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SRUJANI: Indian Journal of Innovative Research and Development (SIJIRD)
Volume-4 Issue 6, January-February 2026, Pp. 18-25
Bi-Monthly, Peer-Reviewed, Open Access, Indexed Journal

I S S N: 2583-3510
SIRDF JOURNALS
editor@srujani.in
www.srujani.in

# The Role of Economic Liberalisation in India's Growth and Development

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***Abstract:***

*Economic liberalisation refers to the systematic reduction of state control over economic activities and the promotion of market-oriented reforms such as deregulation, privatisation, and openness to international trade and investment. Since the late twentieth century, economic liberalisation has emerged as a dominant development strategy adopted by both developed and developing countries to accelerate economic growth, enhance efficiency, and integrate national economies into the global market. This article examines the conceptual framework, objectives, and key policy instruments of economic liberalisation, with particular emphasis on its impact on economic growth, employment, industrial development, and social equity. The study also critically analyses the challenges and criticisms associated with liberalisation, including rising income inequality, vulnerability to global market fluctuations, and the marginalisation of weaker economic sections. By evaluating both the positive and adverse consequences, the article seeks to provide a balanced understanding of economic liberalisation as a transformative yet contested economic reform process.*

***Keywords:*** *Economic Liberalisation, Market Reforms, Globalisation, Privatisation, Economic Development*

## Introduction

Economic liberalisation refers to the process of reducing government restrictions and regulatory controls over economic activities in order to promote free market forces, private enterprise, and global integration. It involves policy measures such as deregulation, reduction of trade barriers, privatisation of public sector enterprises, and encouragement of foreign investment. The primary objective of economic liberalisation is to enhance efficiency, productivity, and overall economic growth by allowing market forces to play a greater role in the functioning of the economy.

***Please cite this article as:*** Asha, K.N. (2026). The Role of Economic Liberalisation in India's Growth and Development. *SRUJANI: Indian Journal of Innovative Research and Development.* 4(6), 18–25

In many developing countries, including India, economic liberalisation emerged as a response to prolonged economic stagnation, balance of payments crises, and structural inefficiencies resulting from excessive state control. The liberalisation process marked a significant shift from a highly regulated and inward-looking economic system to a more open, market-oriented, and globally integrated economy.

Since the early 1990s, terms such as *liberalisation*, *privatisation*, *globalisation*, *market economy*, *competitiveness*, and *free market* have gained increasing prominence in economic and political discourse. In the developed Western countries, these concepts became standardised within the broader ideological framework of liberalism. In the former USSR, during the mid-1980s, the terms *Perestroika* (restructuring) and *Glasnost* (openness) gained widespread attention when Soviet leader Mikhail Gorbachev used them to emphasise the need to liberalise the command economy and open the closed political system.

The political and economic liberalisation processes that emerged in the USSR and other socialist states of Eastern Europe significantly increased the popularity of these ideas. This phase witnessed the collapse of communist regimes and their replacement by liberalised political systems. Simultaneously, economic liberalisation involving structural reforms and the development of open market economies based on competitiveness and free trade began to take shape in these countries. The former socialist states gradually evolved into liberal democracies with liberalised economic systems.

Following these developments in the socialist world, a global movement towards liberalisation, privatisation, free trade, market economy, competitiveness, and globalisation gained momentum. Most countries recognised the potential of these principles in achieving rapid, comprehensive, and sustainable economic development. India, too, decided to adopt economic liberalisation and privatisation as core components of its economic policy framework. The introduction of the New Economic Policy in 1991 clearly reflected this strategic shift.

It is important to note that liberalisation does not imply the adoption of full-fledged capitalism. Rather, it signifies the removal of unhealthy control mechanisms, excessive regulations, and structural barriers that hinder economic growth. Privatisation is only one instrument of liberalisation. Measures such as encouraging the private sector, undertaking disinvestment in public sector enterprises to enhance competitiveness, promoting a market-oriented economy, embracing globalisation, and accelerating industrial, technological, and economic development together constitute the core content of economic liberalisation.

**What is Liberalisation?**

Liberalisation denotes both political and economic dimensions. In the erstwhile communist states, liberalisation was initially adopted to free political systems from authoritarian practices and rigid controls, and subsequently to replace centralised command economies with market-oriented economic systems. For these countries, liberalisation thus implied the adoption of both political and economic liberalism.

In contrast, for a country like India—whose political system was already functioning as a liberal democratic system based on free and open competition for political power among individuals organised through voluntary groups and political parties—liberalisation primarily referred to economic liberalisation. It signified reforms aimed at achieving rapid, comprehensive economic growth and development rather than political transformation.

India's economic system prior to the reforms was a mixed economy in which the private sector already played an important role alongside the public sector. In this context, liberalisation broadly meant the process of *de-licensing*, reduction of restrictive regulations, and easing of excessive state control over private enterprise. The New Economic Policy marked a shift in approach by recognising that, despite certain regulatory distortions, the private sector had often demonstrated greater efficiency and competitiveness than the public sector. Consequently, a reduced emphasis on the public sector and a greater role for the private sector became central to the reform strategy.

