

12th Edition
2020-21

INDIAN ECONOMY

▷ FOR CIVIL SERVICES, UNIVERSITIES AND OTHER EXAMINATIONS

ABOUT THE AUTHOR



Ramesh Singh is an alumnus of *Delhi School of Economics* and an education consultant with over two decades of experience in guiding the aspirants of civil services and other examinations. He is a prolific writer and has authored several books both in English and Hindi for McGraw Hill, including *Indian Economy*, *Bhartiya Arthavyavastha*, *Contemporary Essays*, *Objective Indian Economy and Social Development*, *1000 Plus Questions on General Science*.

He is also a popular columnist of the Publication Division journals *Yojana* and *Kurukshetra*.

A teacher par excellence, he is endowed with exceptional quality of simplifying the difficult concepts of economics in a cogent and crystal-clear way. His *expert lectures* on economics and essay are quite popular across the country. He lives in Delhi busy in diverse academic and social pursuits.

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Ramesh Singh



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In loving memories of my parents

P.N. Singh

&

R.N. Devi Singh

PREFACE TO THE TWELFTH EDITION

After the rigour of revision work, it really feels quite satisfying to present the *12th edition* of the book.

Emerging as a *best seller* was no doubt a recognisable achievement for the book; however, retaining this position has been a tough challenge and quite taxing for me.

India has been facing with subdued investment for the past several years, which got even more challenged by a general fall in demand seen in 2019-20. We found the Government intervening to support the slowing economy streamlining the latest budget 2020-21 to the challenge. Rather, the upcoming year was waiting for an unprecedented catastrophe - the *Coronavirus Crisis*; we do not find any mention of it neither in the Economic Survey 2019-20 nor in the Union Budget 2020 in 21 (may be, it was too early for the documents to figure out its repercussions as the first confirmed case of it was reported in Kerala on January 30, 2020 only). By mid-April 2020, there was no official figure released by the Government regarding present or future economic impact of the novel virus. But if we look at the financial preparations of the Government, nobody should have any doubt about the damaging scale and nature of the impact - unprecedented and unlike any time in past. On April 3, 2020, the World Bank released the *ever-highest* health package (a fund of US\$ 1 billion) for India to fight out the extraordinary crisis. In recent years, India has been busy in finetuning its stance on trade, globalisation, ease of doing business, climate change, human development very wisely, which look all shattered and derailed given the heavy drain of financial and administrative resources caused by the corona crisis.

This is an *enlarged*, *revised* and a *revamped* edition. In the process of revision, ample care has been taken to make it an even more 'focussed' and 'helpful' book for the aspirants.

What is new in this edition?

- The new edition has been thoroughly 'revised' by including the inputs from the *Economic Survey 2019-20*, *Union Budget 2020-21*, *India Development Report 2017 (the latest)*, *India 2020* and other relevant official documents.
- Revamped insight into *Economics* - Economics is more than a dismal science; Macro- and MicroEconomics; Understanding an Economy; National Income accounting; GVA and GDP; Fixed-base and Chain-based methods; Standing Committee on Economic Statistics; and the latest National income estimates.
- Revised outlook into *Development Economics* and *Economic Reforms* including areas like Washington Consensus; Beijing Consensus; Santiago Consensus; Capitalism as a tool of Growth; World Happiness Report 2020; Transformative reforms; and Nudge and Public Policy.
- Priorities of *Planning* and related topics have been updated with the new inputs together with

a discussion on the Niti Aayog documents: Three-Year Action Agenda; Seven-Year Strategy Framework (Strategy for India @75) and a Performance Report of Niti; Core & Core of the Core Schemes; and Development Monitoring and Evaluation Office.

- The section on *Inflation* has been fully revised and new inputs included on its dynamics together with coverage on Disinflation, Deflation; Skewflation; Current Trends; Challenges of Inflation Targeting; and Effects of Inflation.
- Other than general revision, *Agriculture* section has been added with new issues like skewed Cropping Pattern; rising Economic Costs of food grains; Buffer Stock; state of Hunger and Malnutrition; rising Food Subsidy; gains out of Irrigation Efficiency; new steps to promote Mechanisation of farm sector; rising Fertilizer subsidy; new steps to improve PMFBY; Economic importance of the Food Processing industries; Pradhan Mantri Krishi Sampada Yojana; Cash Support schemes for farm community (of the centre and states); and shift from Loan Waivers to Cash Support.
- The chapters on *Industry, Infrastructure* and *Services* have been fully revised and added with the new issues such as Comprehensive management of public assets; India in Doing Business report 2020; Assemble in India for world; Innovation and entrepreneurship; PMAY-U; National infrastructure pipeline; Overall performance of services sector; Trade in services; Sectoral situation of services; IT-BPM sector; and Offshore fund management.
- The section of *Financial Market* has been duly revised and updated and several new items have been added such as revamped functions of the RBI and its new Financial Year; RBI's reserves and surplus capital; Monetary transmission; new Liquidity management framework; IBC amendments; Deposit insurance; Insurance penetration and density; and Third-party insurance.
- The *External Sector* and *International Economic Organisations* sections have been revised, updated and added with new topics such as Forex reserves; External debt and its composition; Export promotion schemes; Trade scenario; Current trade opportunity; FTAs and PTAs negotiations; India and WTO; and Trade facilitation by India.
- The sections on *Taxation* and *Budgeting* have been fully revised and updated according to the changed times and several new topics have been added such as Collection performance of GST; Inducing voluntary compliance of GST; GST and understanding of the economy; Corporate tax reform; Dividend distribution tax; Ease of paying taxes; Major direct tax reforms of 2020-21; Vivad se Vishwas scheme; Monetised deficit phased out; Output-Outcome framework; Public debt; central government debt; Central transfer to states; and General government finances.
- The section on *Sustainability & Climate Change* has been duly revised as per the changing

