ECONOMIC ENVIRONMENT

Those factors which give a shape and form to the development of economic activities and may include:

- **factors like nature of economic system**
- **general economic conditions**
- **various economic policies**
- **economic reforms**
- **various production factors.**

SOME OF THE FACTORS INFLUENCING ECONOMIC ENVIRONMENT ARE:

- Economic Stages existing at a given time- Prosperity, recession, Depression , Recovery.
- The economic structure(systems) such as Capitalism, socialism and mixed economy
- Economic planning such as Five year plans annual budgets etc.
- Economic policies such as industrial, monetary and fiscal policies
- Economic indices like national income, its distribution, role of growth and growth and growth of GNP, Per Capita Income, Disposable Personal Income, rate of savings, imports and exports, balance of payments etc.
- Infrastructural factors such as Financial institutions, banks, transportation, communication facilities, energy sources etc.

ECONOMIC CONDITIONS

- Nature of the Economy
- Stages of Business cycle - **Prosperity, Recession, Depression, Recovery**
- Inflation/ Deflation
- Economic Resources
- Level of Income

ECONOMIC POLICIES

- Industrial Policy
- Trade Policy
- Foreign Exchange Policy
- Monetary Policy
- Fiscal Policy
- Foreign Investment and Technological Policy

INDUSTRIAL POLICY

- It is a comprehensive package of policy measure which cover various issues connected with the industrial development of the country.
- It can even define the scope and role of different sectors like private, public, joint and cooperative or large, medium, small or tiny.
- It will also spell out Govt policy towards foreign capital, labor tariff and other related aspects.

- Industrial Policy is a formal declaration by the Government whereby it outlines its general policies for industries. Any industrial policy has broadly two parts:
- First part generally deals with the ideology of the current political dispensation,
- While other one provides a framework of certain rules / principles.

The main objective of any industrial policy is to:

- augment the industrial production and thereby enhance the industrial growth which leads to economic growth by optimum utilization of resources;
- modernization;
- balanced industrial development;
- balanced regional development (by providing concessions for industrial development in backward areas);
- balanced development of basic and consumer industry;
- coordinated development of large as well as small, medium and cottage enterprises;
- determination of area of operation under private and public sector;
- enhance cordial relations between workers and management and proper utilization of the domestic / foreign capital.

TRADE POLICY

- A **commercial policy** (also referred to as a **trade policy** or **international trade policy**) is a set of rules and regulations that are intended to change international trade flows, particularly to restrict imports.
- Every nation has some form of **trade policy** in place, with public officials formulating the policy which they think would be most appropriate for their country.
- Their aim is to boost the nation's international trade.

- Trade Policies of the Govt. considerably affect the growth and survival of business firms.

  For instance, a restrictive import policy or a policy of protecting home industries may greatly comfort indigenous industries while liberalisation of import policy may create several difficulties for them.

- The purpose of trade policy is to help a nation's international trade run more smoothly, by setting clear standards and goals which can be understood by potential trading partners. In many regions, groups of nations work together to create mutually beneficial trade policies.

MONETARY POLICY

Definition:

"Monetary policy is concerned with deciding how much money the economy should have or perhaps more correctly deciding whether to increases or decrease the purchasing power of money."

According to Macconal:

"Changing the money supply to assist the economy to achieve a full employment"

UNDER DEVELOPED COUNTRIES

- To achieve full employment
- To have high Efficiency
- To have large scale of resources mobilization
- To increase Exports
- To have high investment
- To provide price and exchange stability
- To have efficient allocation and utilization of resources
- To raise living standards

DEVELOPED COUNTRIES

- To have high aggregate demand without inflation
- Eradicate inflationary and deflationary gap
- High research/ further development
- Providing assistance to other countries
- Gaining monetary control over others

TYPES OF MONETARY POLICY

- **Contractionary / Tight monetary policy**

  "Tight monetary policy, also called contractionary monetary policy, tends to curb inflation by contracting/reducing the money supply"

- **Expansionary /Easy monetary policy**

"Easy monetary policy, also called expansionary monetary policy, tends to encourage growth by expanding the money supply

TOOLS OF MONETARY POLICY

Quantitative Tools

Open Market Operations
Bank Rate
Cash Reserve Requirement
Liquidity ratio
Special deposit

