SYLLABUS - ECONOMY

GS - III : Economic Development

- Indian economy & issues relating to planning, mobilization of resources, growth, development & Employment
- Inclusive growth & issues arising from it
- Government Budgeting
- Major crops - cropping patterns in various parts of the country, diff. types of irrigation & Irrigation systems storage, transport & marketing of Agricultural Produce & issues and related constraints; e-technology in aid of farmers
- Issues relating to direct & indirect farm subsidies and MSP (Min. supp. prices); PDS - objectives, functioning, limitations, Revamping; issues of Buffer stocks & Food security. Technology missions; Economics of animal-rearing.
- Food processing & related issues industries in India - scope & significance, location, upstream & downstream requirements, supply chain Management
- Land reforms in India
- Effects of liberalization on Economy, changes in Industrial policy & their effects on Industrial Growth.
- Infrastructure: Energy, Ports, Roads, Airports, Railways etc
- Investment Models

ECONOMICS

NCERTs - XI^th^ - Indian Economy
XII^th^ - Macroeconomics
(National Income Accounts
Money & Banking
Budget
Balance of Payment
X Det. of Income)

Read like a story book
- Don't bother about Graphics.

Dictionary (Economics) - Collins / Penguin - If very necessary
- usually not useful after some time

- Empirical evidence - Always back opinions with data
- Entertain the different questions
- Keep your political findings off - No favouritism
(Be keen in getting data, analyse it from all dimensions and understand it with the present system and try to arrive at a solution which is equitable, pragmatic and appropriate)

What is an Economy?

An economy is any space (real or virtual) with well-defined rules and established institutions to implement those rules.

What are economic activities?

All those activities which create value and which can be measured are called economic activities. they include:

- Production: converting inputs → outputs
- Consumption: utilization
- Exchange: presence of a market
- Distribution: How is things reaching ppl

Opportunity Cost

Cost of sacrificing the second best alternative.

What is GDP?

Total value of final goods & services produced in domestic territory of an economy in a given accounting or Financial year is called GDP. — Where is it produced?

If something is institutionalised, there is more probability of it being continuous — procedures followed as 'a system'.

Examples he cited:

- Ujjwala scheme
- Delhi electricity subsidy
- Agricultural subsidies, investments
  - Empowering or Dependent keeping pittance
  - Taxation on Farmers
- Don't just allocate funds, but target it properly with backups of data collected scientifically.

Investments	Savings
Only things which produce further	Things which doesn't produce something

Financial investments in economics are considered savings → Resource to Finance Investment

Ex: Additions to capital goods

Ex: Financial investments

⇒ GDP in India is estimated by CSO [Central Statistical Organisation] under Ministry of Statistics & Program implementation.

⇒ Financial year in India ⇒ April 1st – March 31st

↳ Divided into Quarters – 4 divisions – 3 months each

↳ In 1984, 1st time debate started to make Jan–Dec the fin. Year:

- Benefits:

  India in co-ordination with Global Economy

  People will be comfortable when calender year is same as it.

- Difficulties:

  Mighty administrative shift to advance the data collection req. to prepare early Budget

  ZERO YEAR

  Heavy information campaign to inform ppl to submit in advance in an economy as diverse as us.

Final Goods & Services

I] Use Based classification:

i] All those G & S that are used for final satisfaction & not for further production are called Consumer goods & Services

Ex: Refrigerator @ Home

Only exception: Housing – Always capital good

ii] All those goods which are used for further production of G & Ss over a long period of time are called Capital Goods.

– Addition to the stock of capital goods is called Investment.

Ex: Refrigerator @ Shop; Car used in service

ii] Intermediate Goods & Services

All those g&s which are used for further production of G & Ss for sale in the market & which get completely utilised during production process are called Intermediate goods & services.

Ex: Fuel used in that car for service

↳ These are not included in the Final goods & Services for GDP.

- To avoid double-counting
- Consider only as Value added to the produced good.

Don't get entangled with -isms Capitalism, Socialism - Be pragmatic - Not Dogmatic - solving the problem & achieving obj is the focus. Don't see promises but what it delivers

no use if -isms however great as theory if can't be implemented

Quality of Answers
- Knowledge
- Way we structure our answers with that knowledge

- Be nuanced, diverse, analytical, empirical

Domestic Territory

i) Land + Sea Boundaries [12 Nautical Miles]

ii) Aircrafts + Ships - By Operated residents of the country

iii) Oil platforms + Gas rigs - operated by residents of the country

iv) Embassies + Consulates - countries which they belong & not they are located.

SNA - System of National Income Accounts - 1992 - 2008

LA meeting of UN members to arrive at a common system of calculating the aggregates (GDP).

Indigo aircraft (HQ in India) in US is still an Indian territory

[These divisions are only for the calculation of GDP. Rules of the country will bind on Aircraft, Oil platforms]

What is GNP? Total Value of Final Goods & Services produced by normal residents of an ~~country~~ economy in a given accounting year is called GNP. – Who produced it?

__Normal Residents__ are individual who live in a country for more than one year and whose centre of economic interest is in that country

$$GNP = GDP + \overbrace{\text{Factor income from Abroad} - \text{Factor Income To Abroad}}^{\text{Net Factor Income from abroad}}$$

production done by domestic resident in foreign country — Production by Foreign resident in dom. country

[there is nothing like: always GDP > GNP or vice versa as Net factor can be +ve or -ve]

2 Exceptions to the rule of qualifying normal residents:

i) All tourists, students and Govt. employees posted abroad are considered as Normal residents of country to which they belong irrespective of the time period.

ii) Border workers (ppl who cross international border everyday) are considered as normal residents of country in which they live and not in which they work.

What is Depreciation? Loss in value of capital due to normal wear and tear during production process and foreseen obsolescence is called depreciation. It is also called Replacement cost of capital.

When value of depreciation is subtracted from GDP, it is called NDP [Net Domestic Product]

In General:

When we subtract depreciation it becomes "Net", if not, "gross".

- Depreciation is not even 1% of the economy, so it doesn't matter much.
- It is difficult to calculate depreciation of every firm.

Reasons why we use GDP & not ~~GNP~~ NDP even if ~~GNP~~ NDP is more accurate way of assessment.

we use this to measure growth rate

What is GDP @ Market Price?

When GDP is calculated by including value of net indirect tax then it is called GDP @ Market price.

% in GDP
Production method
Income method
Expenditure method

[Net Indirect tax = Indirect tax - Subsidy]
(Indirect tax: increases cost, ex: GST; Subsidy: decreases cost)

Expenditure of Firm:

1. Intermediate goods
2. Depreciation
3. Net Indirect Tax
4. Rent + wage + Interest + Profit

Opp. cost of entrepreneur is profit for firm & it is obliged to pay that to him

Receipt of Firm:

Gross value of Output [1+2+3+4]

"Don't fall into glamour part of UPSC — Just one more exam — be work-man like." (Build basics first)

Gross value of Output @ Market price − Intermediate G & S ⇒ Gross Value Added @ market price

"Circumspect"

Gross value added − Depreciation
@ market price − Net Indirect Tax ⇒ Net Value added
NDP@FC { @ FACTOR COST

bcos net indirect tax subtracted
- Actual cost of production

Σ G. Value added @ market price of all firms } GDP @ market price

Production method

Σ Wages + Rent + Interest + Profit of all H.Hs by all firms — INCOME METHOD
NDP @ factor cost

Earn
Firms → Revenue
↓ distribution
H.Hs → Income

INCOME METHOD:
(for tangible goods)
① Rent + Royalty (for intangible goods)
② Profit
③ Interest on Investment

Nominal | Real

Post office ex:
1000 @ 8.7% − 8% infl
1000 @ 7.5% − 5.5% infla

Here-Real interest = Interest − Inflation
(Nominal interest = Interest including inflation i.e - @ money value)

RBI repo rate ex:
why interest % is reduced in post office?
RBI ↓ Reporate

④ Compensation of Employees
(Including social securities, facilities like insurance)

⑤ Mixed income of self employed Ex: A fruit vendor
(used only if ①,②,③,④ not clear)

Income = Rev − Exp

NDP @ Factor Cost

National Income:

N.D.P @ F.C + Net factor income from abroad

N.N.P @ F.C

NDP @ FC
+ Dep

GDP @ FC
+ N.I.T

GDP @ MP

Calculate any aggregate and we can reach all others!

EXPENDITURE METHOD:

① Final Consumption Expenditure (C)
+
② Investment (I)
+
③ Govt. Expenditure (G)
+
④ (Exports − Imports) = Net Exports (NX)

GDP @ M.P

In India, we include subsidies in expenditure even though they are actually TP.

also includes spending on imports (goods of foreign)

Export is the expenditure of foreigners on our Production

Total expenditure on G&S produced in domestic territory.

(i.e) Expenditure of all 4 sectors
[① HH ② Firms ③ Govt ④ External sector]
Financial sector is included in all ④s.

If the economy is too controlling or too restrictive most ppl will evade.
Ex: High tax on registration

Critical Analysis of New Measure of Growth in India:

What? the ~~govt.~~ did
why? did they do it
What? are the issues ppl oppose / question it
L Gaps

Till January 2015 we were using GDP @ FC. Now @ MP.. (Passed in 2001 itself

How? To fill the gaps - solve issues

In the new method, introduced in Jan 2015 by CSO, growth is calculated using GDP @ MP while earlier it was calculated using GDP @ FC. $\boxed{GDP_{MP} = GDP_{FC} + N.I.T}$ Product tax — Product subsidy.

CSO has also introduced another aggregate called Total Gross value added @ Basic price which is sum of Total Gross value added @ FC and Production Tax like stamp duty.

$\boxed{\text{Total G.V.A @ Basic price} = \text{Total G.V.A @ FC} + \text{Production tax (Ex: stampduty)}}$ which can't be immediately got from consumer

i) This helps in knowing both consumption side and Production side of Economy. It also makes India's growth measures more contemporary because most of the market economies use GDP @ MP as growth measure.

ii) The old method used data from 2500 firms, in the new method auditioned report of approximately 5 lakh firms submitted to Ministry of Corporate Affairs (MCA 21 technique) is used along with enterprise survey (manufact. sector) & establishment survey (service sector) to get better understanding by including new sectors like

Tution, brokerage, beauty salon, recycling Industry etc., It helps in increasing the understanding about economic activities and sources of income.

Tuition sector: 38,000 crore.
[Till 2012, no services tax on tuition centres]

iii) Base year has been shifted from 2004-05 to 2011-12. Base year is used as standard year to make comparisons by calculating GDP in Real terms. ∴ Base year should be chosen such that it is a normal year (i.e)- without any war, severe drought, bumper production — No extraordinariness.

Nominal GDP (or) GDP @ Current year price

=> shifting base year every 6-7 years is essential bcos it will better represent the trend, new G&S, consumption patterns.

Final G&S	$P_{2011-12}$	$Q_{2011-12}$	$(P \times Q)_{11-12}$	P_{15-16}	Q_{15-16}	$(P \times Q)_{15-16}$	$P_{11-12} \times Q_{15-16}$
X	10	10	100	20	20	400	10 × 20 = 400
Y	10	10	100	20	20	400	10 × 20 = 400
		Nominal GDP (or) GDP @ curr. price	200		Nominal GDP 15-16	800	Real GDP 15-16: 400

Problems in New Method:

i) Growth rate recorded in certain sectors by new method doesn't match

Equitable	Vs	Equal
Similar		same
→ Toy guns	Ex:	→ Video game
→ Considers Preferences		→ Considers only no.

Considers only volume - not value added

the findings of other Indices like Index of Industrial Production [Audi alto ex]

ii) The impact of Indirect tax should be studied to understand its significance in affecting growth rate.

Ex Case

		N.I.T	GDP@MP
2013-14 GDP_{FC}	→ Rs.100	10%	110
2014-15 GDP_{FC}	→ Rs.100	15%	115

iii) The choice of GDP deflator is not correctly done in India. ∴ It should be improved to calculate better values of real GDP. [In India steel, iron ore etc. are given weightage more instead of very essential consumer goods]

$\boxed{\text{GDP deflator}}$ is Price Index used to convert Nominal GDP into Real GDP. $\boxed{\frac{\text{GDP (Nom)}}{\text{GDP deflator}} \times 100 = \text{GDP (Real)}}$

Prof. B. N. Goldhar committee [2016-17] to improve GDP deflator in India.

INCLUSIVE GROWTH (Growth Vs Development Debate)
Quantitative / Qualitative

INCLUSIVE GROWTH

(Growth Vs Development Debate)

Growth / Dev^t was not talked about much earlier. why?

Peasants in Feudalism became workers in Capitalism. this change was not resisted much bcos the standard of living got better gradually. so, the existence of capitalists was not threatened.

Ex: A husband-wife – 3500 Rs. Village $\xrightarrow[\text{to}]{\text{goes}}$ URBAN Area – 2500 Rs.

Advantages:

- Identity-free in Urban areas whereas in village there were many restriction. same happened in 18th cen Europe
- New commodities.
- ↑ Income though exp. in urban is more
- though Exploitation was there, due to standard of Living was increasing, its impact was not felt then.

But after 1930s – Existential crisis for capitalists

i) Great depression of 1928 (Recession + Deflation)
↳ 1st time standard of living fell in capitalist world

ii) Growth of Soviet Union – 5.3% growth
↳ opposite to Capitalism; beginning of Socialism – Looked good at beginning – Stalin's atrocities not known then

Development needs PEACEFUL LIVING.

Never justify VIOLENCE – Hypocracy of Communists: supports violence for revolution but criticise Rightists/Terrorists for the same.

People play on VANITY (we always believe we are better & we give more)

Ex:- Globalisation/outsiders are the problems solely.

