

# Indian economy back on the track under the Gandhi government

by Susan Brady and Ramtanu Maitra

In a gloomy world economic situation, the performance of the Indian economy has been a relative bright spot. After two years in power, the government of Prime Minister Indira Gandhi has succeeded in putting the economy "back on the rails," showing substantial gains in production and lowering the rate of inflation following the three-year debacle of rule by the coalition Janata government. During those years output stagnated and inflation soared as the government pursued a ruralist, anti-industrial policy.

## The next step

India is now situated to make new strides toward the goal originally set forth after independence by Jawaharlal Nehru: consolidation of a strong industrial base utilizing advanced science and technology, alongside a self-sufficient, productive agricultural sector. The Gandhi government appears committed to such a path, but it faces enormous obstacles and risks, not the least being the reality of world depression. While India's performance is to be applauded, it will quickly face nightmarish conditions if world economic collapse shrinks Indian export markets and dries up the sources of essential credit and capital investment from outside India needed to meet the targets of the Sixth (1981-85) Five-Year Plan and future plans.

Within the world economic context, there are two dangers in Indian economic thinking and planning which must be confronted. The first is the potential for pressures on foreign-exchange holdings to become a point of almost total fixation, such that a foolish approach to export development and promotion is established to the detriment of other needs. In a worst-case scenario, the Sixth Plan itself would be subordinated to forex-earning concerns.

The second danger is a lack of clear focus in economic planning, an absence of a clearly determined set of priorities for major projects and investments. This is already a problem in regard to the power sector, in particular nuclear-energy development, where the priority of electrical energy generation and of even small but catalytic funding for advanced scientific research and development has been insufficiently understood.

## A progress report for 1981-82

The distinct economic improvement that began with Mrs. Gandhi's resumption of power in January 1980 has continued during 1981-82 (fiscal year April-March). As shown on page 30, the major production indicators in industry and agriculture are up, import costs have been moderated, and inflation has dropped from almost 17 percent to 3 percent (with latest figures showing a zero rate of growth of inflation). The one clear trouble spot is the plummeting of the Indian foreign-exchange balance, a situation which prompted the government to negotiate a three-year, \$5.7 billion balance-of-payments credit from the International Monetary Fund (IMF), a move which prompted a great deal of controversy inside India reflecting fears that the IMF would dictate changes in Indian government economic policy.

## Agriculture

The agricultural situation has been a major source of strength during the past year. After a bad year in 1979-80, the past two years have produced good crops and the 1981-82 foodgrain production is expected to reach 134 million tons (mt), an all-time high surpassing the 1978-79 level of 132 mt. Projections for the current year are also good although weather conditions, including unseasonably cold and rainy conditions this spring in the northern wheat-producing region, could lower estimates somewhat.

In general India has achieved something few other developing nations have, and with 700 million population: basic foodgrain self-sufficiency. The prospects for the major cash crops are also good—sugarcane, groundnuts, cotton, jute, mesta, and tea—and steady progress has been made in allied rural activities such as animal husbandry, poultry development, and fisheries.

In the area of animal husbandry generally, the emphasis has been on improving the quality of cattle and other animal stocks, improving the processing capacity, and establishing the institutional framework for making animal and poultry products available throughout the country. India's "Operation Flood," which has increased milk production by 50 percent between 1970 and 1980, from 20 mt to 30 mt, is

