

## The Unequal Effects of Liberalization: Evidence from Dismantling the License Raj in India

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*We study whether the effects on registered manufacturing output of dismantling the License Raj—a system of central controls regulating entry and production activity in this sector—vary across Indian states with different labor market regulations. The effects are found to be unequal across Indian states with different labor market regulations. In particular, following delicensing, industries located in states with pro-employer labor market institutions grew more quickly than those in pro-worker environments. (JEL J50, L52, L60, O14, O15, O25)*

In the postwar period, planned industrialization became a widespread development strategy for tackling economic backwardness. In the 1980s, however, amidst growing dissatisfaction about its results, many developing countries progressively liberalized their economies by dismantling government controls over industry and opening up to trade. Despite the pervasiveness of these reforms, there is little sound empirical evidence on whether and how they interact with local institutions. The same nationwide reform could lead to quite different outcomes, depending on the local institutional environment.

The aim of this paper is to examine the interaction between product market deregulation and the organization of labor markets in India. We focus on a little-studied internal liberalization episode, the dismantling during the 1980s and 1990s of the License Raj—a system of central controls introduced in 1951 regulating entry and production activity in the registered manufacturing sector. Delicensing reforms were staggered over a decade, but were nationwide in scope: when an industry was delicensed, the policy change affected all Indian firms in that industry, irrespective of location. The focus of our analysis is on whether institutional differences across Indian states, particularly in labor market regulations, led to a differential response in industrial performance to the reform across states.

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