- politicians are responsible for all problems, not us?

whatever is new & what gives results – ppl catch upon it

that is why initially socialism in USSR was supported.

↳ ppl from Germany, France, Belgium, etc.. were migrating to USSR

2 Notions

Welfare state

Growth ⟶ Trickle down Effect

"Growth only for the sake of it is like Cancer Cell."

Growth is not important by itself but what we do with growth is what it matters.

Ex: when more patients pay doctor – GDP increases. Is it growth? Does ppl become better off?

—Growth of GDP is Necessary but not Sufficient—

GROWTH:

i) It is a quantitative concept, which consists of additions in flow variables to add to accumulation of stock variables.

Flow Variables

→ Measured over a period of time

Ex: GDP, Savings, Investment

→ Can't be defined without a time period - connect.

Ex: Income - 2000 per ——.

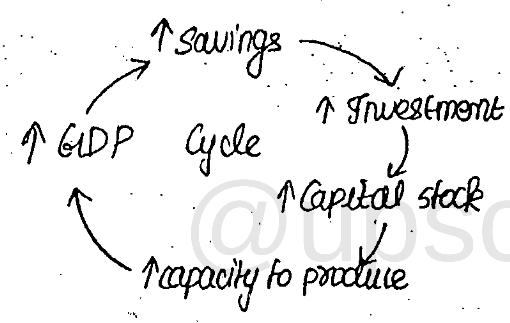
→ As flow variables evolve they keep adding stock variables.

Stock variables

→ Measured at a point of Time

Ex: Population
Capital stock
Wealth of a person

→ No importance for time period connect.



Note 1: Don't give importance much to quarter GDP growth. Don't bother about monthly data & unnecessary analysis of newspaper. MAGNIFICATION of either achievements or lags - both are very bad.

Note 2: Till the upper middle class doesnot have sleepless nights poverty in India will remain.
The powerful must be conscious of powerless for Inclusive growth
Development is about RESPONSIBLE RICH.

NSS 2018 — 81% Literacy rate - 250 mn still illiterate

Inclusive growth is not about SYMBOLISMS as practised in India. Ex: Pro-poor; Pro-Dalit- They say but not working on ground.

IN LAST 1½ YEARS
NPA → Increasing
GDP → Increasing
NPAs has not slowed down GDP.

GROWTH

i) It consists of Increased URBANISATION & COMMERCIALISATION which can improve standard of living for ALL.

DEVELOPMENT / INCLUSIVE GROWTH

i) It is a QUALITATIVE concept which consists of GDP growth in a manner that it includes Benefit of All in the economic system.

ii) Main features:

a) Equitable distribution.

Equity: ppl have equal opportunity, Freedom to make choices } ppl don't envy each other

b) Poverty Alleviation

Direct attack on poverty: 330 mn ppl BPL.

c) Sustainable Development

Environmental protection + Growth of GDP
Only when GDP growth is based on Greed & wastage it is harmful - if preservation; conservation is there ok.
Excess exploitation must go

d) Capability Enhancement - AMARTYA SEN

Income can be one source but not the only source of capability

Till 1750 – 1st IR

pop. was not even 1Bn in world.

By 1880 – 2nd IR

we touched 2 Bn

By 1947 –

we touched 3 Bn

By 2018

we touched 7 Bn.

By 1847

89% of America was Agro-Based

No TV; No assembly line manuf. of car.

In such rapid development – even with best of intentions

we couldn't have much – But our intentions too was not best of.

In Mechanical virtues' praise – PUNCTUAL, skill, AI –

we have forgotten Humanity (Emotional Intelligence)

· HUMANITY STUDY (literature, Art) – are important for humanity

less importance for it has made many HUMANOIDS.

Machines are only worried of instant results;

Humans can see future prospects – EQ.

Ex: Instead of INSULT prone society, we can discourage

the –ves & Become TRUST based society.

Example of upper middle class women

✓ Majority of them are capable - drive car, work, etc.

But still they ask permission from husbands rather than informing them.

✓ They've been conditioned in our social system even as per this - Gender stereotyping by women too

→ Any STEREOTYPING is CAPABILITY DEPRIVATION.

The need is to EMPOWER → To develop EQUITY → CAPABILITY Enhancement

POLICIES TO ACHIEVE INCLUSIVE GROWTH

i] $\boxed{\text{Developing a physical structure:}}$

⇒ Development of physical infrastructure like ROADS, RAILWAYS helps in improving CONNECTIVITY which can open new opportunities for people in deprived sections.

⇒ Similarly, Improved ELECTRIFICATION can help in increasing WORKING HOURS, reducing work load by making MECHANISATION possible, Creating new EMPLOYMENT opportunities through new Businesses and uplifting STAND. OF. LIVING

GUJARAT Report-2016

Milk production doubled due to 24x7 electricity

This ↑ Cold storage

↑ Mobilisation

KERALA Report-2016

Fishery producty ↑ 38% from 2011-14 due to Mobile phones.

'DEMONSTRATION EFFECT'

Till we are DEFENSIVE of poverty, we can't cure.

⇒ Development of **COMMUNICATION** increases flow of Information & makes it possible to increase the PRODUCTION CAPACITY & improve the STABILITY OF INCOME for people in lower income group. It also means faster movement of Information which promotes BETTER DECISION MAKING.

⇒ Developing **CIVIC AMENITIES** like
- ✓ Clean water supply
- ✓ Drainage Facilities
- ✓ Public Transportation etc..

will help in reducing COST OF LIVING for the poors which will help in Increasing their DISPOSABLE INCOME (in hand) and improving LIVING STANDARD.

⇒ **FINANCIAL INCLUSION** will enable the poors to achieve SELF SUSTAINABILITY by participating in the monetary system. It consists of ▷ BANKING Inclusion (i.e) Accessibility to Bank account for all.

▷ CREDIT Inclusion (i.e) provision of cheaper loans via formal institutions like Micro-credit Institutions; SHGs; Small Finance Banks; etc.

How Indian rich act like POOR?

1) Airport - Bus - Fight to get in - hurry
- Needlessly in hurry as if there is scarcity of resources.
- They are surrounded by poverty so they are in constant fear of resources.

2) Movie theatre entry.

Can we even imagine such ppl to share their wealth with poor?

We need to
- ✓ INSTITUTIONALISE INCLUSION
- ✓ Only then DISTRIBUTION can have.

→ Educating the poor is not charity - but IMPERATIVE.
- Social disruptions where some feel they are deprived is very bad for all
- 'MIDDLE INCOME TRAP'

Ex: Latin America
- SOUTH KOREA
  - Good inclusive growth

▷ INSURANCE Inclusion (i.e) availability of Insurance support for people in deprived section. this will help them in taking CALCULATED RISKS so that they can achieve Higher standard of Living.

ii] HUMAN DEVELOPMENT

a] Education:

→ It increases efficiency & therefore earning opportunities.

→ It increases Adaptability to new changes in Technology.

→ It improves Analytical capabilities which helps in increasing choices.

→ It increases Information set developing Better opportunities.

72% ppl in India
↓ per capita Income

LAND PASS BOOK SYSTEM
In Telangana.

ASSET INEQUALITY >
INCOME INEQUALITY

INHERITANCE
exists INFUNITIVELY

ABSENTEE Landlordism
Misused to evade Tax.

Steps taken by Govt. to promote Inclusive Education

▷ Govt. has Initiated TOTAL LITERACY MISSION (SSA) to promote UNIVERSAL Education

▷ Govt. has implemented RASHTRIYA Madhyamik Shiksha Abhiyaan Rashtriya Uchhatar Shiksha Abhiyaan to promote SECONDARY & HIGHER SECONDARY education.

▷ Govt. has set up Min. of Skill Development to implement programs like PMKVY (PM's SKILL DEV^t PROGRAM) to provide Employment oriented skills to youth.

▷ Govt. facilitates publishing of Annual Status of Education Report (ASER) by PRATHAM (NGO) which is a qualitative evaluation of education in India.

Further steps that can be Taken

* Improving INFRASTRUCTURE & ACCESSIBILITY to school.
  - ASER → 24% schools in rural India – No roof
  - 31% – multiple classes in same room
  - 17% – No drinking water
  - LALU PRASAD's suggestion → CHARWAHA VIDYALAYA
    Bring school to children – He got UNESCO award.

* Reducing Teachers' ABSENTEISM & providing SUPPORT to children AFTER SCHOOL.
  ↳ the ABC story

* Developing coordination b/wn ACADEMICS & INDUSTRY.
  ↳ The poor kids will be aware of the job & this gives incentive for them to learn.
  ↳ It creates 'DEMONSTRATION EFFECT'

* From TSR SUBRAMANIAN Committee Report
  To develop a dedicated CADRE OF TEACHERS to support Teachers
  ↳ Education can act as asset for assetless people

INCLUSIVE HEALTH CARE

WHO: 4 Criterias for Inclusive Health Care

I. Accessibility to Nutrition

II. Accessibility to Clean water

III. Accessibility to Sanitation

IV. Availability of Trained Medical Professionals.

Post 2001 [Millenium Development Goals set up]

Steps taken by Govt. for Inclusive Health Care

i] Govt. has implemented National Health Mission since 2013 for UNIVERSAL HEALTH CARE.

[NRHM + NUHM — Merged in 2013 to create NHM.
Objective: Accountability, overcome Overlap in Jurisdiction]

ii] Govt. has appointed ASHA [Accredited Social Health Activists] to provide PRE-NATAL & POST-NATAL Care to pregnant & lactating women.

[Purpose: Nutrition at right time for women;
care for children to prevent IMR (21) – 39/1000 – not uniformly distributed [Dualistic Economy].

For ex: Drinking water → High/middle class – not fatal
– not dehumanising

Why no action? → Low class – ill – work loss – poverty

No FUNDS (?) But for AIR INDIA, Space program – Funds.

Human in Space – Ego – not necessary.

Latest data

NSSO – If 14 L/annum for family – top 1% in India [1.35 B]
half of Australia

Even decent income ppl calling themself Middle class.

May be socially middle class but not Eco. middle class.

Middle class – ₹9,000/month [50th percentile] – 72% don't earn even this much.

GREEK CRISIS – Mother pension – 5 ppl surviving.

Incentivising young ppl not to work.

His concern – no chocolate twice a week.

Per capita – 2.6 trillion shared by 130+ crore

Do TV debates concern Poor people?

Rafale deal, Sabarimala, 377 – Poor are not even informed of these due to illiteracy & poverty

Vs

Primary school, sanitation, health care

Hunger Index:

NUTRITION – i) Information deprived [over feeding – obesity]

– ii) child stunting

begins in womb if mom no nutrition.

Mom at very young age – & we are accepting it.

– Everything is not economy –

– iii) Child Wasting

Vaccination at child birth (ex: Polio) crucial

Many in rural don't bother.

– iv) Child Mortality (<5 yr die /1000)

Even if we grow more fruits or prevent fruit wastage, these ppl won't get access.

LOUIS XIV – Y don't ppl eat pastries if not bread.

Even open defecation leads to lack of child Nutrition
We need, Structural Establishment - functional
Disease Identification
Inform ppl

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iii] Govt. has implemented Mission INDRADHANUSH for Vaccination against 12 diseases [on 25th Dec, 2014 (7 diseases then).

iv] Govt. has implemented Clean India Mission to make India OPEN DEFFECATION FREE BY OCT, 2019 [2nd Oct, 2014 start]

9mn toilets – needed – must be made functional / utilised by ppl.

Identify y not used? ○ Water ↓
○ Poorly constructed pits
○ Behavioural (habit) — Info. campaign on problem of open defecation (5-6 yrs)
Ex: Educated ppl – not washing hand bfr eating. Food on time but unhygienic.

We've been talking on it for long but not acting enough.

v] Govt. has initiated National Health Protection Policy [PMJAY] with dual intention of providing INSURANCE & HEALTH CARE to people.

Don't read only criticisms
Mostly they are Notional criticism,
Highschool debate - 1st 5 lines should destroy opposition
But it is not useful in policy debates — making even debate futile
— Digital India — Videos, y not apps.
Bharat net must precede Digitization.

Health Index – India worst

Dev.^d countries as they grew moved from
Poor man's disease ⟶ Rich man's disease
Fight on one Front.
But, India – we have both – Fight on 2 Fronts.
Problem: More curative than preventive.

Cond / use: Focus on prevention & save cost. How?

Vaccination
Nutrition
Dr. water
cleaner air.

i) Spread Info at right time.
(children smoking, women smoking – Taxes not enough.)
Campaigns by heroes very ⊕ instead of moral lectures.
Has to imprint in their minds

ii) Supply side provision of Trained medical professionals.
a) Increase no. of training facilities/centres.
b) Bringing dynamism in nursing as a career
Not much career growth now. In Europe – Bridge course after 15 yrs & allowed some medical practice – legally – happening now. In India illegally however.
will attract lower middle class

Dr. KALAM

c) Providing Urban amenities in Rural Areas [PURA]
To encourage rural shift for docs. to work.
Money is not the only factor – system frustrates ppl with even noble intentions.
Rural posting – punishment – X Civic Amenities.

Concl. use } Improve expenditure on Health Care.

Qualitative [Increase - part of it but not complete.

Result oriented.

1.2% of GDP - present UG expenditure since 2010-11.

2010-11 ⇒ 2018 - Doubled GDP - so 2.5% of 2011 GDP
$1.3 tr $2.6 tr
is now 1.2% of 2018 GDP.

Large question? 2.2 trillion rupees is achieving what?

Improve on it — • Accountability
→ This will make • Social auditing
corruption difficult • Technology - basic apps for ppl
↓ instances of it ←

Once you ensure it reaches ppl, then make it 2.5%.