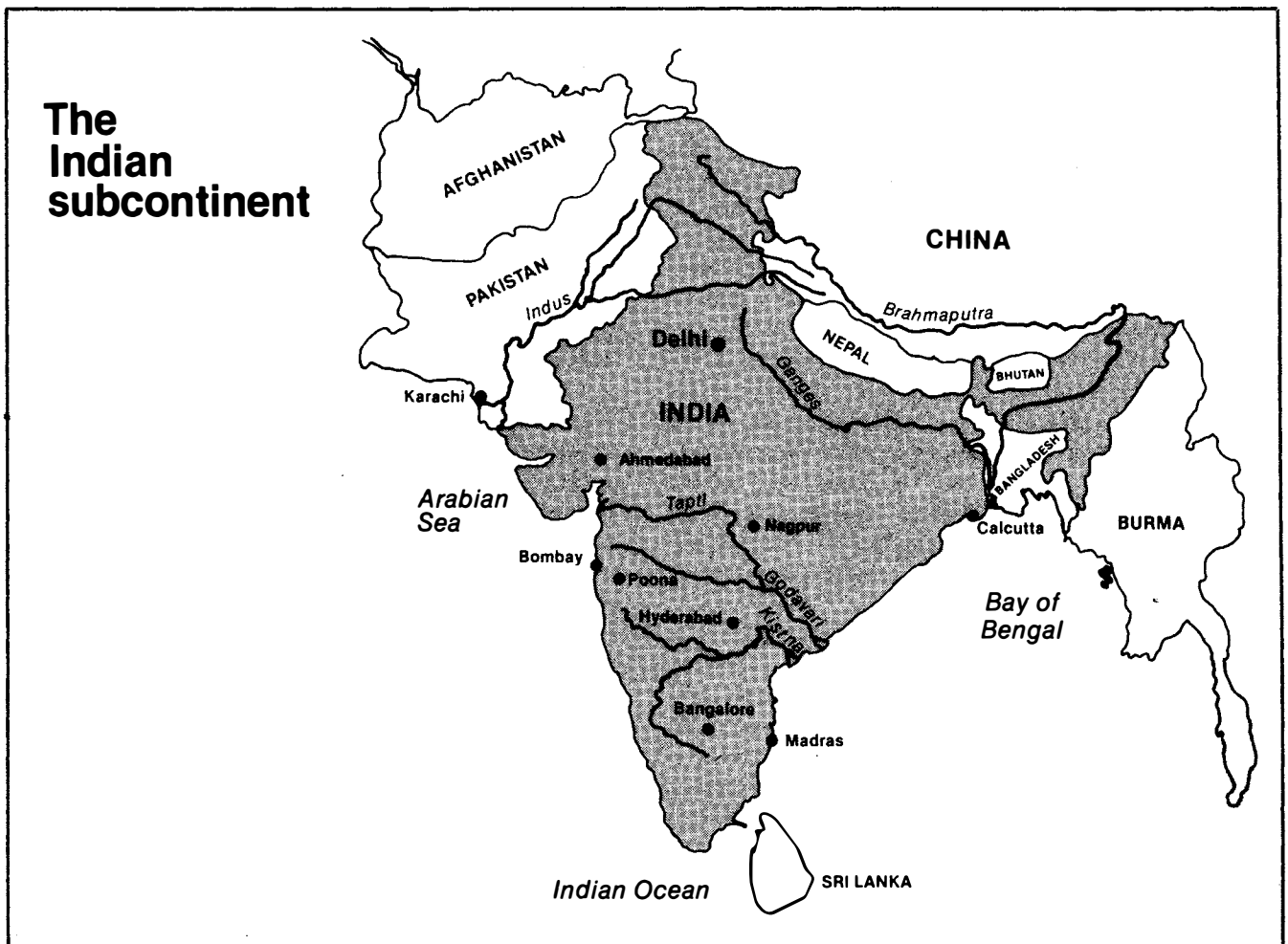
exemplary of this type of effort. This will be a model for a similar effort to gear up oilseed production and the edible oil industry (edible oil is one of the top three or four items imported by India).

In the crucial grains-production sector, the emphasis has continued to focus on a high-technology "package" approach involving the efficient use of existing irrigation systems and further irrigation development, coupled with increased fertilizer use and the continued spread of high-yielding varieties of seeds. The policy is aided by the provision of electricity to farmers on a priority basis, necessary for running electric pumpsets and thus mitigating the effects of shortages of rainfall, particularly in high production areas like the Punjab and Haryana in the northwest. There are also new initiatives to assure credit availability to farmers and to provide adequate price supports through the government's grain purchasing program.

Within this "package," irrigation development has been given priority. In 1980-81, 2.46 million hectares of land were provided irrigation, 1.6 million through "minor" and .86 million through "major" irrigation proj-

ects. At the end of 1981 the total irrigated land area in India was 55.02 million hectares. The target of 2.63 million hectares in new irrigated land for 1981-82 is expected to be "substantially" achieved despite local shortages of cement and steel, and cost escalation.