challenges and priorities by incorporating the issues such as COP25; India & the SDGs; SDG Nexus; India and Climate Change; Eight National Missions; Aligning Financial System with Sustainability; International Initiative of India; International Solar Alliance; Coalition for Disaster Resilience Infrastructure; India and the UNCD; India's Forests; Agricultural Residue Burning; and Waste Management.

- One of the most vital areas *Human Development in India* has been revised, updated and added with several new issues such as the latest Human Development Report 2019; Multidimensional Poverty; Education for All; Skill Development; Reforms in Apprenticeship Rules; Employment Scenario; Formalization of jobs; Gender dimension of employment; Participation in labour market; Labour market formalization; Health for All; Preventive health care; Health care affordability; medical infrastructure; Mission mode interventions; Housing for All; and Social Sector expenditures of the governments.
- The existing topics of the *Burning Socio-Economic Issues* chapter have been fully revised, updated and streamlined with the changing policy priorities and times. Several new contemporary areas have been included in the section such as Economic impact of the Covid-19 (UNCTAD and Economist reports); Exploring a new economic model for the world (steady-state and circular economies); Shift from green revolution to green methods; Data as public good; Legal logjam (pendency in Indian courts); and Amalgamation of the public sector banks.
- The section on *Multiple Choice Questions* has been fully revised and made current in perspective. Several questions have been replaced by new ones touching the relevant and burning issues such as Interest rates of loans and CRR; Samagra Shiksha Abhiyan; Accommodative stance of monetary policy; Relationship between the primary and fiscal deficits; Money supply and interest rate of loan; Consumption and investment expenditures; Liquidity of money stock; Depreciation and foreign trade; Convertibility of rupee in the current account; Inverted custom duty; Fiscal glide path; Lag between investment and its impact on the national income; World happiness report 2020; Doctor-population ratio in India; Mission mode interventions in healthcare; Climate risk in India; National health accounts; Human development report 2019; Global multidimensional poverty; New labour force participation survey; and New periodic labour force survey.
- Among the most favourites of the readers, the section on *Model Answers* has been fully revamped and updated keeping in mind the emerging dimensions of the economic issues and challenges - several old questions have been dropped and new ones added which touch the areas such as Crop residue burning; Declining female labour force participation in the economy; Steps to formalise labour market; Central transfer to states and the recent changes;

Output-outcome framework; Dovetailing assemble in India with the Make in India; Decentralised approach to promote entrepreneurship; National infrastructure pipeline; Challenge of the lack of monetary transmission; Nudge and public policy; Need of sustainable cropping pattern; Rising food subsidy; Cash and investment supports to farmers; Santiago consensus and India's third-generation economic reform; and Wealth creation, formalisation and inclusive growth.

- One of the most favourite sections of the readers, the *Glossary*, has been fully revised, updated and added with several new topics - BEER; Circular economy; Comparative advantage; D-SIBs; Modern monetary theory; Operation twist; P/E Ratio; PSEs and PSUs; Round tripping; Round-trip trade; Sovereign bond; and Sterilised intervention being the major ones.
- This edition comprises exclusive coverage of the latest *Economic Survey 2019-20* (volume-wise) and the *Union Budget 2020-21*.
- In this edition we are introducing a new feature, the [Online Learning Center \(OLC\)](#). Under it, the readers will get access to a *fortnightly* column written by the author on 'Burning Topics'. For details readers are advised to see the back cover of the book.

With all sense of care and responsibility, I, hereby, present this book to the readers with the wish that it serves their requirements of the examinations taking place in 2020 and 2021 in a better way. Constructive suggestions from the readers are always welcome.

Wishing all the very best to the readers in their endeavours!

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PREFACE TO THE FIRST EDITION


I felt my first serious inclination towards writing when my first article was published in the journal *Mainstream* way back in 1988 while pursuing my post graduation studies at the Delhi School of Economics. My interaction with students inside and outside the classroom in 1990-91, when India faced a serious financial crisis, made me realise that there was an immediate need of a book on Indian economy, which could educate the students about the various aspects and challenges of the Indian economy in a simple and lucid manner. It took nearly two decades to fulfil this dream of mine.