Privatisation emerged as one of the important instruments of liberalisation, involving disinvestment and restructuring of public sector enterprises to enhance efficiency and competitiveness. The primary objective of liberalisation was to create an economic environment conducive to rapid economic, industrial, and technological development through healthy competition. Providing greater opportunities for private enterprise, encouraging entrepreneurship, and promoting efficiency became essential components of India's liberalisation strategy.

Along with these reforms, the need to attract foreign investment and to integrate the Indian economy with the global economy led to the adoption of globalisation as an integral part of the policy of economic liberalisation. Thus, liberalisation, privatisation, and globalisation together formed the core of India's new economic policy framework.

## Meaning and Concept of Economic Liberalisation

Economic liberalisation refers to the relaxation of government controls over economic activities. It does not imply the complete withdrawal of the state from the economy; rather, it involves a redefinition of the state's role—from that of direct control and ownership to one of regulation, facilitation, and oversight. The focus of liberalisation is to create a competitive economic environment in which private enterprises can operate freely, innovation is encouraged, and resources are allocated efficiently.

The key aspects of economic liberalisation include:

- Removal or reduction of industrial licensing and permit requirements
- Reduction of tariffs and quotas on imports and exports
- Encouragement of private sector participation and foreign direct investment
- Deregulation of financial markets
- Simplification and rationalisation of tax structures

Economic liberalisation aims to integrate the national economy with the global economy, enabling countries to benefit from international trade, technology transfer, capital flows, and enhanced competitiveness in the global market.

**Background of Economic Liberalisation in India**

Before 1991, India followed a mixed economy model with a strong emphasis on central planning and extensive state control. The government regulated major industries through an elaborate licensing system, exercised strict control over foreign trade, and dominated key sectors of the economy through public sector enterprises. While this model contributed to the creation of a basic industrial infrastructure, it also resulted in inefficiency, low productivity, bureaucratic delays, corruption, and a relatively slow rate of economic growth.

By the late 1980s, the Indian economy was confronted with a severe macroeconomic crisis marked by a high fiscal deficit, rising inflation, and an acute balance of payments problem. Foreign exchange reserves declined to critically low levels, severely limiting the country’s ability to finance essential imports. In response to this crisis, the Government of India initiated a comprehensive programme of economic reforms in 1991 under the leadership of Prime Minister P. V. Narasimha Rao and Finance Minister Dr. Manmohan Singh.

These reforms introduced the policy framework of Liberalisation, Privatisation, and Globalisation (LPG), with economic liberalisation forming the central pillar of the reform agenda. The reforms aimed at restructuring the Indian economy to enhance efficiency, competitiveness, and integration with the global economic system.

**Objectives of Economic Liberalisation**

The primary objective of economic liberalisation is to promote sustained economic growth by removing excessive regulatory restrictions and encouraging healthy competition in the economy. Through market-oriented reforms, liberalisation aims to increase production, improve efficiency, and enhance overall economic performance. Another important objective is to improve efficiency and productivity by compelling firms to utilise resources more effectively, reduce operational costs, and enhance the quality of goods and services through competitive pressure. Economic liberalisation also seeks to encourage greater participation of the private sector by creating a favourable investment climate that allows private enterprises to expand, innovate, and contribute actively to economic development. Additionally, liberalisation aims to attract foreign direct investment (FDI) by simplifying regulations and opening up various sectors of the economy, thereby facilitating the inflow of advanced technology, capital, and managerial expertise. Finally, economic liberalisation strives to integrate the national economy with the global economy by promoting international trade and cooperation, enabling countries to benefit from globalisation, technology transfer, and increased global competitiveness.

**Progress of Economic Liberalisation Since 1991**

The New Economic Policy, implemented in 1991, based on the principles of liberalisation, privatisation, globalisation, and a market-oriented economy, laid the foundation for a system marked by significant deregulation of industry. The practice of industrial licensing, introduced under the Industrial (Development and Regulation) Act of 1951, was largely abolished. Restrictive control mechanisms were minimised, and only industries related to defence or those posing serious health or environmental hazards now require licensing.

Similarly, the concept of monopoly control over large business houses, as prescribed by the Monopolies and Restrictive Trade Practices (MRTP) Act, was abolished. There are now no limits on large industrial houses wishing to undertake new investments, allowing greater freedom and flexibility in industrial expansion.

Over the past 25 years, successive Indian governments have consistently supported the liberalisation of the Indian economy. After assuming office on 13 October 1999, the National Democratic Alliance (NDA) government announced plans for introducing second-generation liberalisation reforms. The Congress-led United Progressive Alliance (UPA) governments under Prime Minister Manmohan Singh actively continued the process of economic liberalisation, privatisation, and promotion of a market-oriented economy.

