the masses.

## References

- Bernanke, B.(1983), Non-Monetary Effects of the Financial Crisis in the Propagation of the Great Depression, *The American Economic Review*, Vol. 73, No. 3 (June), pp. 257 – 276.
- Bernanke, B, Gertler, M. and, Gilchrist, S.(1996).The Financial Accelerator and the Flight to Quality, *The Review of Economics and Statistics*, Vol. 78, No. 1 (Feb), pp. 1-15.
- Ghosh, C. and Ghosh, A. (2016). *Indian Economy*, PHI Learning Private Limited, Delhi.
- Ghosh, C. and Ghosh, A.N. (2019<sup>a</sup>). *Keynesian Macroeconomics Beyond the IS-LM Model*, Springer.
- (2019<sup>b</sup>). *An Introduction to Economics: Economic Theory and Society*, Palgrave Macmillan.
- Godara, R.L. (2014).“Agriculture Credit in India: An Analytical Study”, *International Journal of Latest Trends in Engineering and Technology*, 3(4).
- Keynes, J.M. (1936). *The General Theory of Employment, Interest and Money*, Palgrave

Macmillan.

Mishra, S. (2006). "Farmer's Suicides in Maharashtra". *Economic and Political weekly*, Vol. 41(16), pp 1538-1545.

**Mishkin, F.S.(2009).**Is Monetary Policy Effective during Financial Crises? *American Economic Review*, Vol.99, No.2 (May), pp. 573-77.