The book has been designed to cater to the requirements of the General Studies paper for various Civil Services Examinations (Union as well as the States), and the optional Economics. It would also be useful for graduate and postgraduate courses in Economics of various universities. Adequate and required notes and references have been given after consulting and referring to an array of sources. I have taken care of both the objective as well as the subjective aspects based on my classroom experience of interacting with the students.

I am grateful to Prof. Majid Husain for the inspiration and motivation I got from him to complete this work. I have especially learnt the art and importance of work, punctuality and honesty in a very practical way from him.

Thanks are also due to Mr. Rajesh Kumar Baghel, Mr. Rakesh Kumar, Md. Ishtiaq, and Mr Vikash. I am indebted to my wife, Mrs Ila Singh, for her full support and my two little daughters, Medha and Smiti, for providing the sparkle in an otherwise monotonous work.

Finally, my special thanks to the team from McGraw-Hill, who took great pains to finalise the project and complete it in a record time with all the possible expertise. I welcome from the I welcome from the readers constructive advice, and comments, which could guide me in further revision of this book.

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ABOUT THE CIVIL SERVICES EXAMINATION

The Civil Services Examination comprises of two successive stages:

- (i) Civil Services (Preliminary) Examination (Objective Type) for the selection of candidates for Main Examination; and
- (ii) Civil Services (Main) Examination (Written and Interview) for the selection of candidates for the various services and posts.

Scheme and subjects for the Preliminary and Main Examination.

▷ A. PRELIMINARY EXAMINATION

The Examination shall comprise of two compulsory Papers of 200 marks each.

Note:

- (i) Both the question papers will be of the objective type (multiple choice questions).
- (ii) The question papers will be set both in Hindi and English. However, questions relating to English Language Comprehension skills of Class X level will be tested through passages from English language only without providing Hindi translation thereof in the question paper.

▷ B. MAIN EXAMINATION

The written examination will consist of the following papers:

Qualifying Papers:

Paper A: (One of the Indian Language to be selected by the candidate from the Languages included in the Eighth Schedule to the Constitution).

300 Marks

Paper B: English

300 Marks

The papers on Indian Languages and English (Paper A and Paper B) will be of Matriculation or equivalent standard and will be of qualifying nature. The marks obtained in these papers will not be counted for ranking.

Papers to be counted for merit

Paper I: Essay

250 Marks

Paper II: General Studies-I (Indian Heritage and Culture, History and Geography of the World

and Society)

250 Marks

Paper III: General Studies -II (Governance, Constitution, Polity, Social Justice and International relations)

250 Marks

Paper IV: General Studies -III (Technology, Economic Development, Bio-diversity, Environment, Security and Disaster Management)

250 Marks

Paper V: General Studies -IV (Ethics, Integrity and Aptitude)

250 Marks

Paper VI: Optional Subject - Paper 1

250 Marks

Paper VII: Optional Subject - Paper 2

250 Marks

Sub Total (Written test)

1750 Marks

Personality Test

275 Marks

Grand Total

2025 Marks

Candidates may choose any one of the optional subjects from amongst the list of subjects given below:

List of Optional Subjects for Main Examination:

- (i) Agriculture
- (ii) Animal Husbandry and Veterinary Science
- (iii) Anthropology
- (iv) Botany
- (v) Chemistry
- (vi) Civil Engineering
- (vii) Commerce and Accountancy
- (viii) Economics
- (ix) Electrical Engineering
- (x) Geography
- (xi) Geology
- (xii) History
- (xiii) Law
- (xiv) Management
- (xv) Mathematics

- (xvi) Mechanical Engineering
- (xvii) Medical Science
- (xviii) Philosophy
- (xix) Physics
- (xx) Political Science and International Relations
- (xxi) Psychology
- (xxii) Public Administration
- (xxiii) Sociology
- (xxiv) Statistics
- (xxv) Zoology
- (xxvi) Literature of any one of the following

Assamese, Bengali , Bodo, Dogri, Gujarati, Hindi, Kannada, Kashmiri, Konkani, Maithili, Malayalam, Manipuri, Marathi, Nepali, Oriya, Punjabi, Sanskrit, Santhali, Sindhi, Tamil, Telugu, Urdu and English.

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GLOSSARY

CHAPTER 1

INTRODUCTION

*Economics is the study of how goods and services are produced, distributed and consumed. As resources are always in short supply, the British economist Lionel Robbins in 1935 described the discipline as ‘the science of scarcity’.**

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▷ MORE THAN A DISMAL SCIENCE

Economics has been called a dismal science, precisely a depressing and poor science¹. Other than this the discipline has also been criticised for being a kind of riddle for common people to comprehend. Last but not the least, it has been called a ‘failed science’ also (more so after its failure to predict the US *sub-prime crisis* of 2008). Still, nobody can deny the invaluable role played by economics to make this world a better place for humanity.

