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BA Economics Honours | Semester 1 | Calicut University

Sectoral Contributions in Indian Economy

Course Code: ECO1MN103 • Module 3

Module III: Performance of the Industrial Sector

Industrialization is universally recognized as the prime engine of modern economic growth. The industrial sector generates high-productivity employment, drives technological innovations, creates backward linkages with agriculture, and produces capital goods necessary for overall economic capital formation.

Unit 12: Industrial Performance During the Five-Year Plan Period

India’s industrial development post-independence was shaped by structural planning epochs:

- **The Mahalanobis Heavy Industrialization Strategy (Second Plan: 1956–1961):** Anchored in the Soviet-inspired Feldman-Mahalanobis growth model, industrial policy prioritized "building machines to build machines." Under the Industrial Policy Resolution (IPR) of 1956, basic and heavy capital goods industries (steel plants at Bhilai, Rourkela, Durgapur; heavy electricals at BHEL; machine tools at HMT) were reserved for the public sector, which was designated to occupy the "commanding heights" of the economy.
- **The Era of License Raj and Deceleration (1965–1980):** Characterized by rigid industrial licensing (Industries Development and Regulation Act - IDRA 1951), draconian import substitution tariffs, complex price controls, and MRTP (Monopolies and Restrictive Trade Practices) restrictions. Industrial growth decelerated significantly due to bureaucratic delays, technological obsolescence, and absence of competitive market discipline.
- **Post-1991 Economic Reforms (New Industrial Policy - NIP 1991):** Sparked by the 1991 balance of payments crisis, India dismantled the License Raj: abolition of industrial licensing for almost all sectors, contraction of public sector reservation to atomic energy and railway transport, automatic approval for Foreign Direct Investment (FDI), and elimination of MRTP asset ceilings, unleashing private corporate dynamism.

Unit 13: Core Basic Industries in India

India’s industrial base is supported by the **Eight Core Infrastructure Industries** (comprising over 40% of the weight of the Index of Industrial Production - IIP):

- **Iron and Steel:** Foundational material for automotive, construction, and infrastructure sectors. India is the world's second-largest crude steel producer.
- **Textiles and Garments:** India’s oldest modern manufacturing industry and second-largest employer after agriculture, characterized by high export orientation and integration of cotton farming.
- **Cement:** Second largest global producer, critical for national urban infrastructure and residential housing projects.
- **Sugar and Jute:** Major agro-processing industries providing agro-industrial linkages across Uttar Pradesh, Maharashtra, and West Bengal.

Unit 14: Role and Problems of MSMEs and Cottage Industries

Micro, Small, and Medium Enterprises (MSMEs) represent the vital engine of India's manufacturing dynamism, contributing ~30% of national GDP, ~45% of total manufacturing exports, and employing over 110 million individuals across 63 million enterprises.

Critical challenges confronting the MSME sector:

- *Delayed Payments and Working Capital Squeeze:* Massive payment delays by large corporate buyers and government departments, leading to severe liquidity crises.
- *Credit Gap:* Over 85% of micro-enterprises lack formal collateral, locking them out of formal commercial bank credit.
- *Technological Obsolescence:* Reliance on outdated machinery, resulting in low energy efficiency and inferior product standardization relative to imported Chinese goods.
- *Regulatory Compliance Burden:* Multiple labor laws, local inspection requirements, and GST compliance complexities.

Public Sector Enterprises (PSEs): Reforms, Disinvestment, and Navratna Status

While Central Public Sector Enterprises (CPSEs) laid India's industrial foundation, many succumbed to operational inefficiencies and political interference. Structural reforms post-1991 include:

- **Managerial Autonomy Charters:** Classifying profitable CPSEs into *Maharatna*, *Navratna*, and *Miniratna* categories, granting board-level autonomy to make substantial capital investments and enter global joint ventures without ministerial approval.
- **Disinvestment and Strategic Privatization:** Selling minority equity stakes to retail and institutional investors through IPOs and OFS (Offer for Sale), alongside strategic privatization (e.g., the privatization of Air India).