Qualitative Tools

Credit rationing
Credit ceiling
Moral persuasion
Direct action
Advertisement

OBJECTIVES OF MONETARY POLICY

- Price stability
- Credit availability
- Stability of exchange rate
- Full employment
- High rate of economics growth
- Distribution of money

Fiscal Policy-Meaning

- The word **fisc** means '**state treasury**' and fiscal policy refers to policy concerning the use of 'state treasury' or the govt. finances to achieve the macroeconomic goals.
- "any decision to change the level, composition or timing of **govt. expenditure** or to vary the burden ,the structure or frequency of the **tax payment** is fiscal policy."

  - G.K. Shaw
- The fiscal policy is concerned with the raising of government revenue and incurring of government expenditure.

Objectives of Fiscal Policy

1. Development by effective Mobilisation of Resources.
2. Efficient allocation of Financial Resources
3. Reduction in inequalities of Income and Wealth
4. Price Stability and Control of Inflation
5. Employment Generation
6. Capital Formation
7. Development of Infrastructure

FOREIGN EXCHANGE POLICY

- Policy on exchange rate and cross border movement of capital.

  FERA 1973

  FEMA 1999

FOREIGN INVESTMENT AND TECHNOLOGICAL POLICY

- Global sourcing of capital and technology

ECONOMIC SYSTEMS

- The institutional framework regulating the environment on economic basis.

  The ownership, control and management of the enterprise reveal the nature of the economic system.

- Free market economies (Capitalism)
- Centrally planned economies (Socialism)
- Mixed economies

CAPITALISM

- The economic system under which all factors of production are the property of private individuals and firms.

  It is an economic system which is inspired by the spirit of enterprise and is guided by calculation of profit.

CHARACTERISTICS

- Private ownership
- Free Enterprise
- Price Mechanism
- Consumers Sovereignty
- Freedom of Choice of occupation
- Freedom to save and invest
- unplanned economy
- Economic inequalities
- Profit motive
- Competition
- Limited role of Government

MERITS OF CAPITALISM

- Automatic working
- Capital formation
- Maximum satisfaction
- Reward according to capacity
- Efficiency

DEMERITS OF CAPITALISM

- Economic inequality
- Lack of coordination
- Inefficiency in working
- Neglect of national interest
- Unemployment

SOCIALISM

- An institutional framework in which control over means of production and over production itself is vested with a central authority and economic affairs of society belong to the public and not to the private sphere.
- Under this system, the means of production are owned by the people collectively through their government.
- Individuals do not live or work in isolation but live in cooperation with one another.

CHARACTERISTICS OF SOCIALISM

- Government ownership
- Central Planning
- Social Welfare
- Absence of competition
- Redistribution of income
- Restriction on consumption

MERITS OF SOCIALISM

- Economic equality
- Economic stability
- Production Planning
- Optimum use of National Resources

DEMERITS OF SOCIALISM

- Lack of freedom
- Lack of consumer's sovereignty
- Difficulties of management
- Lack of rational calculation of cost - inefficient production (due to state ownership of the source of production)
- Lack of incentive to hardwork

MIXED ECONOMY

- System which shares certain features of capitalism and socialism and is characterised by the co existence of public and private sectors and the overall government regulation of the economy.

CHARACTERISTICS OF MIXED ECONOMY

- Division of public and Private sector
- Government control
- Protection of Labor
- Reduction of economic inequalities
- Economic planning

MERITS OF MIXED ECONOMY

- Economic Freedom
- Control of monopoly
- Social welfare
- Planning and proper use of Resources

DEMERITS OF MIXED ECONOMY

- Temporary Economic System
- Concentration of economic power
- Danger to Democracy
- Bureaucratic inefficiency and corruption
- Denial of social justice
- Imbalance in the economy

RECENT DEVELOPMENTS OF INDIAN ECONOMY

LIBERALISATION

- It is a process of eliminating unnecessary controls and restrictions on the smooth functioning of business enterprises.