On the fertilizer front, usage in 1981 was up 5 percent from the previous year, to 5.52 mt of which 2.8 mt are imported. The government plans include a major effort to increase domestic fertilizer production, motivated in part by increased domestic needs and by the desire to reduce the import bill for fertilizers. Those efforts are centered in the establishment of two huge new projects in the public sector—the Thal Vaishet and Hazira projects in Maharashtra and Gujarat respectively will include four large gas-based ammonia plants that are harbingers of a new network of gas-based fertilizer plants presently being sited by a specially appointed export committee. The idea is to combine coal with use of gas from the Indian offshore oil fields in Bombay High and Bassein as feedstocks, and to pipe the gas directly to plants in farm areas, so that transport of increased fertilizer supplies does not aggravate the



## Selected indicators of the Indian economy

(Percentage change over previous year)

	1974-75	1975-76	1976-77	1977-78	1978-79	1979-80	1980-81	1981-82 (1982 estimated)
Gross National Product at 1970-71 prices .....	1.2	9.6	1.3	8.6	5.3	-4.8	7.5	4.5
Agricultural production .....	-3.2	15.2	-7.0	14.5	3.4	-15.5	15.4	3.0
Foodgrain production .....	-4.6	21.2	-8.1	13.7	4.3	-17.1	18.4	9.0
Industrial production .....	3.2	7.2	9.6	3.3	7.6	-1.4	4.0	9.8
Electricity generated .....	5.2	12.9	11.5	3.4	12.2	2.1	5.0	11.6
(Utilities only)								
Wholesale prices .....	10.1	-6.5	12.0	0.3	4.6	21.4	16.7	3.0
(on point to point basis)								
Monetary resources .....	10.9	15.0	23.6	18.4	21.9	17.7	17.6	11.3
Imports .....	52.9	16.5	-3.6	18.7	13.2	32.4	38.2	4.0
(in current prices)								
Exports .....	31.9	21.4	27.2	5.2	5.9	12.8	3.9	14.1
(in current prices)								
Foreign exchange assets .....	5.1	144.3	91.9	57.2	16.0	-1.1	-6.6	-27.2
(excluding gold and SDRs)								

Source: Indian Ministry of Finance

already serious rail-transport bottlenecks.

### Industry

Overall Indian industrial output will increase by about 8 percent during 1981-82, a significant rate of growth (see above). All three major industrial sectors contributed to the growth—manufacturing increased 8.6 percent; mining 17.7 percent; and electricity generation 11.8 percent.

This growth, however, is largely a product of increased utilization of existing capacity, the figures reflecting recovery from a depressed condition rather than any significant net additions to productive capacity. This improvement is attributed to the recovery of the functioning of vital infrastructure—mainly power and transport—a focus of major concern by the Gandhi government, with the Prime Minister herself monitoring the performance in these areas.

Virtually every industry group in the manufacturing sector registered growth, with the exception of food manufacturing, textiles, and electrical machinery, apparatus, and appliances. Mining growth is accounted for by the 62 percent growth in crude petroleum output—a stunning tribute to the preliminary successes of India's ambitious oil development program, with some help from the restarting of oil flows from the Assam fields in northeast India which had been blocked by political destabilization in that region. There was also a 12 percent jump in coal production, a result of great

efficiency in the coal fields and increased power availability to the mines.

One of the principal areas of concern is the steel industry. Despite a longstanding Indian commitment (since Nehru's days) to self-sufficiency in steel production, steel remains one of the four major import items. Total availability of steel in 1981 was about 10 mt—including 6.9 mt produced by the six integrated steel mills in the country, 1.6 mt produced by the mini-steel industry, and 1.5 imported. Steel output was affected both by power cuts and by lack of high-quality coking coal. The power problem is particularly acute in the eastern region where all six major mills are located.

The obvious problems in steel are being taken on in part by a decision to construct two new integrated steel plants, the first new steel plants started since the 1960s. These are the 3.4 mt capacity Vizag project, to be built with Soviet assistance (the third Soviet-assisted plant), and a plant in Paradeep, the \$2.8 billion contract for which was originally awarded to the British steelmaker Davy McKee but was terminated just recently when the British attempted to renegotiate the terms of the contract. The plant will now be built by the Indians themselves with the most advanced technology imported wherever it is available.