Understanding Economics Understanding economics and its nuances have always been a challenge, especially, for those who come from no background in it. It doesn’t mean that those with a background (university-educated) in it are very comfortable—great many of such people face an altogether different sort of problem—they *understand* less economics than they *know*! Missing the applicatory dimension of economics is a general problem among such people. Today, emphasis being on the *applications of economics* (especially in the competitive exams) ‘knowing’ economics is not enough rather one is required to have the ability to apply economics in everyday life—and this is only possible if one ‘understand’ economics!

Making economics easier for both categories of the readers have been one of the prime aims

of this book. Rather this has not been an easy task for two reasons—firstly, keeping the soul of concepts intact while simplifying them and secondly, educating the reader about the contemporary economic issues. Developing a book on Indian Economy would have been an easier task had simplifying economics not been among the aims. This is why along with the analyses of economic issues there flows an undercurrent of economic theory throughout the book. For this, it will be *wiser* on the part of the reader to keep in touch with the *footnotes* and *glossary* to feel and comprehend the subject matter in a desired way.

▷ DEFINING ECONOMICS

Simply put, ‘economics studies economic activities of the human being’ (a *working definition*). Humanities are intricately connected as all aim to study the differentiated human activities—that is why inter-disciplinary approach to study humanities is considered wiser.

What are Economic Activities? In a very simple way, all activities where money is involved can be called economic activities. And wherever money comes in question, there comes the economic motive/gain—several examples can be taken of it—getting job, giving a job, buying and selling something, doing a business, so on and so forth. Things are still a bit complicated! Visiting religious places for prayer is clearly not an economic activity but what about giving alms to beggars there or putting some money on the places of worship or for that matter religious donations. Can we call them our economic activities? It looks difficult to say! Here, other than the activity of prayer all are economic activities!

However, defining economics has not been as easy as it has been presented here—defining every discipline has been a complex and contentious task for that matter. Widely used and quoted definitions of the discipline revolve around the uses of resources and their distribution. Let us feel the technicality involved in a typical definition with the help of two such acclaimed definitions taken as reference—

*Economics is the study of how societies use scarce resources to produce valuable commodities and distribute them among different people.*²

*Economics studies how individuals, firms, governments and other organisations within our society make choices and how these choices determine a society’s use of its resources.*³

Economics is the study of ‘how society uses its scarce resources’ is probably the most used definition which is catchy as well as concise also⁴.

▷ MICRO AND MACRO

After the Great Depression (during the 1930s) the domain of economics got divided into two broad branches—the micro- and macro-economics. John Maynard Keynes is considered the *father* of macroeconomics (the branch came into being after the publication of his seminal work, *The General Theory of Employment, Interest and Money*, in 1936).

Simply put, if macroeconomics (macro) is about the forest, microeconomics (micro) is about the trees. While the former deals with the big picture (the forest) the latter deals with the details

(the trees) that make up the forest. Micro and macro are the *Greek* words which mean ‘small’ and ‘big’, respectively.

While micro takes a bottoms-up approach to analyse economy, macro takes a top-down approach. Taking an example, while micro tries to understand the choices which consumers make and the income they earn, macro tries to understand the dynamics of inflation and growth. Though, they appear to be different, they are actually interdependent and complementary since there are many overlapping issues between them. For example, a rise in inflation (macro effect) will cause rise in the cost of raw materials leading to rise in prices which consumers will pay (micro effect).

Micro theory evolved from the theories of how prices are determined, macro, on the other hand, is rooted in empirical observations that existing theory could not explain. While there are no competing schools of thought in micro, macro has schools like New Keynesian or New Classical. Since the late 1980s rather these divisions have been narrowing⁵.

Econometrics is the third core area of economics other than the micro and macro. This field seeks to apply statistical and mathematical methods to economic analysis. The sophisticated analyses of micro and macro sub-fields would not have been possible without the major advances made in econometrics over the past century or so.

▷ WHAT IS AN ECONOMY?

Economy is economics in action. It is a still-frame picture of the economic activities. A country, a company and a family all have their economies. It is popularly used in case of countries—Indian economy, the US economy, the Japanese economy, etc. While the principles and theories of economics remain the same, economies (of countries) show diversities given the socio-economic diversities countries have.

Sectors & Types of Economies

Economic activities in a country/economy are broadly divided into three main sectors⁶ and by their dominance economies get their names also:

Primary Sector: The economic activities which take place while exploiting the natural resources fall under it, such as mining, agricultural activities, oil exploration, etc. When agriculture sector (one of the sub-sectors of the primary sector) contribute minimum half of the national income and livelihood in a country it is called an *agrarian economy*.

Secondary Sector: It contains all of the economic activities under which the raw materials extracted out of the primary sector are processed (also called industrial sector). One of its sub-sectors, manufacturing, has proved to be the largest employer across the western developed Economies. When secondary sector brings in minimum half of the national income and employment in a country it is called an *industrial economy*.

