

TRADE AND FDI RELATED REFORMS IN THE STATES, 1991-2007:

THE CASE OF MAHARASHTRA

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EXECUTIVE SUMMARY

The liberalisation policy of India that was initiated in 1991 was designed to dismantle the protectionist regime through removal of industrial licenses, thereby reducing the strict bureaucratic control under which the country's foreign trade had been suffering for decades. The Import and Export (Control) Act of 1947 was replaced by the Foreign Trade (Development and Regulation) Act of 1992, empowering the central government to announce and amend the export and import policy, or trade policy as it is called. The export-import policy was further liberalised several more times with the introduction of substantial concessions to boost agricultural exports, as well as initiatives of export promotion and the setting up of industrial parks. The unilateral initiative of liberalisation was later supported by commitments made under the World Trade Organization (WTO) regime, and further liberalisation of imports through removal of import licenses, quotas, and quantitative restrictions.

The federal division of power between the central and state governments in India allows the central government to formulate trade policy. The state governments remain primarily as the implementing bodies. With the same liberalised trade policy announced for all states and union territories of the country, the impact of policy on export-import, inflow of foreign direct investment, and growth rates, vary largely among states, partly due to the difference in state initiatives supporting them.

The response to liberalisation policies followed by the WTO mandate at the union level, and its impact on the overall economy, has been broadly discussed in several studies. This particular study attempts to analyse how the state of Maharashtra has fared

in changing its trade-related policies and the implementation, in response to economic reforms that were implemented during the period of 1991-2007. Here, I define 'trade-related policies' as those policies and initiatives of the state government that affect international trade of the country or support the trade policy of the Centre. This includes state-level tax policies, initiatives to attract foreign or domestic investors in the state, export promotion initiatives, and development initiatives affecting business and investment in the state. It also discusses the changing role of business in the state, the bureaucratic mechanism working towards implementation of policies, the role of political parties of the state, and the role of chief minister as a leader of the state in framing and implementing trade-related policies.

The business climates across states of India vary to some extent due to the difference in state-level bureaucracy. Getting government approval for business or to set up plants, getting environment clearance, getting utility connections, and all other related procedures, take time of different lengths across different states in India. Some states are a little ahead of their counterparts in these respects, because of their various initiatives including e-governance, or the creation of a single-window system for all required clearances. These initiatives work to attract investments in the state and to increase the contribution of the state in the volume of international trade. Maharashtra, the subject of this case study, has been among the forerunners in some of these initiatives, along with the states of Gujarat, Andhra Pradesh, and Tamilnadu. Maharashtra is currently in the process of creating a single window clearance system for industries.

Maharashtra has been able to attract investors primarily through various incentive schemes and the development of several industrial clusters. According to industrial bodies, however, most investors would rather see more of the long-term development of infrastructure required for the industries than the setting up of incentives.

As things are, Maharashtra has in place a certain amount of reliable infrastructure. It has one of the best road and railway networks across India and houses two of the country's major ports. There remain concerns, however, including the increasing amount of port traffic and the delay in issuance of clearances at ports. Since international trade and investment has direct links to the availability of port facility, the state government should work to reduce the amount of turn-around time at port, along with more efficient

issuance of clearances. Moreover, the state government must take proactive measures in making labor laws more flexible in order to encourage the flow of foreign investments into the state, keeping in mind that the center is unable to repeal laws without state approval.

In most of the electoral terms thus far, the leading party of the state of Maharashtra -- either the coalition or the single party -- had some representation in the central government. This helps to maintain good relationship with the Center. However, when we look at the state leadership, none of the political leaderships in Maharashtra has been as exemplary as those of the states of Gujarat or Andhra Pradesh, where the chief ministers were showcased as leaders in their respective states' reform initiatives. The case of one of the largest automobile corporations in the country, based in Maharashtra, indicates that if the state leadership has a larger say in the cabinet then that facilitates implementation of any project.

The example of Enron project provides a lesson calling for political stability in state leadership. Enron Corporation from the USA signed an MoU to build a power plant in Dabhol in 1992. From the very beginning, this project was enmeshed in controversies relating to non-competitive bidding, inefficiency and high tariff rate. Finally, the project was scrapped in 2001 after ninety-five per cent of its completion. This case also highlights the fact that when a state is ruled by a coalition government, then sometimes major decisions are taken keeping the political interest of all partner parties in mind..

In this study the performance of the state of Maharashtra has also been analysed by looking at some major macroeconomic indicators affecting business. An examination was also made of whether state policy was effective enough to take advantage of liberalisation or it was, by nature, more protective.

The following were considered as major indicators for this present study: growth indicators of the state; patterns of revenue receipts in the state; patterns of state financing; governance and institutional regulatory/quality indicators; and the availability of physical infrastructure. The growth indicators indicate that Maharashtra stands among India's leading states, with the highest figures for state domestic product and its rate of growth. The ratio of debt to Gross State Domestic Product has increased over the years, indicating higher amount of borrowing, primarily for public projects. The state is ranked sixth in the

Index for Social and Economic Infrastructure, lagging behind states like Tamilnadu, Gujarat, and Kerala. Finally, the study includes two sectoral case studies: one on Automobiles and Auto component industry, and another on the Pharmaceutical industry.

The objective of the present study is to explain how all these factors have worked in Maharashtra in the growth and development of those sectors. The study reveals that Maharashtra has been a major hub for automobile and auto components companies for the last few decades, due to several factors, including: the closeness of ports and good connectivity; availability of skilled manpower and designing, training institutes; state-level initiatives to attract investors; and, most important of all, the forward and backward linkages for the industry. However, state needs to be more proactive in the coming years through development of infrastructure, if Maharashtra intends to stand in competition with states like Uttaranchal and Tamilnadu for attracting FDI. The development of Maharashtra's Pharmaceutical industry can also be attributed to the availability of skilled manpower and state-level initiatives through development of Specialized Industrial Areas. The state has also announced a separate Biotechnology Policy, which brings some benefits to the investors in Pharmaceutical sector as well. But the sustained development of this industry perhaps needs strong initiatives by the state in order to boost research and development, particularly in areas contributing to intellectual properties, rather than concentrating only on services like contract research and manufacturing or clinical research.

A brief policy prescription, along with a list of recommendations, concludes this study. These recommendations are being made in order to assist policymakers, investors, and business houses alike in learning from the past and making those lessons work for an improved economy.