Concl use. } Inclusive growth becomes more possible by making Rich responsible for basic amenities to poor.

Institution Building [Inclusive] is key.

Empowerment, not charity, is required.

Security doesn't come by dependence.

HDI [Human Development Index]

UNICEF statistics

Published by : UNDP [United Nations Dev. Program) under HDR [Human Development Report]

Since : 1990

Credit : Prof. Mehboob-ul-Haq, – chairperson – Pakistan
Prof. Amartya Sen – Member } India
INGY KAUL – Member }

CRITERIA

(1) HEALTH:

Parameter: LIFE EXPECTENCY [LE]

Method: $\text{Health} = \dfrac{\text{Life exp. of given country} - 20\text{ yrs}}{\text{L.E of country with highest LE} - 20\text{ yrs}}$

LE : The no. of yrs a child on an average would expect to live during birth.

Y 20 yrs : Min. 20 yrs to survive – Historical
those societies < 20 yrs LE can't survive.

Relative term btwn 0 & 1.

Criticism: Only survival, Quality of life not concerned here

(2) EDUCATION :

2 Sub parameters :

a) Mean years of schooling for adults (A > 25 yrs)
(MYS)

b) Expected years of schooling for child entering school.
(EYS)

Method :

a) $$\frac{\text{MYS for Adults in given country} - 0 \text{ years}}{\text{MYS for Adults in country with highest MYS} - 0 \text{ years}}$$

0yrs : symbolic. Worst one can do to human is not educate them.

b) $$\frac{\text{EYS for C in given country} - 0 \text{ yrs}}{\text{EYS for C in country with highest EYS} - 0 \text{yrs}}$$

Y special? Also reflect diff. in depth of education & quality (hoco literate pplace) unlike Literacy rate.

EYS – not only enrolling; but also possibility for C to drop out later.

$$\text{Education} = \frac{a+b}{2} = \text{Avg of MYS \& EYS}$$

③ SOL [Standard of living]

Source
UNDESA - Health data
UNICEF - Edu data.

In terms of: ($ GNI/capita) @ PPP level.

Why PPP & not MER? Cost of living is different in diff countries. \$1 lakh <-/-> ₹. 72 lakh
\$1 lakh <--> ₹. 25 lakh.

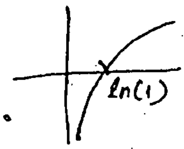
$$\frac{\log_e(\$GNI/capita) \text{ of given country} - \log_e(\$100)}{\log_e(\$75{,}000) - \log_e(\$100)}$$

Y 100\$ → Min. needed for survival [2009-10].

Y \$75,000 → Once eco. starts earning more than this per capita, income doesnot affect S.O.L.

(i.e) Further growth of income has no affect on SOL.

Y $\log_e$ → Increasing at a decreasing rate
Every successive increase will be less that the previous increase.
'Law of Diminishing Marginal Utility'.



⇒ HDI is calculated by taking Geometric mean of
✓ Health
✓ Education
✓ S.O.L

$$HDI = \sqrt[3]{H \times E \times SOL}$$

Y not $\frac{H * E * SOL}{3}$ = Each parameter is dependent on other.
Arith. mean?

HDI Categories Countries

0.8 – 1	–	Very highly developed
0.7 – 0.79	–	Highly developed
0.55 – 0.69	–	Medium developed
0 – 0.54	–	Less developed.

Recent HDReport, 2018 on 188 countries

	2016	2017	2018	
India –	130	131	130	Rank
		0.628	0.64	Score

Rise due to – SOL & Health only.

Education is stagnant for 6 yrs.

In SOUTH ASIA (SAARC) – SL > Maldives > India (3rd) > Bhu > Bang > Nepal > Pakistan > Afghanistan

In BRICS – We are last rank.

Top 3 (2017, 18) – Norway > Australia > Switzerland

For 7 yrs from 2011.

Y Scandinavia does well? Value to human dignity. Separate room to children, even frock.

All Indices: Cultural beliefs too play a role. So may not be matching all alike.

' You should not judge women by the type of cloth they wear.'

— Then y judge those with traditional clothes as old?

→ French - Modern; Sanskrit - Old ?

Community beliefs → Disturb HDI

'Prejudices' → Harm HDI, Happiness index.

→ We no need to qualify ourselves with standards of west.

Criticisms: i) Doesn't penalise ~~any~~ inequality.

so, from 2011- UNDP also publishes

"INEQUALITY ADJUSTED HDI" IA-HDI

"Countries are penalised by reducing their score for presence for inequality"

2018 - 26.8% lost by India for inequality

0.46 Vs 0.64.

ii) Doesn't consider Women inequality

In 1995, HD report started publishing "GENDER DEVELOPMENT INDEX" GDI

"Ratio of HDI of females to HDI of males in that country"

CRITICISM: Tilted towards rich countries.

From 2011, UNDP publishes "GII [Gender Inequality Index]"

GII consists of :

① Maternal Health Care

a) MMR (die / 1 lakh children born)

b) AFR – Adolscent Fertility Rate

On an average, how many children a woman has when she is between 15 & 19.

② Empowerment

a) % of women in Parliament

b) % of women in Higher Education (ppl > 12^{th} std)

③ Labour Force Participation Rate of Women [in Paid Work]

India : 24%

SHYAM Sir

* Multidimensional Poverty Index by UNDP.
* Hunger index by IFPRI

GROSS NATIONAL HAPPINESS INDEX

Published by: UNFSS - UN Framework on Sustainable Solutions

Under: GHR - Global Happiness Report

Since: 2012

Credited to: King Wangchuk of Bhutan

6 Criteria:

1. GDP per capita
2. Healthy Life Expectancy
3. Social Support
4. Freedom to make life choices
5. Freedom from Corruption
6. Trust & Generosity

We are Community-living people. Our sense of privacy is very different & also our sense of what is freedom & happiness is different from west Nuclear-Living.

Debate: ◦ Y some democracies at lower than non-dem.?

INDIA – 133/154
Pak – 76/154
China – 92/154
Nepal – 101/154

Cultural ethos - different
Intercept points - different
! where u start also decides.

Ex: Pak – feel freedom even that election happ.
Ind – worried of 73rd CAA.

– Work/ target Human development & the Index will take care of itself. –

Note: We rejected HUMAN CAPITAL REPORT

1) productivity less? Status survey for taking up jobs

INDIA IN PLANNING PERIOD

1951-65	1966-80	1980-90	1991 Onwards
Nehruvian period	Structural Retrogression	Period of Revival	Eco. crisis + Eco. Reforms

Centralised planning

1951-56 → 1st FYP

1956-61 → 2nd FYP

1961-66 → 3rd FYP

1966-69 → Plan Holiday

1969-74 → 4th FYP

1974-77 → 5th FYP

1977-79 → Rolling plan

1980-85 → 6th FYP

1985-90 → 7th FYP

Indicative planning

1992-97 → 8th FYP

1997-02 → 9th FYP

2002-07 → 10th FYP

2007-12 → 11th FYP

2012-17 → 12th FYP

2015 – PC abolished.

Our Inheritence from British made it Imperative to go for Socialist Model:

From, British – Poorly inherited.

Structure of Economy – Backward

53% GDP from Agriculture

73% workforce in Agriculture (age: 15-59)

85% population dependent on Agriculture.

Agriculture

Poor productivity – still import of grains happened

Capacity to produce – V low?

* 17% only under irrigation (of total cul area)

① Technology – Equipments

② Irrigation insufficient, non-uniform.

③ Market absence – Institutions lack [Subsistence farming]

④ Land distribution was regressive

17% GDP from Industries

Cotton Textile, Jute, Sugar

Iron & Steel – Only dom. capital goods industry

In 1950s – modern industries chemical industries

But chem. indus in India was < 2%

~~Very less~~ Heavy Industries, Infrastructure – Absent

2300 MW – Total elect then

71,000 MW – Now, Delhi alone

1991 → USSR split

World wrongly took USSR's failure to be US's success in economy.

New Rules made based on this wrong underst → ↓ Tax, Opening up, Pvt. investment, ↓ Control → Washington Consensus

In true sense, all countries can't have same rules – diff. set of systems req. diff. strategy.

R. C. Guha → 'Bam Times Now' – Hypocrisy of a liberal.

Voltaire → 'I will disagree with you but I will protect your right to speak'

Conditioning of feudalistic society : 'Power rules'

Conformist society : Don't question past.
Then how will we evolve?

The policy of liberalisation has been implemented by:

a) Removal of licensing

Govt. removed licensing requirement on all, except 18 industries, in 1991 and further reduced it to 5 - those 5 are:

i) Alcohol

ii) Cigarettes - selectively only for filtered cig & not beedi
Most beedi org. are owned by MLAs.

iii) Hazardous chemicals & Pharmaceuticals

iv) Electronic Aerospace

v) Industrial Explosives / Defence Ordinance.

The policy of licensing has been replaced by a system of permissions under set rules and regulations.

Manipulation of this

1st come 1st serve but I choose who comes 1st

I make rules hard for late entries.

psychophant

Crony capitalism grew →

License raj was replaced by Inspector Raj

It is about the system & not whether Pvt. or Public.

If sys

Chrony Socialism → Govt. controls common resources and gives rights to mining etc.. to selective ppl.

→ This is creating stigmatised Capitalism (ESI)

⇒ We need systemic checks instead ~~to~~ of selective opp-of events.

b) Removing Reservation for Exclusive investment of public sector

The no. of industries exclusively reserved for public sector was reduced from 17 to 8 in 1991 and it has been further reduced to 3. These 3 are:

i) Atomic minerals
ii) Nuclear Energy
iii) Railways

This has been done to promote competition in the market which will encourage
- quality improvement
- cost cutting
- Higher supply of commodities (↑ provisioning)
- Better facilities to the consumer.

c) Remove restrictive legislations to encourage investment

MRTP was removed & replaced by Competition Act, 2002 under which Competition Commission of India was established in 2009. It has 2 advantages over MRTP Commission:

It doesnot discourage expansion of a firm by restructing investment. It targets unfair trade practice instead.

It has an inbuilt Tribunal where all its orders can be appealed which saves the time on Dispute Resolution.

FEMA (Foreign Exchange Management Act) has been introduced to replace FERA (Foreign Exchange Regulation Act) from 1999.

It allows:

i) Foreign investors to bring any amount of foreign investment in India if they have 100% subsidiary

ii) Indian firms have been permitted ECBs including borrowing by Masala bonds → Typically issued in terms of Forex & paid back in domestic currency terms. There are 2 advantages:

- No forex risk for the borrower.
- Inflow of forex into the economy

The company needs to list itself in foreign stock market before issuing masala bond. In case of India - both ICICI & YES Bank which issued masala bonds in 2016 & 17' were listed on London SE on recommendation of IFC ["Intn'l Finance Corp."], a WB body. (Now NHAI is also issuing MBs).

MRTP → CCI - 11 yrs
GST
2005 → 2016 - 11 yrs
FERA → FEMA - 7 yrs
Walmart ← Flipkart
Govt gain: 7200 Cr.

Exporters are not restricted from keeping their earnings abroad. [After 1994: India shifted from Fixed → Fl. ER]

Individuals are allowed to carry upto $2,50,000 while travelling abroad [1999: $10,000 ; Now: $2,50,000]
[FERA: $500 – $2000]

d) The govt. removed controls on price & output for several industries like – I & steel, Cement, Aluminium, etc.

$\underbrace{\text{I \& steel}}_{\text{6 mn tons to} \sim\text{80 mnt: 2018}}$, $\underbrace{\text{Cement}}_{\text{28 mn tons to 268 mnt: 2018}}$

CCI & FEMA	Vs	MRTP & FERA
Treat ppl as bonafide		Prev. laws treated ppl as Malafide
Encouraged reporting		Penalised for mistake

e) The govt. has made taxation relatively more rational in India.

Inherent Trust deficit b/w Govt & Business people.

What is a Liberal Policy?

– Make participation easier by simplification of Rules –

PUBLIC SECTOR REFORMS

- PSU → PSE + other firms under diff. Acts
  PSE → Firms under Companies Act specifically
  CPSE → PSE by UG – 293 nos now
  SPSE → PSE by SG – 974 nos now

Problems
Populistic Employment Vs Productive Employment
Not enough cost control.

I] Providing autonomy to public sector

In 1992: Govt. introduced a system of MoU to be signed between public sector & concerned ministry. It contained all details w.r.t. Targeted profit, price charged, quality of output, etc. Once MoU is signed, the Ministry is expected to maintain all operational distance from it.

Problem: Delays in permission reg. App, Inv, new posts
1997: P.Chidambaram – Navaratna
2010: Maharatnas ...

From 2010-11, Govt had provided autonomy to public sector firms classifying them into 3 categories on performance:
MAHARATNA

93% Women illiterate (7% LR) } Cascading impact
84% Population illiterate (16% LR) }

IMR = 400/1000 $\xrightarrow[\text{to}]{\text{led}}$ Population explosion due to hoarding of children.

Reasons for adopting Socialist model of Growth after Independence:

i) Govt. had majority of resources (for aid) which could be used for eco. devt. & social welfare

ii) Absence of market due to SUBSISTENCE nature of Economy.

85-90% Indian ppl - Subsistence living.

Threat of monopoly due to very few willing pvt-sector ppl.

iii) Absence of Basic & Key Industries which have Long Gestation Period. [Initiation ⟶ Earning profit].

iv) Large scale poverty and poor human development required Active participation by the Govt.

v) Success of Soviet Union in economic development.

Then ppl didn't know about Stalin's acts.