Tertiary Sector: All of the economic activities where services are produced falls in this sector, such as education, healthcare, banking, communication, etc. When this sector contributes minimum

half of the national income and livelihood in a country it is called a *service economy*. Later on, experts created two more sectors of economy—quaternary and quinary. Though, they are sub-sectors of the tertiary sector.

Quaternary Sector: Known also as ‘knowledge’ sector, the activities related to education, research and development, etc. come under it. The sector plays the most important role in defining the quality of the human resources an economy has.

Quinary Sector: All activities where top decisions are made fall under it. The highest level of decision makers in governments (inclusive of their bureaucracy) and the private corporate sector fall under it. The number of people involved in this sector is very low rather they are considered the ‘brain’ behind socio-economic performance of an economy.

Stages of Growth Looking at the way developed countries did grow, a theory about it was proposed by W.W. Rostow⁷ in 1960 as per which economies grow following *five linear stages* through the three main sectors i.e., agriculture, industry and services. However, several countries did show exceptions to this standard pattern—India and many other South East Asian countries such as Indonesia, Philippines, Thailand and Vietnam fall under this category. These countries moved from the stage of agrarian to service economy without much healthier expansion of their industrial sector.

India saw a transition from the dominance of the agriculture to services sector by late 1990s when the contribution of services in her national income crossed 50 per cent mark.

▷ ECONOMIC SYSTEMS

Human life depends on uses (consumption) of certain things (goods and services) some of which, upto a level, are also essential (such as food, water, shelter, cloth, etc.) for survival. How to let people have these things was the *first challenge* for the humanity⁸. This challenge has two dimensions of it—firstly, these things need to be created (produced) and secondly, they should reach (distributed/supplied to) the needy people. For production one needs to set up productive assets for which money needs to be spent (known as investment). But ‘who’ will invest and ‘why’? In the process of taking on this challenge there evolved different types of economic systems (i.e., different ways of *organising an economy*). We can prepare a long list of economic systems, however, three of them are considered the major ones—a brief over view of which follows below.

Market Economy

This is considered the first formal economic system emerging out of the traditional economic system. Its origin is traced back to the work (*An Inquiry into the Nature and Causes of the Wealth of Nations, 1776*) of the Scottish philosopher-economist Adam Smith (1723-90). His main ideas can be summed up, in a simplified way, in the following way—

- It is the self-interest which motivates individuals/firms to do economic activities out of

which society gets goods and services supplied with. It means the products society gets is unintended social benefits of someone's self-interested actions. Adam Smith called this motivating factor the *invisible hand* (often called as the 'animal spirit'). This way the questions like 'who' will invest in productive assets and 'why' seem get answered.

- To attain higher prosperity there should be increasing *division of labour* (specialisation of labour force by breaking down large jobs into small components). Specialisation brings in speed, precision and quality in the labour force.
- For invisible hand to operate properly a suitable environment (i.e., market) determined by the forces of demand and supply (called the market forces) is required. What to produce, how much to produce and at what price to sell (i.e., supply) all such decisions depend on these forces.
- Such an economic system needs to be regulated by *competition* prevailing in the market.
- For efficient operation of the economic activities, government should follow a policy of *laissez faire* (French word which means 'leave it alone' which is generally translated by economists as 'non-interference'). Lesser the government, better the economic performance. Here, non-interference by government means great many different things such as—government playing no or least economic role (producing none of the goods and services), no economic regulation, no taxes imposed, etc.

Adam Smith himself called such an economic system as 'the system of natural liberty'. Rather these ideas were the drivers of two major economic systems— 'capitalism' and 'free market economy'. Though, they are based on the same economic environments (demand and supply), there are subtle differences between them:

- While capitalism is focused on creation of 'wealth' and ownership of productive assets, free market economy is focused on 'exchange' of wealth (through production and supply of goods and services).
- In a capitalist system there might be some government regulation but private owner can have monopoly on the market and thus prevents competition. However, a free market economy is solely based on market forces (demand and supply), and there is little or no government regulation. That is why in free market economy free competition is possible without any intervention from outside forces.

Such an economic system got *first* tried in the USA in 1777 from where capitalism spread across the whole Euro-America (Northern America and Western Europe). These economies enjoyed high prosperity and operated well till got hit with the Great Depression⁹ in 1929. By that time great capital was amassed by few (the multi- and trans- national companies) while majority remaining poor—widening inequality in the process over the time. Taxes were imposed but they were very few in number and at very lower rates with state playing negligible welfare role.

Cons of this System Supported by the democratic rights and freedoms, this system had great environment for individual success, innovation and business activities. Though, it looks smoothly operating for over one and half centuries (with subtle changes) it had its own set of limitations which can be summarised precisely in the following way—

- There was almost no tool to look after those who have lower purchasing power (i.e., the poor).

- Negligible to total absence of welfare actions from the state.
- Widening economic inequality even after launching distributive measures such as progressive taxation (in which richer are taxed with higher rates).