It includes:

- Abolishing industrial licensing requirement in most of the industries
- Freedom in deciding the scale of business activities
- Freedom in fixing prices of goods and services
- Simplifying the procedure for imports and exports
- Reduction in tax rates
- Simplified policies to attract foreign capital and technology to india

PRIVATISATION

- Giving greater role to private sector and reducing the role of public sector. To execute policy of privatisation government took the following steps:

- Disinvestment of Public sector.
- Setting up of Board of Industrial and Financial Reconstruction (BIFR).

- Dilution of Stake of Government.

Features of Privatisation:

- Reducing the role of public sector and increasing the role of private sector
- Reducing fiscal burden of the government
- Reducing the size of government machinery
- Speeding up of economic development
- Improving management of enterprises
- Increase in government treasury

GLOBALISATION

- Integrating the economy of a country with the world economy. This implies free flow of goods and services, capital, technology and labor across national boundaries.
- For this Govt. adopted:
  reduction in custom duties
  removal quantitative restrictions
  facilitating foreign investment and encouraging foreign technology
  These measures are expected to:
- achieve a higher growth,
- enlargement of employment potential and
- reduction of regional disparities.

Globalisation has four parameters:

- Free flow of goods and services across national frontiers
- Free flow of capital among countries
- Free flow of technology between nations
- Free flow of labor among different nations

FEATURES OF GLOBALISATION

- Doing or planning to operate business globally
- Considering the whole world as single market – giving up distinction b/w domestic and foreign market
- Locating business on a global consideration not on national considerations
- Global sourcing of factors of production
- Production development and planning on global market considerations
- Global orientation in organisational structure, culture and strategies and managerial expertise

- Buying and selling of goods and services across the globe
- Close cooperations, transportation and communication facilities and acceptability b/w countries and organisations.
- Prevalence of a global investment climate without discrimination and fear of nationalisation
- Global stds. In respect of products, processes, methods, transactions
- Existence of competitive market mechanism

- It witnesses the emergence of new technologies
- Reduced involvement of the state in social security and public utility services
- Globalisation of investment
- Emergence of new markets in Services like banking, insurance etc. new financial markets and global product markets.
- Emergence of new actors in global business, MNCs and TNCs, WTO, Regional Blocs.

- New rules and norms i.e., new multilateral agreements for services, IPRs, communications, trade etc; conventions and agreements on the global environment
- New tools of communications i.e, internet and electronic communications, cellular phones, faster and cheaper transport by air, rail and road.

GLOBALISATION OF INDIAN BUSINESS

Obstacles to Globalisation:

- Government Policy and Procedures – Complex, confusing and cumbersome
- High Cost- Of many vital inputs
- Poor Infrastructure
- Obsolescence
- Resistance to Change
- Poor quality image
- Supply problems

- Small Size
- Lack of experience
- Ltd R&D and marketing research
- Growing competition
- Trade Barriers

FACTORS FAVORING GLOBALISATION

- Human resources
- Wide base
- Growing entrepreneurship
- Growing domestic market
- Niche market

MERITS OF GLOBALISATION FOR INDIA

- High GDP _ 1990-91- GDP -5.6 ; 2007 -08 - 9.3; `2016-7.9
- Wider Choice
- Increased the flow of foreign capital
- Transfer of Technology
- Increase in exports
- Improvements in Balance of Payment (BOP)
- Information Technology revolution
- Growth of service sector
- Growth of Technology and Business Process Outsourcing

DEMERITS OF GLOBALISATION FOR INDIA

- Growth of PVT Sector and unhealthy competition
- Jobless growth
- Neglect of agriculture and adverse impact on food security
- Threat from MNCs
- Overexploitation of resources
- Less flow of technology
- Inequality widened
- Threat to small enterprises

PERFORMANCE OF INDIAN ECONOMY AFTER 1991

Variables	1990-91	2009-10
Growth Rate	5.6	8.6
Wholesale price index	10.3	3.8
Foreign exchange reserves	$1billion	$279.1billion
Gross Domestic saving	23.1	33.7
Gross capital formation	26.3	36.5

IMPACT OF GLOBALISATION ON INDIAN ECONOMY

The following achievements have been claimed especially on the external front:

- India's share in the world trade which had fallen 0.53% in 1991 from 1.78% in 1950 has been reversed trends and has improved to 0.86% in 2003.
- Our foreign currency reserves which had fallen to barely one billion dollars to June,1991 rose substantially to about 141 billion dollars in March, 2005.
- Exporters responding well to sweeping reforms in exchange rate and trade policies. This would be clear from the fact that as against a fall in the dollar value of exports by1.5 % in 1993-96. However, export growth slowed down during 1996-2002. The annual average growth rate during this period was around 8%. Since 2002-2003 however, exports have picked up once again. The average growth of export has been around 10% per annum during 1992-2004.