But, leaders - Socialistic; Society - Feudalistic

The leadership we inherited was automatically inclined towards Socialism.

But the mistake they did was they thought their followers would be the same. Hence poor checks & Balances in our system still.

Five Year Plans

1951-66 : Nehruvian Period

Ist FYP [1951-56]

→ It was more a plan of Intent than actual Growth plan (mainly abt what ? & less abt How?)

→ It was based on Harrod-Domar model, which focussed on GROWTH on basis of SAVING & INVESTMENT.

→ The plan was mainly focussed towards AGRICULTURAL DEVELOPMENT based on institutional reforms like LAND REFORMS [zamindari, Tenancy prot, Ceiling] & through Technical support in fields like IRRIGATION with development of LARGE DAMS.

→ It also focussed on INDUSTRIAL DIVERSIFICATION [only 13,14 products before it]

→ Introducing RENEWED INVESTMENT in Sectors like:

- Heavy Engineering
- Heavy Electricals
- Infrastructure, etc.

} Large Industries

(Ch-4 & 5 - Health & Education - will automatically improve when resources start accumulating. ↓ Import ↑ Save & then spend on Social - H&E - so not intentional but this was the thought process - trying to make balance -

sometimes disrupted - when demanding classes are favoured more than those of ordinary ppl's demands - then we also love quantities, nos. rather than Qualitative focus -

Ex: ONGC - 2014-18 - 178 new exploration fields - But production: 26 mnt to 22.5 mnt. - we love quantities, not quality.

Ex: Illiteracy Vs literacy ⇒ Functional literacy Vs Just literacy

Also Edu & H, are long-term, slow changes & are not easily notable in ppl's eyes as they are gradual - SOFT INFRASTRUCTURE was dull but HARD INFRASTRUCTURE improved)

→ The plan targetted a growth of 2.1% ;
The plan achieved a growth of 4.6%
(Investment ↑ + Govt. Exp ↑ + Consump. exp ↑ But Exports ↓ ; + foreign aid ↑. Also world was trying to woo us towards US or USSR (bfr NAM) by more loans from World banks. But when NAM came in 1966, it was seen pro-socialist & Anti-US, foreign aid slowed yet WB still gave us)

→ This was the 1st properly designed plan based on MAHALANOBIS MODEL with following features:

> Development based on LARGE SCALE INDUSTRIES, Focussing on BASIC & KEY Industries
- o Infrastructure
- o Heavy Engineering etc.

> Industrial development to take place under the PUBLIC SECTOR CONTROL. Public sector was given the status of commanding heights for following reasons:

a) Price control
b) More equitable distribution
c) Balanced Regional Growth
d) Efficient use of Resource with higher Employment Generation.
e) Re-investment of profit for Welfare of the people.

→ It is ok that public sector must not be judged on profit but must be held accountable, as it is on public money, on other objectives

→ Do they actually serve the intended purpose

AIR INDIA Vs Kingfisher ; PSBs Vs Pvt. Banks ;
[11/19-PCA]
(570 Cr/yr Govt pills) → not serving poor; capital intensive so ↓ Employment

Revive or Dilute based on context & timeframe.
↑ case-by-case basis – relevance now

> IMPORT SUBSTITUTING INDUSTRIALISATION was introduced as an important aspect.

> LICENSING was introduced for private sector as an Entry Barrier [to prevent over production of one / few commodities – Govt will predict demand & then give license – But no proper prediction mechanism – later misused]

> 17 INDUSTRIES RESERVED exclusively for public sector. Heavy investment.

1951-65' → Good leadership to run this

Post-65' → Name sake socialists – Hypocrites.

Late realisation of need for balances & check btwn Pub & Pvt.

* Planned growth rate : 4.5% pa
  Achieved growth rate : 4.2% pa,
  with Industrial growth > 8% pa

Indian plans lack dynamism – world changes & we too need to change. Shortage of consumer goods was not expected & problem came in 3rd FYP. Wars, Death of 3 PMs, lack of good leadership (Syndicate – I. Gandhi)

1967 – friction started ⇒ 69' – completely disruption; 66'-69' – Behind scene power games – Rhetorics – Eco. policy also got affected.

RBI Vs Govt → Common in most countries;

Subbarao Vs Chidambaram; MMS Vs Rajiv Gandhi (85'-86')

Pol. parties → Try POSITIONING SOMETHING else – Pro Poor!...

↓

Rationality takes a toll.

post 65-66' → more rhetoric, less substance.

Present gen → taking extremities, missing nuances.

X Nuancical debate } real issues go for hide, fight remains

PATEL statue → World will look up to us, but inside or behind will laugh at 250 mn illiterates.

Like in 1991 — Good for nothing;

Own social contradictions → will put us down & not external forces.

POLLUTION → not even an election issue; 3 yrs - nothing done.

↓ (Delhi)

Unequal Growth → Co-existence of rich & poor

Post 65' → Talked inclusion but didn't do — Bulwark Corruption

1978-79 → started poverty alleviation

till 2018 → 47L33Cr : still not much difference

Huge than 1.5 lakh to each poor.

Fodder Scam (LALU) ⇒ Buffaloes on scooty (360 km ? ☺)

Haryana ⇒ Well – mosquito – Again well – cycle went on.

Dig close Dig close

IAS officer found out that no well was dug up.

IIIrd FYP [1961-66]

* Targeted growth : 5%
  Actual growth : < 3.5%
  Industrial growth : remained @ 8%.

→ The plan couldn't achieve most of its targets & at the end of this period, 2 MAJOR issues afflicting India still remained (i.e) :

a) Lack of Food sufficiency
b) Continuous increase in poverty

The govt. declared a PLAN HOLIDAY [1966-69] & 4th FYP was brought from 1969-1974.

IVth FYP [1969-74]

Focus of plan was on:

Equal allocation of resources
Poverty alleviation via Direct attack on poverty
Growth in Rural development

Similar was followed in 5th FYP [74'-77']

* Growth rate btwn 1966-80 : ↓ to 3.3%.

Per capita even < 1%.

'HINDU RATE OF GROWTH' – Social rigidities, multiple identities – state, lang, caste, surname } Nation ?

Building states – disgracing country –

'when eyes bleed, hand doesn't laugh'.

15th FC TOR – south India pop control.

I earn, y should I give you? – think of it to at other levels ⇒ State → Districts → Villages → Family (!)

"Developed systems think Developed & become developed; Underdeveloped systems think underdeveloped & remain so"

I. Gandhi – not a grassroot leader – forced positioning 'Pro Poor' – symbolisms artificial, not natural –

Post 1965 → Rules became stringent

- Licensing – also to close & expand – misused via Nexus.

  Ex: 1969 – Public Sector loans – siphoned – mismanagement – Bankrupt – BIFR – to check on it – 6 to 7 yrs – Company taken over by govt – BANKRUPTCY BUSINESS (creditors, employees suffer)

  Ex: Kingfisher – No I&B code till 2013 even.

- 400% import substitution on Gold – Smuggling nexus.

  1984 ALAGH Committee revealed it.

Micromanaging ppl is not effective

I Gandhi & Modi → Polarising force – extremes.

Recently: Railway corruption – Bill – (see) – not in headlines (!)

· 97.5% tax on income of >10 lakh → Tax avoidance, Bribe
Avg. tax rate - 82% ; Cascading taxes
MRTP act, FER act → restriction on investment, forex - ↓ competitive.
I & Steel, Al, Cement ⇒ Govt. fixes price, quantity, quality
'ILLIBERAL SYSTEM' ⇒ Ex: Compulsory attendance in college
↳ Bad rules — incentives to corruption — Bad result
Good rules — admin cost of catching breachers ↓ — less in no.
80s, 90s → Decade of upliftment of many countries Heal
1978 → Chinese per capita < India ; 2018 → 4x India
But china bounced due to good Implementation
NINZ : Just announcement

* Industrial growth fell <5%
Percapita income grew @ <1% pa
This was due to:

a) Making LICENSING very stringent where it was required not only to enter market but also to expand Production & even to close the firm.

It reduced competition & discouraged costcutting and innovation.

b) Political Interference increased in public sector which compromised their performance by restricting investment, Overstaffing, Restricting sources of raw material, etc.

c) PROTECTIONISM increased with increased restrictions on imports and large increase in import duty on several commodities.

This further discouraged Competition & Efficiency.

d) Restrictive legislations like MONOPOLISTIC & RESTRICTIVE TRADE PRACTICES Act [MRTP Act, 1969] → discouraged investment.

under this act, govt identified firms as National Monopoly [for investments > 20 Cr] & Product Monopoly [for > 3 cr] & [Control over 25% of market]

Both these categories of firms couldnot make any further investment w/o permission of MRTP Commission, 1970. (Discouraged from getting 'Economies of Scale' - adv. from large scale production)

IIedU

[FER Act, 1973] FOREX REGULATION ACT → restricted inflow of foreign investment in India, prevented comp.s in India from borrowing abroad, prevented exporters from keeping their earnings in forex beyond 3 months

then we were having fixed FER : more value when out

cat & mouse game — making honest ppl dishonest —

Need Simplified Rules

'TRUST & VERIFY' Method → Self Attestation

Govt introduced IRRATIONAL TAXATION STRUCTURE which encouraged Tax evasion and Tax avoidance.

Growth rate in 1979-80 fell to : -3.5%

The 6th FYP [80'-85'] was designed to bring Comparatively FLEXIBLE POLICIES to promote Economic Growth.

Avg growth rate in 6th FYP : 5.8% p.a

In 7th FYP, Avg growth rate : 6.8% p.a

Highest decadal growth since Independence ; REVIVAL;

Industrial growth rate : 8% pa

Growth was due to Borrowed money ; Hence, 1991 crisis

Reasons for Revival of Growth:

① BUSINESS FRIENDLY Policies of govt under which:

Restrictions under MRTP (20cr-100cr) & FERA (500-5000$) was relaxed

Restrictions on IMPORTS were relaxed which made raw materials easily available

Taxation system was RATIONALISED

Business friendly - existing business flourish but no new comp-
Not, Competition friendly - no new entry of competition.

② Productivity of workers improved with better training.

③ Spread of GREEN REVOLUTION;
YELLOW REVOLUTION;
WHITE REVOLUTION
across rural areas encouraged demand for Industrial commodities which promoted growth.

Marketing Revolution — Sachets — 1st by India

④ Large Borrowings by Govt. for expansion of PUBLIC ADMIN.ⁿ also contributed to GDP growth.

WB, IMF, OECD countries
Quantify of fiscal deficit, etc.. not a matter but
Qualitative improvement has to be seen
↑ Fiscal deficit → Inflation (↑ money printed): 2011-11% inflation

1991 BOP crisis:

- Not only due to BOP, Gulf war
- ✓ weak macro-economic structure - Structural Crisis
  - → fiscal deficit, CAD, Inflation   short term fore. loans = 145% of Forex

1991 Reforms:

why?
- Not only due to IMF pressure. But also willing pollical in Rao.
- RAO took it an opportunity (IMF) to bring reforms which otherwise wouldn't have been possible
- i) → 2000 - paid back all loans; 2003 - FRBM; 1999 - FEMA; 2002 - Competition Act
- ii) → 1965-MMS PhD - Open up market; MS Ahluwalia - PhD . . .

Ideological Criticism:

Neo-liberal reforms: Farmers suffering

who fixes MSP, prices, APMC, exports & imports? All Govt,

where is reform in agriculture.

REASONS OF ECONOMIC CRISIS OF 1991

① Very high FISCAL DEFICIT of both UG & SG

⇒ 8.4% - UG ; 4.2% - SG

② Very high INFLATION

⇒ By 1990, 11%.

③ Poor Industrial structure resulting in:

○ High cost ○ Low Efficiency

④ High CAD (Current Account Deficit)

Combined with very high short-term loans

which Resulted in BOP Crisis during Gulf war

ECONOMIC REFORMS

- Micro-economic Structural Reforms
- Macro-economic Stabilisation

<u>Micro-economic structural reforms</u>

1994- Competition in Telecom ~~centre~~ sector introduced

→ Targetting individual sector & plugging inefficiencies.

<u>Macro-economic stabilisation</u>

FD, CAD, Inflation, GDP ⇒ CREDIBILITY IS THE KEY

→ Stability of macro-economic parameters

$$\underset{\text{more Govt. expenditure}}{\uparrow FD} \longrightarrow \underset{\text{Rupee depreciates}}{\uparrow \text{Inflation}} \longrightarrow \uparrow CAD \longrightarrow \downarrow GDP.$$

<u>Govt-RBI Tussle</u>

started with Govt. blaming RBI for Nirav Modi issue.

Relation of Macroeconomic stabilisation

Income = Expenditure

$$\cancel{C} + S + T = \cancel{C} + I + G + Nx$$

$$S = I + (G-T) + Nx$$

Saving Investment Gap Equation

$$S = I + (G-T) + Nx$$

Pvt-Savings = Pvt.Investment + Fiscal deficit + Current a/c surplus

100 = 110 + 5 − 15

What do we do for extra money?

1. Borrowings
2. Allow investment from foreign

allow investment – FDI ⟶ ↑ Tax for Govt
GFD bridged

↓

Inflow of forex

But, how do we have Credibility?

Stability in parameters

→ Pay for ur own exp from own revenue & use for.inv. to bridge any gaps.

1995 – WTO signed
1998 – TRIPS signed
1999 – TRIPS signed

} Then how blame American hegemony?

Under Neo-liberal reforms, agriculture is suffering?

Actually Agriculture is not liberalised. Govt is controlling.

Market prices – MSP

Inputs – Fert-subsidy, ...

Exports & Imports — Canalised.

How come For. inv. is bad for India?