The existing set of policy approaches could not help these economies to recover out of the Depression. It was in wake of this crisis that we see the rise of a new branch of economics—the macroeconomics—proposed by the British economist John Maynard Keynes (1883-1949) in his seminal work *The General Theory of Employment, Interest and Money, 1936*. Together with analysing the causes which might have caused this crisis, Keynes suggested a new set of policy approach also to help economic recovery. In very simple term, Keynes suggested these economies to include certain traits from the other economic system (Non-Market Economy) to correct the crisis faced by them. After including the Keynesian advices these economies recovered out of the Depression and in this process (practically) the *mixed economic system* evolved.

Non-Market Economy

Rooted (immediately) in the ideas of Karl Marx (1818-83), it had two variants—*socialist* and *communist*. While in the socialist model (ex-USSR, 1917-89) state was having ownership control on only natural resources, in the communist model (China, 1949-85) the state used to have ownership control over labour also. It got also known by its other names such as *State Economy*, *Command Economy*, *Centrally Planned Economy*. Basically, this system evolved in ‘reaction’ to the market economy and was based on the following main beliefs—

- Resources of a country should be used for the wellbeing of all.
- Resources are best used once they are under the ownership of society/community (Socialism/Communism). Thus, all economic roles will be played by the state only.
- No property rights given to individuals guided by the belief that it promotes exploitation of the labourers (i.e., proletariat) and helps a small minority (i.e., bourgeoisie) to get richer over time—resulting into increasing economic inequality.
- Absence of market (i.e., inter-play of demand and supply was totally absent).
- No idea of competition (i.e., total state monopoly is economic sphere).
- People to play economic role (employed in the state-owned enterprises) *according to their ability* and in return to get all facilities from the state *as per their needs*.
- The decisions such as what to produce, how much to produce and how to supply them to people were taken by the state itself.

This system first got tried by the Bolsheviks in the ex-USSR (in 1919) from where it spread across the whole eastern Europe (the so-called socialist bloc countries) of the time, finally getting its purest form in the communist China (in 1949)—emergence of the socialist and communist models of the non-market economy.

Cons of this System Even after being fully committed to the ‘wellbeing of masses’ with virtual absence of poverty this system had its own limitations which can be summarised briefly in the following way—

- Though, the aim was to serve all there was no idea of creating capital or wealth—which created a scarcity of investible capital in the coming times.

- State used to prioritise the uses of resources—thus the best or optimum uses of resources (driven by market forces) were denied leading to their misallocation and wastage.
- In the absence of property rights there was no motivation to work hard and tap the animal spirit of the people (as no money was paid to them)—leading to virtual absence of innovation (i.e., research and development)—a process of internal decay.
- Being non-democratic political systems the things like *liberty* and *freedom* were totally absent. Aimed at avoiding exploitation of the labourers at the hand of the capitalist state itself emerged as the sole agent of exploitation—critics called this ‘State Capitalism’.

A process of internal decay was being faced by these economies since early 1970s caused by the in-built shortcomings they had. It was way back in mid-1950s that the Polish philosopher Oskar Lange¹⁰ had advised these economies to embrace ‘market socialism’ which was outrightly rejected by both Soviet Bloc and China. At last by mid-1980s state economies moved to modify their economic systems by including certain traits of the market economy—

- Ex-USSR, by late 1980s, announced the twin policies of *Perestroika* (restructuring) and *Glasnost* (openness) switching over to mixed economy with fundamental traits of market economy. Similar changes were adopted by the existing East European socialist economies and the CIS (Confederation of Independent States).
- China, by mid-1980s, announced its *Open-Door Policy* embracing mixed economy with fundamental traits of the market economy. Rather China had started preparations for this change by mid-1970 itself but they were not explicit in nature.

In a way the two major and contrasting economic systems of the time had completed the full circle and moved closer to borrowing traits from each other—the evolution of the mixed economy (where we find the mixture of traits of both of the economic systems). This event has been also termed as the *end of ideology*—as the ideological divide between these economic systems looked bridged now—eventually ending the long-drawn *Cold War* which originated from this ideological difference¹¹.

Mixed Economy

In practice, mixed economic system was already there (by late 1930s) once the market economies adopted certain policy changes (borrowing from the non-market economy) to recover out of the Depression. But first country to announce adopting this system was France (in 1944-45, with the announcement to adopt national planning). The system got further strengthened once the non-market economies started modifying themselves by mid-1980s. It was with few reports of the World Bank that helped world agree on the best model of the economic system—

- World Bank accepted the need of ‘state intervention’ in the economy (i.e., the market economy) which used to be an ardent advocate of the free market economy. But the time and nature of the intervention cannot be universal¹².
- World Bank further concluded that neither of the economic systems (market and non-market) are free from flaws and even a novice of economics can agree that the best economic system can be the mixture of the both. But the state and market mix in any country has to be decided by its socio-economic needs of the time as there cannot be a fixed model of mixed economy¹³.