The decision to build the two new plants, combined with projects to increase the capacity of existing steel facilities, are looked to as hopeful signs that the long stagnation in steel production has ended. The govern-

ment is working with conservative estimates that steel demand will reach 18.4 mt by 1990, and plans to increase installed capacity in the integrated plants to about 20 mt. This will be difficult to achieve, however, unless parallel efforts are made to improve the infrastructure needed to support it.

## Energy

The weak point of the Indian economy remains in its energy and transportation infrastructure. The growth of power generation capacity and the performance of that sector have continued to lag behind the rest of the industrial—and agricultural—economy, and act as a drag on overall growth. There are vast areas of the country plagued by lack of power; and power cuts continue to afflict urban areas and industry with regularity. Efforts to improve rail transport of coal to power plants and to construct coal-fired thermal plants at the coal pithead to reduce transport problems have helped, but the basic problem remains.

The most recent figures show the gap in the power sector in 1981-82. Despite an increase of 11.6 percent in electricity generation, there will be nearly an 11 percent gap between requirements and availability for the year. In 1980-81, the addition to generating capacity was 1,600 megawatts (Mw), compared to a target of 2,600 Mw, and in 1981-82 no more than 2,300 Mw is to be commissioned against a target of 3,200 Mw. Slippages in the construction time of power projects is chronic, due to many factors including the inability of the main domestic power-generation equipment supplier, Bharat Heavy Electricals and Instrumentation (BHEL) to supply on time and in sequence. (See page 32 for graphs of selected industrial and energy production figures.)

The Indian government is working within the framework of estimates that power demand will increase to 32.7 (gigawatts) Gw by the end of the Sixth Plan, and to 52.6 Mw by the end of the Seventh in 1990. As of March 1980 total installed generating capacity stood at 31 GW, and according to present plans new capacity amounting to 19 Gw is to be commissioned during the period of the Sixth Plan, achieving an installed capacity of 48 GW by 1985. This framework already imposes constraints on industrial development because targets are so low. Recognition of the situation and of the fact that even these low targets may not be achieved is evidenced in the government's decision this year to allow public-sector undertakings in the core sectors to set up their own captive thermal power plants.

The realities of the power picture are also reflected in the government's plans regarding coal production: the bulk of power generation will depend on coal-fired thermal power plants. In 1981-82, coal production jumped 11 percent to about 124 million tons, and the Sixth Plan sets a target of 165 mt by 1985 which would

require 10 percent annual growth rate for the rest of the Plan period. Central allocations for coal are to increase, and there are efforts to improve and modernize technology with assistance from many countries including France, the United Kingdom, the U.S.S.R., and Poland. The increased use of coal poses severe problems, however, for already strained rail transport. As well, most Indian coal has a high ash content, making for great maintenance problems in existing thermal plants.

The obvious solution is to increase India's nuclear-power generation program, already the largest in the developing sector, and backed up by the third-largest storehouse of scientists and engineers in the world. At present, plans call for gradual increase of nuclear-powered electrical generation to a level of 10 Gw by 2000, well below earlier estimates and hopes. In large part this is the result of U.S. sabotage by means of a cutoff of supplies of equipment and fuel under the guise of the discriminatory "non-proliferation" policy. India has tried to compensate with development of indigenous technical capabilities; but while the Indians are now theoretically capable of constructing a heavy-water moderated nuclear plant from top to bottom, the construction time is quite long, and capacity is limited. The nuclear program, despite considerable success, has been put on the defensive in favor of more "practical" alternatives like coal. But if there were a new commitment from the government to a thorium-based fuel cycle (India has the largest thorium reserves in the world) utilizing high-temperature gas-cooled reactor technology, progress could accelerate.

## Transportation

Transport, which principally means rails and, less important, water surface and port development, is pivotal to the Indian economy. Though showing improvement, it is acknowledged to be unable to achieve Plan targets with currently available resources. The railways the most extensive system in Asia, have suffered from prolonged underinvestment that has left them with inadequate capital stock (rolling stock, track, and other equipment) and with extensive repair and modernization needs. The track bed and rails are in need of large-scale overall inputs to allow for increased freightage, higher speed of transport with reduced accident rates.