Forex	Year
$1 Bn	1991
$400 Bn.	2008

⇒ Should've increased Public Investment in farming instead of subsidies, MSP, etc. which only benefits rich farmers.

To control FD → ↓ Pub. Inv. in Agri was done
(under Neo-liberal reforms)
→ Bad thing to do

⇒ Recently, to control FD;

1 Public sector is bought by another public sector (shares)

Ease of Doing Business Index

Done for 2 cities – Delhi & Mumbai

Need to do for all states individually — Pan India like GST, I&B Code ✓

— Target must be on Efficiency, rather than indices —

LIBERALISATION

The policy of making rules & regulations more simplified and easy to understand with enough flexibility to encourage participation by all elements of an economy represents liberalisation.

Adam Smith, J.S. Mill, Voltaire, Rousseau } 18th century — Mercantilism was going on.
But, these liberals told consumers are affected at cost of benefitting domestic producers.

1820s - 30s → capitalism started rising
Factory system
Exploitation of workers
At wrong time, Govt came out & ↑ exploitation

1860s - 70s
MARX, Engels, C. Dickens } Socialism, Marxism

1902 → Bolshevics

1919 → Russian revolution
Dictatorship of proletariat turned into Dict. of Comm. party.

Till 1970s → Welfare State
Nexus b/w Govt. off. & Capitalists.

M. Friedman, Phelps, Stiglitz } → Govt control < chronism, Nepotism
NeoLiberals — Govt. must come out of market
↓ Tax ; Pvt. property

Maharatna All those firms which have turnover atleast 25,000 Cr, networth of atleast 15,000 Cr &
(Total assets - T. Liabilities)
profit of atleast 5,000 Cr can qualify under this category
They should've also been a Navratna for 3 consequtive yrs.
(However, final deciding authority is M.o. Finance)
They are free to:

a. Make investment upto 5,000 Cr
b. Enter into foreign collobration
c. Make all appointments except Board of Directors
d. Take all operational decisions
(pricing, RM, Quality of output, ...)

There are 8 Maharatnas in India:

① BHEL ② CIL ③ GAIL ④ IOC
⑤ ONGC ⑥ NTPC ⑦ SAIL. ⑧ BPCL (Sep, 2017)

Commission $\xrightarrow{\text{into}}$ Corporation

Navaratna

→ All those firms which had been MINIRATNA for 3 cons. yrs. & which score ≥60 points out of 100 given on 6 criteria by govt can qualify for this category.

→ They have the freedom to:

a. Make investments upto 1000 Cr.

b. Make all appointments till GM level

c. Take all operational decisions

→ There are 15 Navaratnas: (Now, BPCL & HPCL not)

Miniratna

category 1:

✓ All those firms with net worth of 300 Cr or more &

✓ which make profit for 3 consequtive years or which have made profit of atleast 30 Cr in one of last 3 yrs can qualify under this category.

They have freedom to invest upto their networth or 500 Cr whichever is lesser.

There are 58 firms in these category — update on 31, May, 2019

Category 2 :

→ All those firms with :

✓ Positive networth

✓ Profit for 3 consequtive years

can qualify under this category.

→ They are free to invest upto 300 Cr or net worth, whichever is lesser.

→ There are 16 such firms.

Advantages

✓ Growth incentives

✓ Performance oriented autonomy incentives

PRIVATISATION

Disinvestment (Divestment) → Selling of govt. shares to any other enterprise. (govt or pvt)

3 ways:

① MINORITY SALE → Govt = >74% shares after disinvestment (Y 74? min 26% req. to pass resolution to Board of directors. So it won't ~~go~~ have any impact on control of govt) - as good as 100%

② STRATEGIC MINORITY SALE → Govt = <74% but >50% after disinvestment (Y strategic? To send a signal to market that Govt is gradually going to privatise it)

③ STRATEGIC DISINVESTMENT / PRIVATISATION

✓ Govt = <50% shares after disinvestment.

✓ Managerial control is transferred to pvt-sector

– All disinvestment is not privatisation but it's only an aspect of disinvestment –

REASONS FOR DISINVESTMENT

GOVT. OPERATIONS

CORE	NON-CORE
– L & O	– other manufacturing
– Defence	– airlines
– Edu & Healthcare	
– Judiciary, admin	

Reallocation of resources from Non-core to core areas.

May be in 1950s & 60s, we needed govt. to work on non-core areas too, but now in 2018 not necessarily. Many core areas even are MISSED OUT by govt. So there is a need to focus on core. Now we can have competition & Pvt. in market. Need to focus on GOVERNANCE.

why primary school of govt in India is bad?

NO funds → Really? 87,000 crore for Air India.
1000s of crore for Scooter, etc...

During elections – we talk about Rafael & not day-to-day issues like Sanitation, Edu, etc..

Y so much issues on Rafael?

No ~~Institutional mechanism~~ on Defence deals.

INSTITUTIONALISATION

How IRCTC is giving tenders for catering? Not in public domain.

Y?	Not registered, not on stock exchange Internal audit & no external audit Not regulated by SEBI	what to do? Minority sale ✓ List on stock exchange Do ex audit by SEBI.
ILFS	Not listed on stock exchange. But, 120/300 subsidiaries are listed.	Y? To avoid info. in public domain.

Not only due to corruption but ESTABLISHED BELIEF

(Like parents lying to children. Ex: Bunking classes)

~~Systems will always~~ be imperfect - Don't dream of a perfect world, do a proper imperfect world → For this, only we need EXTERNAL checks & Balances.

Signal to market that gradually govt will move out of the sector, in case of large disinvestment.

YELLOW JOURNALISM [Oil prices rise will not impact inflation if other macroeconomic factors are managed well] Ex: Past 4-5 months, oil is ↑ but inflation is going ↓ 3.5 to 3.3%. etc. (July to Nov)

2 fun. problems - Populism in India

- Necessarily looking at Pvt. & Business deals with suspicion - not all profit is bad. Wrong means is only bad.
- Confusion in Bureaucracy - not trained in topic

Making policies on PERCEPTION & not REALITIES - is the problem.

— public — ↓ literate — Just talk w/o knowing — 'BELIEVERS Can Never be SEEKERS'

Y not HAL but Reliance in Rafael?

HAL couldnot even deliver sukhoi, it just brought it from Russia & gave to AF.

where disinvenstment is wrong?

- ~~Strategic sector~~
- Sufficient profit giving company
- No pvt. sector will enter in that sector otherwise.

R/W - is a case by case idea. Need to analyse of data w/o any silos of ideas.

Govt. job is to make sure disruptions in eco-system is minimised. Qn is not Y should I or Y shouldn't I? It is to make thing better, protect people.

EX:- Govt did very Good in issue of SATYAM.

Govt. took over managerial control w/o making it public sector, revived it for 2 yrs & gave it back - All ppl protected.

@upsc.risefinity

(Driver - Owner) 'Autonomy of public body will always be subject to sovereign guarantee' - Practically only certain autonomy is possible - Govt. will take ultimate call.

- No controversy on this -

EX: LIC buying IDBI shares.

IDBI is on loss. Govt wants to revive it becos to dilute it, we don't have FRDI (any law for diluting it), so investors will loose.

EX: ~~Why~~ RBI Vs Federal Bank .. (Qn asked)

RBI doesnot only see inflation.

Yes - Fiscal policy must be coordinated with Monetary policy.

Reasons for Disinvestment:

(i) Disinvestment is req. to focus on CORE activities of govt. and avoid the NON-CORE activities.

(ii) Proceeds from disinvestment ~~should~~ can be used for other developmental activities which can legitimise the govt. better.

(iii) Disinvestment will result in listing of public sector unit which will help in increasing transparency about their operations.

(iv) Disinvestment can be used to signal to market about future Industrial structure as visualised by the govt.

Precautions in disinvestment/Privatisation:

① Proper valuation of enterprise should be done before disinvestment.

(In 1997 : VSNL sold to Tata for a huge sum
In 1999 : 1st spectrum allocation to Tatas } very less base price – No proper valuation.)

② Social security of workers should not be compromised.

Economic reason? Fun. obj. of disin. is efficient use of capital

Vulnerable group:
- Old tenure (last years of work)
- Special provision (Disabled)
- Replaceable by machines

How to address them?
- VRS
- Allow rehab. (Shifting from 1 pub sector to other pub-sector)
- Buying a peace clause w/ pvt. player (no firing anyone for 8 yrs)

Ex: INDAL & BALCO case - Good thing due to peace clause,
INDAL started to train them for other jobs as they can't fire them or pay them for free either

Y not worker rights talked about in Kingfisher airline issue?

'Permanent job in a temporary life'? ☺
~~Permanent~~
Secure ✓

We are making Orwellian truth reality - All animals are pigs but some pigs are more than equal ☺.

Give workers the feeling of security but not permanance, so that competence remains.

Japanese Culture

"You are responsible for yourself & no other is responsible."

Parents - affection - tradeoff.

"Carrot & Stick" policy ✓ "Carrot & Carrot" policy ☺

not necessarily threat but competition

Air India

Good prospects, Can be revived

Need to remove certain clauses like 36,000 Cr loan also must be bought.

⇒ 71% tax on air turbine fuel = Y? somuch?

"Fleecing like Shylock"

"Don't kill Golden Geese"

③ Proceeds from disinvestment should be used to create new assets by reallocating funds towards social sector, infrastructure, etc.

(Production capacity must not be compromised - Reallocate Funds.
Facilitate business, make roads, edu. ppl)

[<u>Double tax avoidance agreement</u> signed in Flipkart case
amendment in 2017
So, it has been made Destination based & not Source based.
& Flipkart has already bee paid ₹4,000 Cr to Indian Govt].

"1985-86 → Rajiv Gandhi didnot want MM Singh to remain as RBI govt as MMS didnot want more money printing"
— From MMS Biography by his daughter.

<u>RBI</u> Autonomy is limited to the scope they can operate

④ If a public sector is on loss, then it should be revived wherever possible before disinvestment.

circumstances may also be reasons for losses
<u>Quantum of</u> profit is also important
<u>AI</u> → Civil Aviation policy 2016 → 3% fly in remote areas - all airlines

<u>Name change:</u>

Costly
243 Cr for Calcutta → Kolkata. [In WB Gazette]
330 mn ppl hungry - Y spend on this ?
"Judgement should be made w/o considering belief system"
"Gale of Creative Destruction"

Chachacha policy ⇒ 2 step forward, 1 step backward. — unstable, inconsistent. — Hoar

98-2004 - pvt

2004-09' - either not

10-14 - pvt

The Govt. has appointed Department of Investment & Public Asset Management (DIPAM) from 1st April, 2016 w/ following objectives: (to replace Disinv. Commission of 1997)

a) To co-ordinate usage of public asset

b) To suggest strategic sale & disinvestment of public sector units to the govt. by studying them on a case by case basis.

c) To suggest revival of public sector enterprise & allocation of their resource to improve efficiency.

Nodal body for public asset management.

144 companies - suggested to be disinv. (in 3 meets)

NMP - National Manufacturing Policy, 2011 &

MII — Make In India program

2015 - revised some NMP. To improve NMP, MII was brought.

Y SS is not enough & need Manufacturing?

Service sector can't create work for large semi/unskilled workers

w/o manufac. even clients of SS will be abroad.

SS growth is attached to manufacturing

So: koreans & Chinese developed not in today's world.

Ind : $300 Bn – 1.6% of Global trade – our exports.

US – 11% } we don't need to care abt trade war
Chinese – 12% }

chinese are moving out of Textile export – India can't afford to miss this opportunity. Our comp. is w/ BANG & VIETNAM.

— From NITI aayog ; 3 year action report —

Objectives of NMP

(i) To increase the share of manufacturing from 15% of GDP in 2015 to 25% of GDP by 2022.
[21% to 52% ⇒ when china grew; Services are elite, value creating but not volume creating]

(ii) To create 100 mn new jobs in manufacturing by 2022.
[2015–22 → 96 months – 1 mn/month but 52 ~~months~~ jobs/mnth only.
Bureaucratically slow – need ↑ single window clearance + SG & UG co-operation ;

Article by SAINATH
PMFBY → Farmers are quitting – Oriental Ins - Govt's own
Ins. business – playing on risks 38% in PMFBY. Then how scam ?

270mn – 2016-17 → } Normal monsoon, so ↓ risk.
280mn – 17 – 18 → }
foodgrains

CCE (Crop cutting Evaluation)
Jan – ~~Kharif~~ Rabi } But not done properly
June – ~~Rabi~~ Kharif }

(iii) To improve technical coefficient of Indian manufacturing and promote their export potential.

- Clean, Hygienic, ↑ Productivity

(iv) To train the work force to adapt to requirements of Manufacturing.

- PMKVY

The govt. initiated Make In India program from Sep, 2014 to promote Manufacturing in India. Under this program, govt. has identified 25 industries (20 are labour intensive) to be supported through:

✓ Policy Initiative.

✓ Fiscal Incentive.

✓ R & D & Innovation support

✓ Marketing & Export promotion support

The govt. has taken following steps to promote MII:

(i) It has allocated ₹1,000 Cr – NH development
1,48,000 Cr – Railway CAPEX
340 Cr – Warehousing devt, (2018-19 Budget)

to improve Logistical cost for the firms.

Govt. has also given 'Infrastructure Industry' status to LOGISTICAL sector to further reduce its cost.

(14% of total manufacturing cost goes for Logistics - now, so this measure is important)

(ii) Govt. has provisioned a package of
₹100 Cr – Textile
2600 Cr – leather goods industry
to focus on • Worker's training
• Technological improvement, etc.
[These are labour intensive.