The *chief characteristics* of the mixed economy may be summarised in the following way—

- State and private sector both to have economic roles.
- Private sector to play those roles where invisible hand (the motive of profit) can work properly. Production and supply of the ‘private goods’ (which people use by purchasing them from their own income) is the best example in this case. But state is not prohibited from playing this role.
- Those roles which private sector will not be motivated to play (due to absence of any profit element) should be better taken care of by the state. Supply of the ‘public goods’ is the best example in this case. But private sector is free to play this role also.
- The economic roles played by either state or private sector may not remain fixed for all times to come and may get modified as per the needs of the time.
- Regulation (things like rules, competition, taxation, etc.) of the economic system to be taken care of by the state.

It means, mixed economic system is not a kind of *finality* which the market or non-market economic systems used to be rather continuous change looks its main feature—capable to modify as per the socio-economic needs of the hour. This way, the long-drawn debate about the possible *role of state*¹⁴ in economy also got decided.

Distribution Systems

Along with the three economic systems there evolved three distribution systems also. While capitalist economy distributed the goods and services through market (people buying their needs from the market at a price decided on market principles), state economy distributed them without taking the help of market (directly state used to supply them to the people without any payments). In the case of mixed economy, the distribution system was a hybrid of the former two models of distribution—state and market both being used (certain goods and services people used to buy from market while certain others being supplied by the state either free or at subsidised prices).

Though, we see a kind of consensus emerging in favour of the mixed economic system, the future had much in store. Over the time, it came under influence of several ideologies some of which also left enduring impact on the world economies—major ones have been briefed below.

▷ WASHINGTON CONSENSUS

It is a set of reform policy package which was suggested by the International Monetary Fund, World Bank and the US Department of the Treasury (i.e., the US finance ministry) to the developing countries faced with economic crisis. Since all of these institutions were based in Washington, the policy prescription was called Washington Consensus by the US economist John Williamson¹⁵. The 10-point reform policy prescriptions are as given below:

- (i) Fiscal discipline
- (ii) A redirection of public expenditure priorities toward fields offering both high economic returns and the potential to improve income distribution, such as primary health care, primary education, and infrastructure.
- (iii) Tax reform (to lower marginal rates and broaden the tax base)
- (iv) Interest rate liberalisation

- (v) A competitive exchange rate
- (vi) Trade liberalisation
- (vii) Liberalisation of FDI inflows
- (viii) Privatisation
- (ix) Deregulation (in the sense of abolishing barriers to entry and exit)
- (x) Secure property rights

However, in coming times, the term became synonymous to *neo-liberalism* (in Latin America), *market fundamentalism* (as George Soros told in 1998) and even *globalisation* across the world. It has often been used to describe an extreme and dogmatic commitment to the belief that **markets can handle everything**.

But the reality has been different—the *set of policies* was already being recommended by the IMF (International Monetary Fund) and the WB (World Bank) together with the US Treasury, especially during the period of the eighties and early nineties.¹⁶ The prescription was originally intended to address the real problems occurring in Latin America at the time, and their use later to handle a wide array of other situations has been criticised even by original proponents of the policies. The name of the Washington Consensus has often been mentioned as being somewhat unfortunate, especially by its creator. John Williamson¹⁷, says that audiences the world over seem to believe that this signifies a set of neo-liberal policies that have been imposed on hapless countries by the Washington-based international financial institutions and have led them to crisis and misery—there are people who cannot utter the term without foaming at the mouth. He further adds that many people feel that it gives the impression that the points outlined represent a set of rules imposed on developing nations by the United States. Instead, Williamson always felt that the prescription represented a consensus precisely because they were so universal. Many proponents of the plan do not feel that it represents the hard-line *neo-liberal* agenda that anti-free-trade activists say it does. They instead present it as a relatively conservative assessment of what policies can help bring a country to economic stability.

But the policy prescription led to processes which are known as Liberalisation, Privatisation, Globalisation, thus cutting down the role of the State in the economy—more so in the nations which got developmental funding from the WB or went to the IMF in times of the Balance of Payment crises (as in the case of India which commenced its reform process in 1991 under the ‘conditions’ of the IMF). It was as if the Adam Smith’s prescription of ‘free market’ (liberalism) has taken its rebirth (in neo-liberalism).

Experts believe that the US sub-prime crisis of 2008 followed by the great recession across the western developed economies were rooted in the ideas promoted by the Washington Consensus. Post-recession period has seen a clear erosion of faith in market and a rising sentiments in favour of ‘state intervention’ in the economy (i.e., rising faith in the idea of *development state*).

▷ BEIJING CONSENSUS

Economic rise of China since mid-1980s needs no introduction. Whether this rise was led by any conscious development model has been an issue of scholarly debate. Finally, the idea of Beijing Consensus¹⁸ was forwarded by Joshua Cooper Remo in 2004.

Also known as Chinese Model of economic development, this refers to the policies which were followed by Deng Xiaoping since 1976 (the year Mao Zedong died). This model is believed to be forwarded as an *alternative* to the Washington Consensus (i.e., an anti-Washington Consensus view) for the developing countries. Over the time experts interpreted this model in different ways rather it is believed to be based¹⁹ on three main pillars—

1. Constant experimentation and innovation;
2. Peaceful distributive growth with gradual reforms;
3. Self-determination and inclusion of selective foreign ideas.