Category	Pre-1991 License Raj Regime	Post-1991 New Industrial Policy Regime
Industrial Licensing	Mandatory statutory licenses for capacity expansion, location, and products.	Dismantled for >98% of industrial categories.
Public Sector Reservation	17 major heavy industries strictly reserved for state monopoly.	Contracted to atomic energy operations and railway operations.
Foreign Direct Investment	Severely capped (usually 40%), requiring case-by-case cabinet scrutiny.	Automatic route up to 100% across most manufacturing sectors.
Monopoly Regulation	MRTP Act restricting asset growth of large corporate houses.	Competition Act 2002 promoting market contestability and antitrust rules.

Advanced Theoretical Formulations and Empirical Frameworks (Analytical Division 1)

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Empirical Methodology, Identification Strategies, and Econometric Estimation

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Comparative Institutional Analysis, Market Failures, and Policy Governance

Economic outcomes are fundamentally mediated by institutional architectures, legal property rights regimes, and regulatory governance. In emerging market economies such as India, market imperfections—including asymmetric information, transaction costs, infrastructural bottlenecks, and credit constraints—often necessitate nuanced policy interventions that differ substantially from textbook laissez-faire predictions.

Analytical Dimension	Orthodox / Classical Perspective	Heterodox / Institutional Framework	Empirical Policy Manifestations in India
Market Efficiency	Markets clear instantaneously; price mechanism allocates resources optimally without systemic friction.	Markets are prone to structural failures, information asymmetry, and coordination coordination failures.	Targeted regulatory oversight, public investment in infrastructure, and social safety nets.
Behavioral Motivation	Hyper-rational agents maximizing expected utility with complete cognitive computational capacity.	Bounded rationality, behavioral heuristics, loss aversion, and institutional anchoring effects.	Choice architecture, behavioral nudges (NITI Aayog initiatives), and consumer financial protection mandates.
State Intervention	State role restricted to core public goods, contract enforcement, and national defense (minimalist state).	State acts as developmental catalyst, risk-absorber of last resort, and promoter of equitable distribution.	Strategic industrial policy (PLI schemes), counter-cyclical fiscal intervention, and universal public services.
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Technological Progress	Exogenous technological shocks arriving randomly (Solow neoclassical growth model).	Endogenous technological innovation driven by R&D, human capital, and intellectual property institutions.	National Innovation Foundation, Startup India, and public digital infrastructure (India Stack / UPI).

Comprehensive Empirical Analysis: The Kerala Model and Sub-National Development

In the context of the Indian economy and sub-national development paradigms, the Kerala Model of Development provides a seminal empirical case study illustrating the complex trade-offs between social development and economic growth. Characterized by high physical quality of life indicators—including near-

universal adult literacy, high life expectancy, and low infant mortality rates comparable to advanced Western economies—achieved despite historically modest per capita state domestic product, Kerala demonstrates the transformative power of public social expenditure, agrarian land reforms, and decentralized local governance (Panchayati Raj institutions).

However, contemporary economic analysis also highlights structural challenges confronting this development paradigm: high educated unemployment, fiscal constraints stemming from escalating public debt servicing and pension obligations, and heavy reliance on external remittance inflows from migrant workers in the Persian Gulf. Sustaining this high-welfare equilibrium necessitates transitioning toward a knowledge-driven economy, incentivizing high-tech manufacturing, and mobilizing sustainable sub-national fiscal resources.

Policy Synthesis and Analytical Evaluation

Policy formulation in dynamic economic environments must therefore synthesize foundational deductive reasoning with robust inductive empirical inquiry. Economists must continuously evaluate the balance between market incentives and regulatory governance, ensuring that institutional frameworks promote both productive efficiency and distributive social justice.

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