2017-18 → 6000 Cr to textile but used only 1250 Cr.
Need efficient utilisation.
Now, world is moving towards synthetic shoes. So India has to learn

(iii) Govt has provisioned 3700 Cr – MSME
1400 Cr – Food Processing
to promote labour intensive manufacturing.

(iv) It has imposed Import duty on close to 200 products to protect Indian manufacturing firms.

(v) Rationalisation of Indirect taxes & direct tax
GST cut cascading effect
99% companies – ₹ <250 Cr investment – 25% on profit only
(before it was 30% + surcharge ₹ exemption)

(vi) Govt. has announced establishment of NATIONAL INVESTMENT & MANUFACTURING ZONE (NIMZ) to be developed as Integrated-Industrial townships.

They will be developed over a minimum area of 2500 acres with 30% of region reserved for manufacturing. (To prevent misuse as in case of SEZ).

There will be SINGLE WINDOW CLEARANCE for Financial & Administrative issue in the form of NIMZ Board.

There will be assured Infra to all the firms in this zone. and cnt. govt. will provide VIABILITY GAP FUNDING to the projects.

- ✓ ≯ 20% of total cost &
- ✓ It is a market loan & not free.

There are 22 proposed NIMZ of which 3 have been notified:

a) PRAKASAM in AP

b) MEDAK in Telangana

c) KALINGA NAGAR in Odisha

(Gradually NIMZ can be used to develop Industrial Corridors)

GLOBALISATION

Increased interdependence of countries due to :

- ✓ Larger movement of commodities – TRADE
- ✓ Larger movement of capital – INVESTMENT
- ✓ Larger movement of Labour – PEOPLE.

"GLOCALISATION"

Foreign goods sub-consciously becoming normal discourse.

Mc Aloo tikka, Jackets, English novels, blonde hair, GOT, thanks giving.

We act like we can deglobalise but we can't.

PHASE I – 1830 to 1910

European migration to USA & AUSTRALIA

·colonisation of Asia & Africa

since 17th cent → Interactions.

B/wn 1845-1900 → 2,45,000/year Europe

(1922 - only US Visa came)

Telegraph ; Wireless ; Combustible Engine – Inventions

It was based on Imperialism – struggle for colonies – led to WW-I.

Post 1960s:

Earlier: Japan - lower end manufacturing $\longrightarrow$ USA & W. Europe
Textile, shoe, toys

Post 1960s $\rightarrow$ Electronic items of Japan when US moved to even higher goods.

Then started EAST ASIA development.

By 1973-74: S.Korea, Hong Kong, TP ———— moved to electronics

Then Thailand, Malaysia, Philippines - lower end manuf.

But India did

By 1985: Malaysia, Thailand upgraded to electronics

Now Chinese started lower end manufacturing

Till 1986: 81% of FDI was among developed economies

Y not devd economies?

CW - fear of communism nationalising assets

Trade ↑ ✓ But Investment was not much

By 1992: Soviet split

End of CW & many took it as wrongly success of US capitalism & not failure of USSR socialism.

1992: Washington Meet - several countries. WASHINGTON CONSENSUS

Less role of Govt & ↑ role of pvt.

↓ Subsidisation ↓

- Neo liberal policies -

It was reflection of US model of capitalism.
problem is "CONSENSUS" — there are cultural differences & one model fits all won't work.
"Freedom as I desire you to have it" - Oxymoron.
ROUSSEAU — don't judge women by clothes.
'Not understanding what they meant
But just taking what they said &
Implementing the way we want it'

Post 1992 → some tried following US & many fell flat.
It necessarily not be unequal, bad — Globalisation can be good also.
For some things, there may not be an immediate answer.
Just need to accept "I don't know" w/o arrogance.

<u>How India got Tech?</u>

1992 - opened automobile market
Rule: To produce, must export from India in 5 yrs + only as Joint venture
We increased import duty on spare parts from 25% - 85+%.
So they started giving contract to our suppliers - they gave Tech on condition that we must sell only to them
1997 - Aut. started exporting from India.
Profit sharing tussle
1998 - Vajpayee in FICCI speech threatened indirectly Foreign players - So they allowed us to sell to others instead of sharing profits
2009 - 2nd highest Aut-exporter

Reasons / Benefits of Globalisation – PHASE II

(i) Created benefits for developed economies by giving them accessibility to cheaper labour ; cheaper Raw material; assured availability of inputs & larger markets of developing economies. (Ex. of Malaysia-France rubber-Tyre)

(Production possibility Frontier – reached by W. Europe

Globalisation, like any other policy will create its WINNERS & LOSERS but onus is on Governance to make sure winners compensate losers.)

(ii) Created Resource for Developing economies to fill :

- SAVING INVESTMENT GAP $[S = I + (G-T) + Nx]$ (from Inc = EXP)
- Receive New technology < Reverse Engg. as CHINA did / Technology sharing as INDIA - forced to share tech
- Utilisation of resources
- Opening up of global markets for domestic products

  (our IT sector grew bcos of foreign demand largely – from 1990s)

  \$1 Bn – 1992
  \$400 Bn – 2018 } Are they really here to take away from us?

  10x time GDP grew since then.

(iii) Development of Technology like INTERNET, Supersonic Jets, etc. made it easier & cheaper to communicate long distances which allowed Managing firms all over the world developing

GLOBAL SUPPLY CHAIN (RM → Industry → Market)

Ex: BPO in India

Earlier movies will release 5 yrs later in India but now in advance. It started with TITANIC making 1st $1Bm bcos 60% from Asia.

GLOBAL GDP – 3 times growth btwn 1992 & 2017

Smartphone dev. by pentagon, then others dev'd.

(iv) Profits in Financial markets increased exponentially which promoted wealth creation & hence Globalisation.

PORTFOLIO DIVERSIFICATION – more choices for products.

Rich became better off.

Financial asset (shares...) to Capital Asset (machines.) ratio:

1 : 1 → 1992

3.6 : ~~36~~ 1 → 2018

SUB-PRIME Crisis

2002-03 → US & EU went for 'EASY MONEY POLICY' to increase exchange of money. US allowed Sub-prime loans + Housing for all scheme.

(security value < than loans; To not-credible loan takers too.)

2007 → Housing rates ↓

'Sellers Market' → 'Liquidity Crisis'

– CONTAGION Effect

– RUN-ON-the Bank

($700Bn in global market by US.) to survive from recession.

→ This shook many ppl's belief in good of Globalisation.

2008 – Great Recession.

Poor became more vulnerable - seeds for deglobalisation

Reasons for DEGLOBALISATION (Problems of Globalisation)

(i) Wrong policies of MNCs like:

→ Practising Predatory pricing to capture markets

→ Extracting natural resources & damaging environment

→ Practising Round-Tripping & Transfer pricing to evade taxes by shifting profit from host nation.

[CCI (Competition Commission of India) will prevent the predatory pricing - from 2009. Before it MRTP was not much efficient.

Environmental laws are MISSING/- loophole used by MNCs. Weak & even weaker implementation.

BASE EROSION

Transfer Pricing: shifting profit from High tax country to Low tax country.

→ Round Tripping

→ Input Pricing]

(ii) Dissatisfaction among Industrial workers in developed economies due to Job-loss & in developing economies due to Informalisation of work force ⇒ 'Gig' Economy. Ex: Ola workers. Vajiram teachers

(Job loss ← shifting of companies, Automation.

Inform — X Social Security X Breach of contract)

(iii) Dissatisfaction among farmers due to larger fluctuation in agricultural price w/ less control on profit.

Loosing control on our own life. We suffer for loss somewhere.

Post neo-liberal reforms (1992) : Investment in agriculture ↓
Subsidisation in agriculture ↑

Mistake by India ⟵

Exposing farmers w/o giving them protection.

increasing COP for farmer + ↑ MSP
leaving poor farmer in mercy of weather.

(iv) Fluctuations in Stock market & other Financial markets have reduced Profit earning opportunity for Retail ~~mov~~ investors.

AI { Jobs donot get Removed, they just get Replaced.

Setting up Equitable institutions is the solution to address globalisation.

Human vanity always believes, I give more but get less & ⟶ Passing on responsibility to others.

Foreign Trade Policy, 2015

India's Response to Trade war.

On imports & exports.

Trade war:

\$ 18 tn — Total Commodity trade of Globe.

\$ 302 Bn — India — 1.6% ; china — 13%. \$ 400 Bn (Ind) Vs \$ 3 tn (china) — Forex

\$ 22 Bn — India's Cotton textile ; \$ 52 Bn — Engg. goods. India

\$ 80 Bn — chinese cotton textile ; \$ 781 Bn — " China

The objective of policy is to Increase India's export of Goods & services from $465 Bn in 2015 To $900 Bn by 2020

Trade Policy of India to Counter Trade War:

India announced Foreign Trade Policy, 2015 with an intention to increase its exports of Goods & services from $465 bn in 2015 to $900 bn in 2020.

Main features of Policy:

1) Better coordination among different govt. programs.

For ex: 6 different schemes to promote commodity export have been merged into a single MIS [Merchandise export from India scheme] &

2 different schemes for service export have been merged into SIS [Service export from India scheme].

Both these schemes linked

Global trade → \$ 15 tn – \$ 16 tn
(in commodities)

India's share → 1.6%

	Exports	
2017-18	\$302 bn (comm)	\$190 bn (services)

(i) Broadening of market & diversification of commodities & services for exports.

31% to EU & US alone.

Out of \$302 bn, \$195 bn from 20 commodities. We can diversify this to small goods (toys, leather, electronics..) as china also vacate market.

(ii) Improving efficiency of Manufacturing

✓ Good Infrastructure ✓ Logistics support.

a) → Reduce logistical cost (now 14% must go to 6-7%)

- Grading support, Storage, Transport, Retailing & wholesaling

b) → Ease of Entry & Ease of Exit (now 19 permits) - EDB

- Single window + Faster clearances (atleast less windows)

- IBC for ease of exit.

c) → Resolve NPA issues – to promote liquidity.

d) Improve Input Market

- Labour laws
- Land acquisition laws.

> Flexibility to bring formalisation of work force.

Now, 144 Labour laws (confusion) - Need streamlining.

> 80% affirmation of ppl living in that area - Very difficult.

#Pro-Business need not be Anti-Poor

Crony-capitalism is anti-poor.

crony capitalism increases with rigidity in laws & illiberalism

This new ESI, Crony Socialism - Public property misused by govt. to favour certain parties.

There must be transparency. Why not publicise how contracts are given to IRCTC, colleges, PSUs, etc.

Pre-1991 the condition was worse - connections with ppl would gain info of property etc.

(iii) Promoting Exports

Rationalisation of taxes with quick refund of IGST to exporters for their working capital requirement.

(iv) Improvement in trade negotiations esp. promoting service exports (our strength)

Ayushman Bharat

Trust model

Govt. will pay money

18 states have joined

It's only 3 months, too early to judge the scheme.

Oil prices increase need not lead to Inflation.

Ex: India in 2018.

(V) Focussing on sectors of comparative advantage like lower-end manufacturing;- make for India, Dev. for export - sectors like Tourism.

Tourism - Multiplier effect

Forex

Soft power -

Employment generation

a) Supportive Infra - Schemes like UDAN (small cities connected by air)

Better restaurants, amenities, etc..

b) Packaged deals to domestic & intrn'l tourists: via ads.

Ex: Buddhist tourism. Also need L&O smoothness

Train ppl to behave properly with tourists

2017 - $10mn tourists [India & Singapore similar, But for its scope, India can do much better] - Can improve till 80mn ppl.

Conclusion:

How good you can export depends on how good you can produce

Internal efficiency is the key

(Quality goods at lesser cost)

Sentinel Island issue

He must have taken Evangelical visa

Drama

i) Kartarpur corridor

One hand fight, other hand peace.

ii) Back data GDP

classified info?

INFRASTRUCTURE

ENERGY SECTOR

NON-RENEWABLE SOURCES

OIL PRICING

We not only need to produce more but do responsible consumption.

⇒ Till, 2002 we had: APM (Administered Price Mechanism) for Hydrocarbonds

Oil pool A/c → Petrol, Diesel, ATF, Naptha, LPG, Kerosene

charge more from here   to charge less from here

Cross subsidisation

Till 2001, oil prices were fine but now rose from \$12 to \$30

Gulf war; chinese growth demanding energy

By 2001 end, Oil pool a/c deficit became Rs. 80,000 Crore.

This was huge, so govt. appointed:

* KIRIT PARIKH COMMITTEE, 2002:
  - ✓ To suggest 'Deregulation of Oil Price'
  - ✓ submitted in 2004.

→ It suggested 3 steps to deregulate oil price

(i) Remove APM (Administered Price Mechanism) & Dismantle Oil Pool

(ii) Introduce Competition in the market by allowing private firms & provision Crude oil to all firms at Import Parity Pricing [IPP]

HYDROCARBON —
- Upstream – Exploration & Production.
- Midstream – Refineries
- Downstream – Retailers

Till then, Govt. was controlling all three, this report suggested to let trickle down to pvt also.

Import Parity Pricing [IPP] (of Crude oil)

SUM
- a) Free on board price of Crude oil / Price in world market
  Incl. all prices till it reaches on board
- b) Cost of transportation [Freight charges]
- c) Cost of Insurance [Insurance Premium]

Also called: Landed price of Imported Good

(iii) After the market has stabilised, allow exports of Refined Crude products (diesel, oil, Naptha...) & allow the firms to charge same price in domestic & foreign market
To make oil available in domestic too

This price is <u>EPP [Export Parity Pricing]</u>

- <u>Problem</u>: those who cannot export also will get same benefits as who export.
  It may also deter ppl from not exporting.

