CBSE Test Paper-01
Chapter 08 Economic Reforms Since 1991

1. How many industries still need license for its operations? **(1)**
   a. 4
   b. 8
   c. 10
   d. 6
2. When government disinvests its shares to the extent of 5 to 10 percent to meet the deficit in the budget, this is termed as **(1)**
   a. None
   b. Partial privatisation
   c. Token privatisation
   d. Denationalisation
3. LPG stands for: **(1)**
   a. Liberalisation, Production and Global Cooperation
   b. License, Privatisation and Globalisation
   c. Liberalisation, Privatisation and Globalisation
   d. License, Permit and Goods
4. CRR is **(1)**
   a. None
   b. The percentage of total deposits which the banks have to keep in the form of cash.
   c. The percentage of total deposits which the banks have to keep with the RBI.
   d. Both
5. Define the globalization. **(1)**
6. Privatisation has done more harm than good. Justify your answer. **(1)**
7. Why should tariff and non-tariff barriers be removed to promote globalisation? **(1)**

8. Why did the Indian Government need to borrow from international organisations? **(1)**
9. Those Public Sector Undertakings which are making profits should be privatised. Do you agree with this view? Why? **(3)**
10. In your opinion, what are the advantages of privatisation to the economy? **(3)**
11. Write a brief note on trade and investment policy reforms. How did it lead to economic growth? **(4)**
12. What were the objectives behind Trade and Investment Policy reforms? **(4)**
13. Explain the changing role of state in Indian economy since introduction of reforms. **(4)**
14. Evaluate the positive and negative impacts of LPG policy. **(6)**
15. Write a brief note on International Bank for Reconstruction and Development (IBRD). **(6)**

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Answers

1. a. 4

   Explanation: The only industries which are now reserved for the public sector are 4. i.e defence equipment, atomic energy generation and railway transport.
2. c. Token privatisation

   Explanation: Token privatisation, also known as deficit privatisation occurs when the government disinvests its share to the extent of 5 to 10 percent to meet the deficit in the budget.
3. c. Liberalisation, Privatisation and Globalisation

   Explanation: The government initiated a variety of policies which fall under three heads viz., liberalisation, privatisation and globalisation. (LPG)
4. c. The percentage of total deposits which the banks have to keep with the RBI.

   Explanation: Cash Reserve Ratio (CRR) is the amount of funds that the banks have to keep with the RBI.
5. Globalization is the free movement of goods, services and people across the world in a seamless and integrated manner.
6. **Case for privatisation:**
   i. It will help in reducing the burden on the exchequer.
   ii. It will help in modernising and diversifying PSUs.
   iii. It will help in making PSUs more competitive.
   iv. It will help in improving the quality of decision making of management.
   v. It will help in reviving sick units, which are eating away the revenue of government.
   vi. It will help in developing capital market and international market.
   vii. It is argued that a private firm has pressure from shareholders to perform efficiently. If the firm is inefficient then the firm could be subject to a takeover. A state-owned firm doesn't have this pressure and so it is easier for them to be inefficient. Therefore privatisation inceases the efficiency of firms.

   Case against privatisation:

   i. It will encourage growth of monopoly power in the hands of big business houses.
   ii. It will increase disparities in income and wealth.
   iii. Private sector has no interest in buying loss making and sick enterprises.
   iv. Privatisation may result in lop-sided development of industries in the country.
   v. Private sector may have no interest in long gestation projects, infrastructure investment and risky projects.
   vi. Private sector may not have sufficient funds for many vital projects.
   vii. Unexpectedly, all of the utilities create negative externalities (via pollution, spoiling the environment, etc.) It can be argued that as public sector companies, the government can regulate output and make sure that it is at the socially optimal level (i.e. allow for externalities). In the private sector, maximisation of profit is the only concern, so a socially damaging level of externalities will occur.
7. Tariff and non-tariff barriers restrict the free flow of trade between the two countries. Therefore, these barriers should be removed to promote globalisation. Otherwise, domestic goods would lose international competitiveness.
8. A severe financial crisis due to unsustainable fiscal deficit, fall in foreign exchange reserves and inability to pay interest to international lenders forced the Indian Government to borrow from international organisations. It is because India's export industry was lagging behind due to which she could obtain BOP surplus.
9. No, I do not agree with this view. Even though disinvestment would increase the revenue of the government, the profit-making Public Sector Units(PSUs) are revenue generator for the government and they should be retained in the public sector because the profits of these undertakings add to the revenues of the government and can be used to develop other PSUs and the infrastructure of the company. The profit making PSUs should not be privatised just for the reason that the government can get funds to cover the deficit in government budget. A profit-making PSU should be privatised only if it can earn better revenues and thus higher profit if run more efficiently by the private sector. Also, in the process of disinvestment, if the assets of the profit-making industries are undervalued, it will lead to a substantial loss to the government. Also, the government should retain the strategic profit making industries to avoid emergence of any monopoly in the private sector.
10. Advantages of privatisation are as under:
   i. It will introduce efficiency and profitability in Public Sector Undertakings (PSUs).

ii. It promotes consumer's sovereignty. High degree of consumer's sovereignty implies wider choice and better quality of goods and services.
iii. It will reduce budgetary deficits which result from expenditure on loss making PSUs.
iv. It promotes diversification of production. Also, unlike PSUs, private enterprises invariably generate high profits.
v. Often privatisation of state owned monopolies occurs alongside deregulation – i.e. policies to allow more firms to enter the industry and increase the competitiveness of the market.

11. Liberalisation of trade and investment was initiated to increase international competitiveness of industrial production and also the flow of foreign investments and technology into the economy. Prior to these reforms, in order to protect domestic industries, India was following a regime of quantitative restrictions on imports and restrictions of foreign investments. Foreign trade and investment is an opportunity for the economy to grow faster and expand. Various reforms in policies are carried out to improve foreign trade and investment and at the same time keep domestic market safe. The liberalization of trade policy in 1991 was one of the major reforms which are still carried on in the economy. Reducing import duties and encouraging foreign investment is part of reforms under this sector.
These reforms are useful in the growth of country in the following ways:
i. It helps in lowering the cost of goods by removing tariff barriers.
ii. These reforms help in bringing economies of scale by increasing specialisation.
iii. These reforms help in maintaining friendly relations with other countries.
iv. These reforms increase competition, which in turn help firms to increase efficiency in production.
v. It helps in earning foreign exchange.

12. Trade and investment policy reforms were initiated to:
i. Remove the restrictions on foreign goods and to increase international competitiveness in Indian markets.
ii. Attract foreign investment and to promote the adoption of modern technology into the economy.
iii. Dismantling of quantitative restrictions on imports and exports.
iv. Reduction of tariff rates

v. Removal of licensing procedures for imports.
vi. To increase the efficiency of domestic market.

13. The changing role of state is reflected in the eighth five year plan which mentioned that the planning in India will be indicative increasingly. In order to give some correctness to the changing role of state the eighth five year plan has identified the principles governing public sector. These are :
    i. The public sector must withdraw from the areas where no public sector is served by its presence.
    ii. State should make investments only in those areas where investment is of main infrastructural nature where private sector is not likely to come forth to an adequate extent within a reasonable time perspective.

    After that we saw a major shift in the Indian economy and the role of state has been changing from a controller, regulator and participator to that of a facilitator, observer and guide. The changes that took place in the role of state since 1991 are as under:
    i. Before economic reforms, government had its share in all sectors of the economy. It was producing bread, butter, biscuits, milk, running hotels and many of these were actually not required to be in public sector. Government withdrew herself from these sectors through delicensing, deregulation and disinvestment.
    ii. As a regulator, during 1947-1990, Government regulated all activities with the laws and acts. But after 1991, except some basic and strategic goods and services, decisions were made to be market driven. For this purpose, regulatory authorities were set up for different sectors.
    iii. Since 1991, Government has focused its attention on development of social sector like education, health, defence, law and order.