- Exports now finance over 80% of imports, compared to only 60% in the latter half of the eighties.
- The current account deficit was over 3% of GDP in 1990-91. It has fallen to less the1% in 2000-01. During 2001-03 we even had surplus in current account ranging between 0.7-1.08 percent of GDP.
- At the time of crisis, our external debt was rising at rate of 8 billion a year, after that its growth has been arrested. From 1996-2003, it grew only by less than ₹3 billion %
- Contrary to what many feared, the exchange rate for the rupee has remained almost steady despite the introduction of full convertibility of rupee.
- International confidence in India has been restored. This is indicated by swelling foreign direct and portfolio investment. FDIs were just 155 million dollars in 1991.They increased to around 3200 million dollars in 2004-05

- Certain benefits of globalisation have accrued to the Indian consumer in the form of larger variety of consumer goods, improved quality of goods and in some cases and reduced prices of consumer durable.
- Markets have started responding to the movements abroad. A fluctuation in U S. market or U.K. market has started affecting Indian market. Unlike before, SENSEX and other parts of the globe
- The rating agencies, which rate investments risks in countries for global investors, have aggraded India's rating.
- Programmers of quality management and research and development are systematically conducted by corporate sector

DISINVESTMENT

- Disinvestment is a process in which the public undertaking reduces its portion in equity by disposing its shareholding. “Disinvestment” as per SEBI guideline, means the sale by the central government/state government, of its shares or voting rights and/or control, in PSUs. The disinvestment reduces government participation in the company.

DISINVESTMENT AND INDIA

- In India , the new economic policy have given rise to significant focus for privatization of public sector enterprises.
- Disinvestment is one of the method of privatization, which started in the year 1992.
- It implies selling of govt. equity shares of public sector units in the market.
- It is a concrete step towards privatization and liberalization of our economy .

CRITERIA FOR DISINVESTMENT

The decision regarding disinvestment or liquidation viewed in the light of following criteria:

a) Whether the objectives of the company are achieved

b) Whether there is decrease in number of beneficiaries

c) Whether serving the national interest will be affected because of disinvestment

d) Whether private sector can efficiently operate and manage the undertaking.

e) Whether the original rate of return targeted could not be possible to achieve.

f) Whether socio-economic objectives lots its purpose

MERITS OF DISINVESTMENT

- In Private Sector, the decision making process is quick and decisions are linked with the competitive market changes.
- The disinvestment process would bring in better corporate governance, exposure to competitive, corporate responsibility, improvement in work environment etc.
- The market participation in capital of PSUs through stock exchanges would enable the market to discover the latent worth of PSUs.
- The Loss making PSUs can be successfully revived by asking the strategic partner to infuse fresh capital and exercising excellent management control over sick PSUs.

DEMERITS OF DISINVESTMENT

- Selling of profit-making and dividend paying PSU would result in loss of regular source of income to the government.
- There would be chances of ‘asset stripping’ by the strategic partner. Most of the PSUs have valuable assets in the shape of plant and machinery, land and buildings etc.
- The Government’s Policy or disinvestment includes the disposal of both profit making, as well potentially viable PSUs.

PRIVATIZATION VS. DISINVESTMENT

- **Privatization** implies a change in ownership, resulting in a change in management.
- The privatization of public sector enterprises will occur only when govt. sells more than 51% of its ownership to private entrepreneurs.
- **Disinvestment** on the other hand, has a much wider connotation as it could either involve dilution of govt. stake to a level that result in a transfer of management or could also be limited to such a level as would permit govt. to retain control over the organization.
- Disinvestment beyond 50% involves transfer of management, where as disinvestment below 50% would result in the govt. continuing to have a major say in the undertaking .