Trade Parity Pricing [TPP]

– for <u>Refined Crude</u> – suggested by RANGARAJAN COMMITTEE

weightage of TPP {
80% by <u>IPP</u> – (price @ which refined crude is produced
20% by <u>EPP</u> after getting crude oil @ IPP)

<u>Ex</u>: \$60 – IPP of Crude oil
\$100 – IPP of refined crude

Exporters will get adv:
Extra price via EPP
Market establishment in domestic too.

~~Impo~~ Non-exporters:
will get only 20% extra

⇒ this formula was approved by govt. in 2005.

⇒ we also derived a formula to $\underbrace{\text{convert \$ into ₹}}_{\text{Exchange Rate Parity}}$ to decide on IPP & EPP.
earlier, it was for 15 days; Now, every day

— This all made oil pricing complicated. —

From 2007-08 → Skyrocketing of oil pricing } Govt. gave subsidies - didn't pass on trouble to ppl.

2011-2012 → Very high price

2013 — $137

— $180

— $29

Govt. Interference But kept FD & CAD also in check

2015-16 → 2,00,000 Cr on Oil tax } Govt. didn't pass on

2017-18 → 1,50,000 Cr on oil tax. } benefit to ppl.

2017-18 → again rising — Though no inflation.

Refer: 2015-16 - ES I - Volume - I Ch-6 - 'Bounties for Rich'

How subsidies are taken by rich mostly.

Also, 50% + tax on oil prices even now.

If Govt. need to help poor:

Don't make market cheap - bcos rich also will get

But, buy from market & distribute it to poor

Also, don't put unnecessary tax

Reasons for Rise in Oil Price

2010-11-12 : Rise

a) OPEC cutting supply (↑ profit for them)

b) Chinese growth ↑ } ↑ demand
Indian growth ↑ }

c) $ became weak - depreciation
[American central bank printed more money & gave into market]

d) Russia cut oil produce
[Crimean war]

20~~13~~-14 : Fall

a) US-IRAN deal allowing Iran production.
Saudi started ↑ produce to ↓ price (2013-2014 doubled it)

b) Slow down in chinese economy – ↓ demand.
+ European + Indian slowdown.

c) Shale gas production ↑
(Higher energy eff. than Crude until oil is above $60/barrel).

d) Russia increased production ↑
≃ $35 / barrel.

2017 Sep Onwards : Again Oil price pick up

i) Removal of Quantitative easing in USA → Uncertainity in Financial market

↑ Oil price ← Shift of ppl from Fin.market to commodity market ←

ii) Cutting down of production by RUSSIA & OPEC

iii) Revival in CHINA, INDIA, USA & EUROPE economy
[2017-18 : Highest global growth year after 2007-08]

iv) Less production in shale gas market

v) Possibility of American sanctions on IRAN.

[Depreciation of ₹ & Increase in Oil price cause & Effect for each other]

Recent dip in Oil price since October, 2018

(i) Very Large increase in US oil supply

(ii) Strengthening of $

(iii) Relaxation of sanctions against Iran

(India & Japan given reprieve to buy from Iran)

(iv) Increase in shale gas production after 15, Oct.

(So, again they reduce oil price < $60 to discourage shale gas)

Steps taken by Govt. to improve transparency in Oil Mkt

1) Govt. has allowed daily change in petrol & diesel prices by passing on ER info to fuel pumps. hear

2) Developing strategic oil reserves for emergency

1st – Vishakapatnam – 1.3 mmt

2nd – Mangalore – 1.5 mmt } ½ of them will be filled
3rd – Padoor – 2.5 mmt } by UAE (ADNOC). ADNOC.

proposed { 4th – Chandikhole – 2.5 mmt (Orissa) } To increase 10 days to
5th – Padoor – 2.5 mmt } 21 days to bring stability.

3) Steps to improve efficiency of domestic refineries through vertical integration. [in 2016 Budget]

(ONGC & HPCL – merger – for Economies of scope)

merging similar companies to ↓ admin cost, etc.

Challenges of Merger:
Problems: 1) HR 2) Supply chain management
"n" Diff. sources supplied earlier - need coordination.

[ONGC – Guj. state petrochemicals → Take over was a bad idea. No synergy. But HPCL is reasonable]

Gas Market in India

NELP - New Exploration & Licensing Policy, 1997

Including pvt-sector (including FDI) to explore & produce Hydrocarbons in India – [UP, Mid & Down stream - All]

Govt. started auctioning:

NELP 1 – 1st auction in 1999.

NELP 10 – Last auction in 2010.

- 368 basins auctioned. Out of them only: 160 operational in 2011.

Reasons for failure of NELP:

(i) Disputes due to APM [Administered Price Mechanism]

(ii) Disputes related to cost under profit-sharing arrangement.

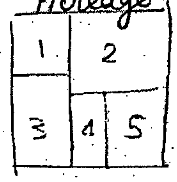
Notional costs — dispute - Govt. accused pvt-companies of (only on paper) showing ↓ profit

(iii) Very high Royalty charges resulted in high fixed cost.

Royalty – 14% on projected revenue, which may not come actually.

(IV) Lack of Universal Hydrocarbon policy & Lack of OPEN ACREAGE.

Acreage



1, 2 .. 5 – Basins

License only for one basin. It led to discouragement to report exploration info in case mine is 1 but resource is in 2 fearing new auction.

HELP – Hydrocarbon Exploration & Licensing Policy, 2016 March

Designed to overcome -ves of NELP.

Features:

(i) Firms can charge their own price subject to maximum price ~~seali~~ ceiling of the govt.

(ii) Profit sharing arrangement has been replaced by Revenue sharing arrangement to remove disputes on cost.

– Earlier, share only during profit. But, now share must even during loss.

iii) Govt. has exempted Royalty for 1st 7 years
[8 yrs in deep sea drilling - beyond nautical zone-2nd] &
Reduce rate from 14% to 10% for Onshore drilling &
to 7% for offshore drilling. — after 7 yrs.
to 2% for deep sea drilling — after 8 yrs.

iv) Universal hydrocarbon policy with universal acreage has been introduced.

Problem of not repor

HELP-1 : Dec-Jan 2017-18
105 auctions of fields.

They can migrate from NELP to HELP w/o cost.

Issues need to be resolved [w.r.t both oil & Gas]

1) Cost of capital has to be reduced by.
[Machines - Imported / leased - ↑ cost]
∘ rationalising Import Duty

2) Increasing competition in market to promote 'η'
[Now only 5-6 firms]

3) Developing a regulator for hydrocarbon market to ensure immediate action against unfair trade practice.

4) Environment regulations must be strengthened to prevent over exploitation by Stren. Env. Control. Laws

RENEWABLE ENERGY

WIND ENERGY

1983-84 → 1st plant

2018 (Oct) → Installed capacity → 34,300 MW

Target → 60,000 MW (2022)

Benefits of Wind Energy:

i) Environmentally cleaner source of Energy.

ii) Long coastline of India (7500 km) & Deserted regions (Thar, Saurashtra, Kutch)

iii) Falling cost of wind energy due to technical improvement

(Ht: Now 120m possible + 5 inches blade now)

2016: Auctioning instead of purchasing; cost ≃ solar.

Authority: Solar Energy corporation of India. (Prelims)

Challenges of Wind Energy:

i) Seasonal & localised impact.

73% - Monsoon

Difficult to Transmit & can't store.

ii) Very costly installation & high skill requirement.

iii) Very low plant load factor → ↓ revenue.

Capacity utilization (only 25-30%)

Potential of India - 3000 MW. check

SOLAR ENERGY

Solar energy:

	2018 (Oct)		2015
Installed capacity –	25,600 MW	;	25,00 MW.

Target – 100,000 MW

60,000 MW solar plants

40,000 MW roof tops.

Benefits of Solar Energy:

i) Tropical nature of India.
   - 300 days of sunshine
   - Inclination more vertical

ii) Negligible running cost
   - Semi-skill req. for maintenance & repair.
   - PMKVY – Solar Mitras (now 50,000 trained for job) to continue with solar energy

iii) It can provide energy security to off-grid regions &
   - Not covered in thermal energy

it can supplement wind energy.
   - Hybrid wind-solar energy plants – Govt. starting

Steps taken by Govt. to promote Solar Energy:

① Govt. has extended ACCELERATED DEPRECIATION BENEFIT to solar energy producers in India.

✓ Necessary in case of dynamic tech advancements which is the case of solar energy [Technical Turnover]

✓ Also larger tax benefit than normal dep. benefit.

② Govt. has provisioned upto 30% tax benefit to social & commercial enterprises if they become 100% dependent on solar energy (for 3-4 yrs).

③ Govt. has permitted devt. of MEGA SOLAR PARKS with capacity upto 40,000 MW. (earlier: 20,000 MW_Now ↑ due to willingness of govt. to ↑ economy of scale)

④ India has been a founder member of INTERNATIONAL SOLAR ALLIANCE (COP 21, 2015, France) – 121 members

1st treaty based organisation HQ in India – Gurugram

1st meeting in 2018 – Gurugram : 3 major focal areas:

i) To scale up use of solar Energy in Agriculture.

ii) To scale up research & development in solar energy

iii) To extend use of solar energy to under-devd. countries

Challenges of Solar Energy:

① Availability of land area.

② Continuous Bankruptcy of solar energy producers.

Companies – too enthusiastic in quoting the price (≈ Rs.2.6) seeing tech. improvements in future.

✓ We need not only more production but sustained production. (so cheap only not enough, regularity is crucial)

ELECTRICITY SECTOR

GENERATION | TRANSMISSION | DISTRIBUTION

Total installed capacity : 3,30,000 MW (31^{st} Oct, 2018)

73,000 MW Renewable (22%)
Coal based (54%)
Oil & Gas based (13%)
~~Sma~~ large hydro (6%)
Nuclear (3-4%)

2 Major challenges of power sector

(1) Very low plant load factor of Gencoms
Ideally (85%-88%) ; India — pvt. (52%)
Public sector (66%)

> Poor availability of coal (Timely factor) [Coal India ltd]
-Unstable
> Outdated machinery
> Very low demand from Discoms.
Technical energy surplus
Discoms - going bankrupt ; hence Gencoms - surplus

(2) Very high Transmission & Distribution losses.
Technically - Friction } 30-50% → harming Discoms.
Practically - Theft }
Slums grow spontaneously → Illegal electricity
Organised crime
Even upper middle class complains - Bad Culture

Irresponsible usage, yet asking for subsidies/concessions.
We need to train for proper usage
Political populism
99% time - breaking law is not spur of the moment
Mostly due to confidence of power to get away

Nov, 2015 - due to high T&D loss;
Discoms losses → Rs. 3,15,000 crore
So - UJJWAL DISCOM ASSURANCE YOJANA

NPAs
10% of total loans
so, 90% honest payers.

$\boxed{\text{UDAY}}$

✓ SGs will take over 75% of loans of Discoms & issue bonds to pay back these loans to respective banks.
✓ Discoms are allowed to issue bonds & payback rest 25% of the loan.
> Soln. of Twin-Balance sheet problems (of Discom & Bank)
> ↓ Interest cost of Discoms - use money to upgrade.
✓ SGs will also work to develop operational efficiency & managerial efficiency of Discoms.
making sure recovery of cost of operation.
to ensure regular raw materials & regularity of generation.
✓ 27 states out of 29 have joined UDAY.
[WB & ODISHA
↓ political ↓ Their Discoms are good]

Challenges of UDAY:

i) No significant drop in Transmission & Distribution losses. (hardly only 2% drop in 3 yrs - Political populism)

ii) 10 SGs have not yet issued bonds to pay back the loans.

SAUBHAGYA (Sep, 2017)

- Sahaj Bijli Har Ghar Yojana

Objective: To provide electricity to all HHs which demand it in India. Each HH will be provisioned with a minimum supply of 1 Bulb Socket;
1 DC fan;
1 DC plug;
5 led bulbs;
5 yrs of maintanence & repair-free

In areas which are not connected by thermal power, Solar power of 200-300 Watts will be used.

There will be No installation charge for HHs BPL - identified through SECC - (Socio-economic Caste Census)

Installation charge of Rs.500 for HHs APL - in 10 months installments of Rs.50 -

In Target Mode - implementation.

India

4.6% - >50,000/month ppl

NSSO - >14 lakh/yr means you are in top 1%

Rich in India choose not to realise they are rich.

(2015-16) ES I - 92% petrol & diesel subsidy taken by rich

70,000 Cr - Urea subsidy
% don't reach farmers

Applications will be taken by conducting information campaign & door to door movement of govt employees, using Aadhar & Mobile to take immediate applications.

It will not be an AMNESTY scheme (early defaulters – lost electricity – will not be part of this)

Total estimated expenditure is Rs 16,900 Crore, out of which Rs. 12,000 Crore has been granted through 2018-19 BUDGET.

> Target : 31^{st} Mar, 2019.

> 3 Cr 10 lakh applied – 2 Cr 85 lakh accepted

> Nodal : RURAL ELECTRIFICATION CORPORATION, M. of POWER.

Hilly, Remote & Naxal areas.

~80 lakh HHs have not demanded yet (4 Cr ppl)

- Poor
- Move frequently
- Lack of awareness.

Challenges of SAUBHAGYA:

→ Reach out to real poor.

→ Motivate ppl who steal electricity to join this scheme

→ We need to have Handholding approach. Most ppl are 1st time users & need to help them in getting used to it by providing needed maintenance.

→ Degeneration into Political Populism

28,000 MW extra electricity needed – Govt is hopeful of meeting it.