    Overall, we can say that the role of state has changed from producer to production facilitator.
14. Following are the dual effects of LPG policy on Indian economy:
    i. **A vibrant economy:**
       Indian economy has definitely become a more vibrant economy. The Overall level of economic activity has definitely picked up after the introduction of the policies of liberalisation, privatisation and globalisation. Results are evident in terms of an impressive increase in the growth rate of GDP.
    ii. **A stimulant to industrial production:**

LPG policies have worked as a great stimulant to industrial production in the Indian economy. Presently, industrial production is hovering around 10 percent which is a big jump from the pre-1991 level.

iii. **A check on fiscal deficit:**
Mounting fiscal deficit has been a serious threat to the process of investment in the Indian economy. it was as high as 8.5 percent prior to 1991. thanks to the LPG policies, there has been a significant increase in government revenue.

iv. **A check on Inflatio**n:
Owing to the greater flow of goods and services in the economy, there has been a check on the rate of inflation. Till 2007-08, it ranged between 4-5 percent which is not a serious threat to interest rate structure.

v. **consumer's sovereignty**:
consumers sovereignty has definitely widened over time. this is evident from the actual fact that a large kind of goods and services from the various international markets are currently among the simple reach of the consumers. producers are widely responding to consumers choice and preference.

Negative impact of LPG policies

i. **neglect of agriculture:**
growth of GDP has primarily been owing to substantial growth of the industrial sector. In the wake of LPG policies, focus shifted from agriculture to industries. Consequently, the growth rate in agriculture suffered a setback.

ii. **Urban concentration of growth process:**
LPG policies have resulted in the concentration of the growth process in urban areas. think of any MNC, you will hardly find its trace in the rural areas of country. All MNCs are focusing only on urban areas, where they find conductive infrastructural facilities.

iii. **Economic colonialism:**
India suffered nearly 200 years of political colonialism during British rule. Now while MNCs are dominating the Indian economy, we might suffer a sort of economic colonialism. Implying a situation where MNCs are exploiting the Indian markets to sell their products.

iv. **Spread of consumerism:**
Spread of consumerism within the country as a consequence of LPG policies has

resulted during a large-scale unfold of consumerism. A variety of global brands in the market lured the masses to become spendthrift, even beyond their means.

v. **cultural erosion:**
Globalisation has also caused cultural erosion of Indian society. Economic prosperity has taken a lead over all other parameters of life. Everybody wants to be economically independent and well off, regardlessly of his responsibility towards his family or society.

15. The IBRD, known as the World Bank, came into force on July 1, 1944, during the Bretton Woods Conference. It is a sister institution to the IMF but has s separate, distinct objective. Its head office is located in Washington D.C., USA. The current emphasis of IBRD is to support the less developed countries as most of the developed countries' economies recovered quickly.
Presently there are 185 members of the Bank. Membership is allowed only to those countries who are also members of the IMF. A member country's voting power is dependent on the capital contribution. Like the IMF, the World Bank is also being dominated by major Western countries.
World Bank focuses on making loans to government in order to rebuild railroads, highways, and other infrastructure i.e., the areas where private sector enterprises do not take interest.
The main objectives of IBRD are as follows:
i. To assist in the reconstruction and development of its member countries by facilitating the investment of capital for productive purposes, thereby promoting long range growth of international trade and improvements in the standard of living.
ii. To promote private foreign investment by guarantees of and participation in loans and other investments made by private investors.
iii. To maintain balance growth of international trade and to attain equilibrium in BoP account.
iv. Motivating governments to act on preventing climate change, controlling communicable diseases, managing international financial crises and promoting free trade.