The model received higher attention in wake of the great recession hitting the western economies (when China remained still dynamic)—experts portraying it as China’s alternative to the liberal-market approach of the Washington Consensus²⁰. Whether the developing countries should embrace the Chinese model has been a contentious issue. Experts believe that the things which worked for China may not work for others looking at the heterogeneity of Chinese performance²¹. Again, in wake of the rise of China, experts almost declared the ‘death of market’ and ‘rise of state-led growth’ rather such hurried conclusions might be misplaced because China’s best economic performance came when market was the dominant force²².

Till 2010 we find rising interest in this model across the developing world but once the Chinese growth took a downturn in recent times, experts have advised double caution in blindly following this model. Some experts believe that the rising protectionism across the world (especially the USA, the UK and other places) has been caused by an inclination towards this model only.

▷ SANTIAGO CONSENSUS

This is yet another alternative to the Washington Consensus. Put forward by the then World Bank group President James D. Wolfensohn²³ (in Santiago) for the developing countries. Core idea of this model is *inclusion* which should not be only economic but social too. This way, this is a socio-economic development model and is bound to have its local characteristics. This way, it looks similar to the Beijing Consensus which also includes the social overtones.

In addition to financial resources the World Bank proposed to harness the incredible power of the information technologies and new spirit of openness and partnership (under the spell of rising globalisation) to make knowledge of global best-practice in development accessible to all. World Bank started building an internal architecture of a ‘knowledge bank’ for the purpose.

This proposal from the World Bank inspired the world governments to focus more on aspect of inclusive socio-economic growth. We see this happening in India also—with the Government launching the *third generation of economic reforms* in 2002 (which was aimed at making the fruits of reforms inclusive in nature).

Capitalism as a Tool of Growth Promotion

Capitalism as an economic system failed in the wake of the Great Depression (1929) and got purposefully modified into the mixed economy. But we find countries coming under the spells of capitalism in coming times too. Two such clear spells can be cited—the *first* under the influence of the Washington Consensus (post-1985) and the *second* after the official acceptance to

Globalisation (via the WTO, post-1995). Experts believe that the ensuing Great Recession (after the US sub-prime crisis of 2007) among the developed countries was largely caused by the extreme capitalistic inclinations (neo-liberal policies) found among them. This way, the world has witnessed the devastating effects of capitalism twice by now.

Over the time, a kind of agreement has emerged across the world that though capitalism is not an ideal (or sustainable) type of an economic system rather such policies can be quite helpful in promoting the cause of growth. This is why today, we find countries across the world having capitalistic policy orientation (i.e., *pro-business* policies) under the overall design of a mixed economy—one set of policies (capitalistic) aiming higher growth while the other aiming at effective welfare. Such a clear policy shift has been seen in India too—it was in wake of the criticism to the *Union Budget 2015–16* (of being *pro-rich* or *pro-corporate*) that the erstwhile Finance Minister categorically clarified that the Budget was trying to be *pro-corporate* as well as *pro-poor*. Basically, over the time, experts treat capitalism less as an economic system and more as tool of promoting growth and income.

▷ NATIONAL INCOME

Measuring progress has been a major riddle for experts. Income as an indicator of progress was tried by many before the idea of the gross domestic product (GDP) was put forward by the US-economist Simon Kuznets²⁴ in 1934. The method tries to calculate (account) a country's income at domestic and national levels—in gross and net forms—having four clear concepts (GDP, NDP, GNP and NNP)—a brief and objective overview is presented below.

GDP

Gross Domestic Product (GDP) is the value of the all *final* goods and services produced within the boundary of a nation during one year period. For India, this calendar year is from 1st April to 31st March.

It is also calculated by adding national private consumption, gross investment, government spending and trade balance (exports-minus-imports). The use of the exports-minus-imports factor removes expenditures on imports not produced in the nation, and adds expenditures of goods and service produced which are exported, but not sold within the country.

It will be better to understand the terms used in the concept, '*gross*', which means same thing in Economics and Commerce as '*total*' means in Mathematics; '*domestic*' means all economic activities done within the boundary of a nation/country and by its own capital; '*product*' is used to define 'goods and services' together; and '*final*' means the stage of a product after which there is no known chance of value addition in it.

The *different uses* of the concept of GDP are as given below:

- (i) Per annum percentage change in it is the 'growth rate' of an economy. For example, if a country has a GDP of ₹107 which is 7 rupees higher than the last year, it has a growth rate of 7 per cent. When we use the term 'a growing' economy, it means that the economy is adding up its income, i.e., in quantitative terms.
- (ii) It is a 'quantitative' concept and its volume/size indicates the 'internal' strength of the economy. But it does not say anything about the 'qualitative' aspects of the goods and services produced.