In the area of rolling stock, despite a large wagons-producing industry in India, wagon production has lagged behind targets.

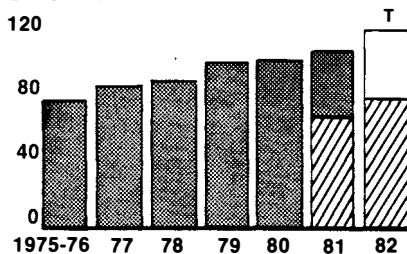
Inadequate traffic-handling capacity at major ports, which has emerged as a major constraint in recent years, is being dealt with through a construction program and the opening of new ports for exclusive handling of containers and bulk carriers. A Japanese firm has just secured a contract for upgrading of the key Cochin port on the west coast.

## Production of selected industries in India

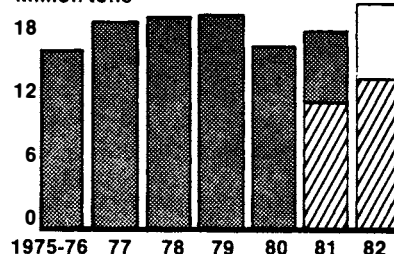
▨ April-November T=Target

Source: Indian Ministry of Finance, economic division

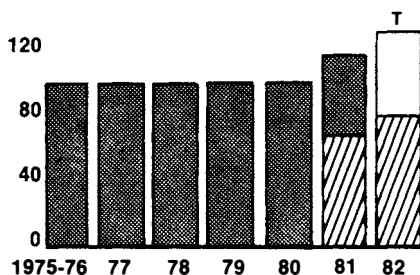
**Electricity**  
Billion KWH



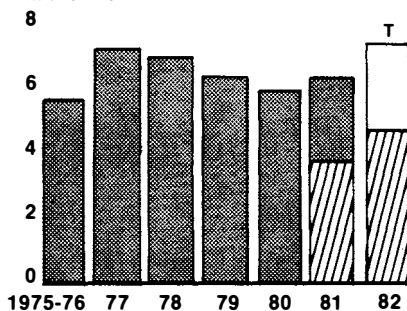
**Cement**  
Million tons



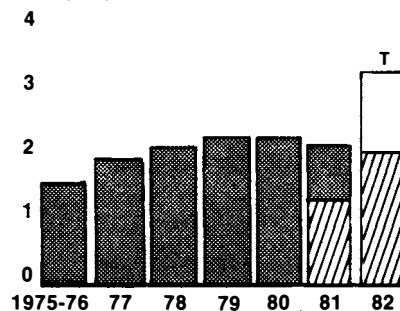
**Coal**  
Million tons



**Saleable steel**  
Million tons



**Nitrogenous fertilizers**  
Million tons



### The balance of payments 'problem'

About 60 percent of India's imports are accounted for by oil, fertilizers, steel, and edible oils. That is the beginning and the end, in essence, of India's "balance-of-payments problem." Increasing trade deficits, likely to exceed 50 billion rupees (about \$5.5 billion) for the second year in a row, have put pressure on Indian foreign exchange reserves.

This pressure has left India open to the intervention and manipulation of international financial circles who gain a foot in the door through India's need for international credit to finance its payments deficit and maintain even the modest pace of capital investment called for in the current Plan. Over the past two years, India has entered the commercial credit market in a significant fashion for the first time—prompted in part by decisions to finance large industrial projects, and by the cutbacks in available credit from multilateral facilities (and lower interest facilities) like the World Bank's International Development Association (IDA):

The concern over the balance of payments has shaped the investment decisions of the government. The value of imports has doubled in the three years from 1979, principally due to the escalation of oil prices during 1979-80 (a problem augmented by the need to import a larger volume of oil due to the destabilization of Assam). Other essential items like fertilizers, steel, and edible oils are imported in volumes dictated by the

gaps left by domestic production. This has left an inadequate amount of foreign exchange for the import of capital goods and industrial raw materials, the categories which need to be vastly expanded if development is to move forward as rapidly as it can.

The basic strategy at present is to increase the production of the principal import items, reducing the import and foreign-exchange burden they pose, and freeing resources for capital goods imports. This is coupled with a vigorous program to promote Indian exports and increase forex earnings.