The NDA government under Prime Minister Narendra Modi, in power since 26 May 2014, has also steadfastly pursued economic liberalisation, recognising it as a key instrument for achieving rapid and comprehensive economic growth and development. Over the past quarter century, multiple governments have implemented reforms across various sectors of the Indian economy, helping it become increasingly liberalised, competitive, and robust.

## Major Economic Policies and Decisions under Economic Liberalisation

### *Foreign Investments*

In the era of liberalisation and globalisation, India not only permits but actively encourages foreign direct investment (FDI). The policy provides for automatic approval of foreign equity participation up to 51% in selected high-priority and high-technology sectors. Foreign brand names and trademarks for goods sold in India are allowed, and the process for entering into foreign technology agreements has been simplified. The approval of such agreements, provided they meet established guidelines, is guaranteed. A Foreign Investment Promotion Board has been set up to facilitate and negotiate foreign investments. Both the Central and State Governments have signed numerous Memorandums of Understanding (MoUs) to strengthen industrial, trade, and economic relations with other countries. In 2015, the NDA government announced increased FDI in core sectors, including railways, defence, insurance, and infrastructure, including real estate.

### *Foreign Exchange Rate System*

The liberalisation of foreign exchange management was a key reform. Recognising that Indian exports were non-competitive due to an overvalued rupee, the currency was devalued twice in July 1991, resulting in a total devaluation of 22%. This measure aimed to boost exports without subsidies and incentivise remittances and capital inflows, particularly from Non-Resident Indians (NRIs). As a result, India's foreign exchange reserves improved significantly, enabling the country to repay debts and finance imports. By the mid-1990s, Indian exports began to increase steadily, a trend that continues today.

### *Rupee Convertibility*

Another major reform was the introduction of the Liberalised Exchange Rate Management System (LERMS) on 1 March 1992. The rupee was made partially convertible, and later, in the 1993–94 budget, it became fully convertible on the current account. Under this system, all foreign exchange receipts—from exports, remittances, etc.—could be converted at market-determined rates. Higher market rates provided better returns to exporters, incentivising trade. The system also encouraged legal remittances, reduced illegal (hawala) transactions, limited the gap between official and market rates, and enhanced India's credibility in the international market.

### *Privatisation of Public Sector*

Acknowledging the underperformance of many public sector enterprises, the government undertook measures to prune and restructure this sector. While 17 industries were previously reserved for the public sector, now only eight remain, and private participation is allowed where necessary. Disinvestment of public sector shares has been undertaken, and budgetary transfers to public enterprises have been drastically reduced. The public sector is now being geared to compete with the private sector. In September 2014, the Modi government announced plans to privatise four major public sector companies, including ONGC.

***Trade Policy***

The new trade policy introduced significant structural changes to liberalise the tightly controlled regime of import licences, high tariffs, import restrictions, and canalised trade through public agencies. Measures towards delicensing and deregulation were initiated to simplify and liberalise trade practices, fostering a more competitive trade environment.

***Fiscal and Financial Sector Reforms***

Financial sector reforms allowed banks and other public financial institutions greater operational flexibility to improve efficiency, productivity, and competitiveness. Following the Narasimha Committee recommendations, the Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR) were gradually reduced. In April 1997, the Reserve Bank of India (RBI) reduced the prime lending rate and primary interest rate by 1% each to increase the availability of funds for industrial and economic development. Private banks were permitted, and banking institutions were encouraged to plan and implement policies within RBI and government guidelines. Tax reforms, guided by the Chelliah Committee, rationalised personal and corporate tax structures, lowered rates, and increased the taxpayer base while simplifying tax collection systems.

***Liberalisation, Privatisation, and Globalisation (LPG)***

The New Economic Policy (NEP) reforms were based on the principles of liberalisation, privatisation, and globalisation. The aim was to strengthen the economy by removing the shackles of licences, controls, permits, quotas, and other restrictive regulations across industry, trade, and fiscal management. Privatisation involved reducing the scope of public sector industries, disinvesting in public enterprises, encouraging private sector participation, and opening previously reserved sectors to private and multinational corporations.

***Integration with the World Economy***

Globalisation, as an integral part of liberalisation, aimed to integrate India's economy with the global economic system. Protectionist measures, such as high tariffs, quotas, licensing, and other controls, were reduced to encourage competitiveness—a key requirement for rapid economic development. Previously, over-protection of domestic industries had hindered growth and led to dependence on subsidies and other concessions; liberalisation sought to address these inefficiencies.

**Conclusion**

Economic liberalisation has been a transformative force in India's economic development. By reducing excessive government control and encouraging private sector participation, it has fostered competition, enhanced efficiency, attracted foreign investment, and accelerated overall economic growth. Liberalisation has also facilitated greater integration of the Indian economy with global markets, creating new opportunities for trade, technology transfer, and investment. While these reforms have significantly strengthened the economy, sustained inclusive and balanced growth requires complementary policies to address social equity, regional disparities, and support for vulnerable sectors. Overall, economic liberalisation has laid the foundation for a more dynamic, competitive, and globally connected economy.

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