The centerpiece of the first part of the strategy is the massive investment in oil exploration and development inside India. Budget allocations for this program in the 1981-82 budget were increased 30 percent from the previous year and the 1982-83 budget raises this allocation another 90 percent to 20 billion rupees.

The major part of the oil-development effort is being carried out by the Indian state oil companies, which have developed an impressive capability including research and development. However, in addition it was decided to supplement their effort by opening up oil concessions to foreign oil companies on a production-sharing contract basis. Some interest has been evoked—Chevron which is involved in a drilling project—interest spurred by several new oil discoveries in offshore areas. In addition, the Soviets have agreed to assist in further onshore development.

Revised estimates for proven oil reserves in India's offshore areas now stand at 2.5 billion tons, an increase of 300 million tons over previous estimates. It is expected that by the last year of the Sixth Plan, indigenous oil production will reach a level of 30 million tons (compared to 14.5 mt in 1981), meeting about 70 percent of total crude demand. The state-owned Oil India Ltd. (OIL) has formulated an ambitious plan which calls for the production of 60 million tons of crude annually by the year 2000. The Indian government is hopeful that their efforts will bear fruit and relieve India's oil-import requirements in the immediate future.

On the income-generating side of the BOP equation, India has launched an export promotion drive. Significantly, the "boom" in Indian exports from 1974-77 was largely due to the price run-up for agricultural products such as oil cakes, marine products, and sugar. Otherwise India's major traditional exports—jute, tea, and textiles—are heavily dependent on world commodity markets and increasingly subject to protectionist barriers in advanced sector markets.

The government is emphasizing the development of exports that are both competitive internationally and for which world demand is rising. There is also a push to increase India's exports of engineering goods and manufactured items which have risen as a portion of total exports in the past decade, and for which there is an expanding market in other developing countries, in Eastern Europe, and in the Soviet Union.

Incentives have been provided to promote exports, including the establishment of two "free-trade zones," where a complete tax holiday for the initial five years is granted to industrial units set up for 100 percent export, including foreign companies. Those producing in these areas, or even outside them, for export are eligible for special credit facilities; for waiving of import duties on capital goods, raw materials, and so forth imported for export processing; and for exemption from central excise duties and other levies. Very recently the sale of 25 percent of output from the free-trade zones to domestic markets was approved, subject to duties. Other tax credits and exemptions are also available, some recently introduced in the 1982-83 budget by Finance Minister Mukherjee.

It is the balance-of-payments problem, viewed in the light of the requirements of the Sixth Plan, that prompted the Indian government to arrange the huge IMF credit last year. The Plan assumes the availability of foreign aid and loans of more than 93 billion rupees (about \$10 billion), probably an underestimate. Under the circumstances, a large loan was a necessity for maintaining the pace of development; and as Indian authorities have explained, the average interest rate on the entire IMF package works out to below 10.5 percent, considerably below the 18 percent-plus prevail-

ing currently in commercial markets.

The IMF is clearly calculating that within a year the Indian economy will be in deteriorated condition, along with the rest of the world economy, and that the loan is a "foot in the door" to dictating stringent conditionalities for the Indian economy, including abandonment of large-scale industrial and agricultural development plans. At present the loan is subject to "adjustment criteria" and "performance criteria," including checking inflation, curtailing non-bank credit to the public sector, reduction in public expenditure, and improvement in the functioning of public sector enterprises. In many instances the Indian government is already pursuing some variation of these goals, and there is no evidence that the Indian government has taken steps contrary to its own objectives, particularly regarding austerity measures, due to IMF pressures. Mrs. Gandhi has made it clear that the IMF will in no way be allowed to contravene parliamentarily approved decisions on the economy and that future installments of the credit will be abandoned rather than bow to such dictates.

Yet the discovery and development of oil in India remains the collateral for the IMF loan and hence an Achilles heel of sorts. Failure in this effort will put extreme pressure on the export-promotion side of things, distorting the economy, and will also mean pressure to adopt austerity measures including curbing development spending and imports of capital goods. The Indian economy has built up a tempo of growth which under favorable world conditions could rise even more rapidly, but under depression conditions India will be no less immune to the consequences of global collapse.

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