"Ppl of the country beget the leadership"
— Samuel Johnson

Telecom Vs Electricity

- Prudency in usage
- Introduced competition to include all
- Institutionalisation req →

- Central Electricity regulatory commn. could be a better solution.
- Intro. electricity into GST as it is universal.

If - 10% HHs + all community institution electrified, then 100% electrification.

Deendayal - Area
Saubhagya - HHs.

ROAD DEVELOPMENT IN INDIA

NHs — 31,000 km
Total road network — 14 lakh km
} Till 1998

NHs — 1,30,000 km
Total road — 55.3 lakh km
} Oct, 2018.

* 1998, NH Development Program

(1) 1st phase — initiated in 2001

i) Golden quadrilateral: 5816 km project
* connects all metropolitans via 4 lane highways

ii) NS-EW Corridor: 7200 km project

Srinagar
Porbandar — Silchar (atleast 2-lane highways).
Kanyakumari

They both were supposed to be completed by 2008.
But, in 2018 : 91% only complete.

Reasons for Delay:

① Lack of timely clearance of the project
   Land, env. clearance

② Lack of timely financing to the project.
   Viability gap funding missing.

③ Over Engineering of the project.
   To extract more cost by unnecessary structures.

④ Monopoly of few contractors in certain regions.
   Cartelisation of contractors.
   Crony-capitalism.

* Sep, 2015 : BHARAT MALA :

Umbrella program - it covers all project of road devt. in India.

Projects covered under Bharat Mala:

1) Dev. of 83,000 km of NH including the impending ones;
   Developing 44 new economic corridors (already 6 exist)
   24 logistical hubs (1 place for facilities integrated -
      Packaging + Grading + Measurement +
      Storage + wholesale)
   36 National Grid connections

2] Connecting 550 district HQs with NH & to backward regions.

3] Constructing 2000 km of Border roads.
(Gujarat H11 Nagaland & Manipur)
All are metalled & Allweather roads

4] Constructing 1500 bridges
SETU BHARATAM 250 road Over bridge (ROB) } for last mile
PARIYOJANA 250 road under bridge (RUB) } connectivity.

5] To develop 4100 km of State Highway;
1100 km of NH in areas afflicted by Left Wing Extremism &
To develop 4000 km of road under NE special Area Road Development program

Nodal body for execution
NH & Infrastructure Devlopment Corp. ltd,
M. of Transport
Total Expenditure estimate
₹ 5 lakh 35,000 Crore
- Funded by issuing Bonds, Budgetary support by UGi, Central Road Fund (2003 - Oil taxes), Monetisation of Assets (Highways into Tolls, Ads..etc.)

Benefits of BHARATMALA
✓ Improving Connectivity will encourage Business
✓ Employment Generation will become high
✓ Promotes Make In India
✓ Inclusive Growth
* Port Development in India.

PORT DEVELOPMENT IN INDIA

12 Major ports	≃200 Minor ports

Total port capacity: 18 mn Metric tons
91% → Foreign trade in volume
70% → Foreign trade in Value

Challenges:
i) Poor port Infrastructure
ii) Large presence of Red Tapism
turnaround — 3 days : India
— 10-12 hrs : Hong Kong etc.

Different ports have different problems
- Haldia (Riverine) — Siltation
- Marmago — size
- Navasheva (Mumbai) — Congestion
- Kandla — ship building
- Chidambaram — Modernisation.

*(July, 2015) SAGARMALA PROJECT:

4 main objectives

① To develop International Port Infrastructure.
② To improve port connectivity to industrial regions.
③ To increase industrialization around ports.
Coastal Economic Zones
↳ 14 have been identified in a min. 20 sq.km area.
All are in project development stage.
④ Community based development.

Finance: Sagarmala is an 8 lakh Crore project, out of which project worth 2,52,000 Crore is already under construction; project worth 1,13,000 Crore has been approved:
↳ 450 projects including development of:
6 new major ports at:
Sagar Island, WB
Outer Paradeep, Odisha
Enayam, TN
Shrikadi, TN
Bellekari, Karnataka
Wadhavan, Maharashtra.

Nodal Body: SAGARMALA DEVT. COMPANY, M.of Shipping

National Waterway Development

1st NW → Haldia to Banares
1st commercial use of waterway post-Indep.
3 Nodal pts
i) Haldia, WB
ii) Banares, UP
iii) Sahib Ganj, Bihar

> Eastern Dedicated Freight Corridor (Delhi to Haldia)
only commodity — railway & waterway
D to DDI — DDI - Hal
Banaras.

> Western Dedicated Freight Corridor
Still not yet developed.

Aviation Devt In India

National Civil Aviation Policy, 2016

1953 – Nationalised Airlines (TATA → Air India)
57 – Indian airlines
94 – Opened up
2007 – NACAL (Merged IA & AI)

① New airlines were allowed to operate on foreign routes if they reserved 20% of total seats for domestic flying.

Before 2016: 5yrs in India } for flying foreign.
20 own aircraft }

From 2015: New airlines started asking to ease.

② Govt. introduced REMOTE AREA FLYING PROGRAM under which every airline has to reserve atleast 3% of its total seats for remote area flying.

Remote Areas → NE; Leh & Ladakh; Islands

③ Govt. has introduced REGIONAL CONNECTIVITY SCHEME called $\boxed{\text{UDAN}}$

→ Govt. will fix max. air fare for all identified routes upto 1 hr of flying & provide viability gap funding on 50% of the seats (Not more than 40 seats in aircraft & 9 in helicopters).

The service providers will be chosed by REVERSE BIDDING method.

→ Support to Airlines:

a) Exemption from fee to AAI, on UDAN routes.

b) 0% GST on maintenance, repair & overhaul activities on UDAN routes.

c) 3 yrs of CAPTIVE FLYING (none except the chosen one will fly)

Benefits of UDAN: (2 questions own)

i) Promotes Business & Tourism (esp. to smaller cities)

ii) Promotes Make In India

(now, SARAS - Indigenous manufacturing of small aircrafts)

iii) Better utilisation of Airport Capacity.

155 air ports - audit of usage

55 new air ports added for usage.

iv) Employment generation (Direct & Indirect)

Here too, we need Handholding approach.

Indian aspirations growing → ↑ viability of flying

RAILWAY DEVT. IN INDIA

Challenges:

i) Poor Infrastructure development & low capacity creation.

- 5 times - increased capacity

But, 14 times - Ppl capacity demand

17 times - Freight capacity demand.

Delays, accidents, congestion

(65% — above 100% capacity operating)

ii) Poor Technological development:

a) Only 51% of routes electrified

b) Large presence of Manual signalling.

c) Lack of lighter coaches (More fibre; less steel)

(Same speed with more bogies)

iii) Irrational Pricing Structure

1994 - 2012 → No raise in fare, rather down sometimes.
But input prices rose.

But, one of the highest freight rate in the world.
Open container transfer in many places
No assurance of timely delivery
Only, 29% – bulk comodity via Railways
71% – bulk commodity via Roadways (Opposite from world)

92% - 98% → Operational ratio -
(Rs. 98 spent to earn Rs. 100)

2004 – Rs. 260 Cr loss
Lalu – Rs. 150 Cr profit
Mamta – Rs. 270 Cr loss

* 2014 - NATIONAL RAIL VIKAS YOJANA

i) Capital Expenditure in Railways has been doubled ≃
from: 81,000 Cr (2014) to 1,48,000 Cr (2017-18)

ii) Introducing e-ticketing to remove touts (middlemen)
Platform ticket losses – ≃ 350 Cr.

iii) Introducing Bio-toilets in all coaches by end of 2019
73% – now covered.
✓ less water usage (bacteria)
✓ stops open defecation.

iv) Reducing no. of manual signals < 10% by 2019.
(Now, 27%)

Untill we don't invest in humans, they are capable of destroying even excellent facilities
→ To make them responsible

v) Introducing high speed Rail project (Bullet train) (> 300 kmph).
(Today fastest - 150 kmph)
1st → Mumbai - Ahemedabad : 1,08,000 crore
80% Japan loan
@ 0.1% interest for 50 yrs.

2 WRONG CRITICISM:

× Costly loan. (₹ has appreciated against yen in last 10 yrs)
× Tech transfer [E-Shinkasen 1] of Japan is outdated as they use E-shinkasen 3. But, we could only absorb E-shinkasen 1 as of now.

Benefits (Claim by Govt)
→ ↑ Speed of connectivity & promote Business.
→ Promote Make In India. (But, who will buy it?)
→ It will promote employment generation.
→ It will create +ve spill over effect of Technology

Write-up
ILF&S
Ayushman Bharat
(Feb 2nd week)

Challenges :

i) Financial Viability may not be possible.
Need Economies of scale from 500 km → 5000 km.
Long gestation – so will it be relevant after 30 yrs.
(UDAN, hyperloop, bharatmala - - - also coming)

ii) Technical Absorption will be difficult.
E-shinkasen : metre gauge
But we use : Narr & broad gauge

iii) Safety Training will have to be enhanced.

2nd GEN REFORMS

Extension of 1st GEN REFORMS (1991) which can help make them more efficient.

1. APMC Market Reforms (shiv & SS)
2. GST
3. FRBM Act
4. Monetary Policy Reforms (MPC, etc.)
5. Exit Reform (I & BC) –(SS)

TOPICS:

1. Fiscal Policy
2. Inflation
3. Foreign Investment

11th, 12th NCERT → New

1] C.P. Sachdeva (or)
T.R. Jain (or)
I.C. Dungra

2] Pratyogita Darpan (bs
- Don't buy monthly
- It gives something of everything

3] Economics Dictionary
- Penguin / Collins

4] Indian Economy (if need)
- Mishra & Puri (or)
- Dutt & Sundaram (or)
- I.C. Dingra

5) Classnotes, YB, Eco Survey

1. Fiscal Policy

It deals with 3 things:

1) Revenue of Govt. - Taxes
2) Govt. Expenditure - D-D, long term, subsidies
3) Borrowings of ~~Fi~~ Govt - Reflected by fiscal deficit

Fiscal deficit: (FD)

↑FD → ↑ Borrowings

- i) ↑ Interest burden (from current income)

↓

- ii) ↓ Credit Rating

↓

- Borrow on ↑ interest rate

4 Energies
Food (Awake)
sleep
Deep breathing
Meditation

Union Budget:

It gives figures for three years:

(Ex: Feb 2018 budget is for):

1. 2018-2019 - Following year - BE - Budget Estimate for April 18 - March 19 (1st - 31st)
2. 2017-2018 - Current year
   - BE - Budget Estimate for Feb 18 - Mar 18
   - RE - Revised Estimate of April 17 - Jan 18
3. 2016-2017 - Previous year - AE - Actual Estimate of April 16 - March 17

i) First Component of Fiscal Policy – REVENUE – TAX

General Classification of TAX STRUCTURE of a Country

Every country's tax structure has the following THREE types of classification of Taxes:

a) Direct & Indirect Tax

b) Specific & Ad Valorem Tax

c) Progressive & Regressive Tax

a) Direct & Indirect Tax:

⇒ A Direct tax is a tax which has to be paid by the same person or entity on whom it is imposed. (i.e) Its burden cannot be shifted to someone else.

Ex: ▷ Taxes on Income & Wealth:

- Income tax
- Property tax
- Corporate tax
- Wealth tax etc.

▷ Direct taxes reduce inequalities as those earning more are subjected to higher rates than those earning less.

⇒ An Indirect tax is a tax which is imposed on someone but whose burden falls on someone else (i.e) Its burden can be shifted. Ex: ▷ Taxes on Goods & Services:

- GST
- Excise duty
- Entertainment tax
- VAT
- Custom duty etc.,

5 Major taxes of Govt.

1. Income tax
2. Corporate tax-34%

} Direct - 52%

(Now)

3. Excise duty
4. Custom duty

} Indirect - 48%.

5. GST - Before July 2017 it was Service tax

In a country, always

Direct tax % > Indirect tax %.

⇓ bcos it is on Income & wealth ⇓ Rich pay more, Poor pay less

⇓ bcos it is on G & S ⇓ Rich & Poor pay Same amount - higher burden on poor

b) Specific & Ad Valorem Tax:

⇒ A Specific tax is a tax imposed on the basis of any specific feature/attribute of a commodity.

↳ like its length, width, weight, volume, quantity etc.,

⇒ An Ad Valorem tax is a tax which is imposed on the basis of

" Progress is equal to the diff. between MIND & MINDSET ".

- Narayana Murty

Income tax Act 1961

- Before 1991, In India

DT % < IT %

- 19 % - 81 %

See : 9/6/18 Newspaper

Oil price cut - Rajiv Kumar

- central imposes specific tax per litre

- state imposes Ad valorem on total value

Burden by Advalorem > Burden by Specific

5 × 10 - 50 - 5 % =

5

French revolution was bcos of Regressive tax

Price of a commodity (or) total value of the commodity

⇒ The distinction b/w these 2 taxes can be explained by foll. example: We go to a restaurant – order 4 dishes – bill ₹3000 without tax. If tax is imposed by the restaurant on the basis of no. of dishes (each dish) it is specific. If it is imposed on ₹3000 it is Ad-Valorem tax.

↳ Every country has a mix of both specific & Ad-Valorem taxes depending upon the nature of the commodity & prevailing conditions in the economy. Ex. for mix ⇒ Electricity bill in our home.

3] Progressive & Regressive Tax:

A progressive tax means as the income of a person goes up the rate of tax imposed on him goes up so that @ higher income he pays higher tax. Thus Progressive tax reduces inequality and makes the tax structure more equitable

Ex: 20% on 10 lakh } – Diff in income double before tax
10% on 5 lakh } But after tax not so – so reduces ineq.

A Regressive tax means as the income of a person goes up the rate of tax goes down so that @ higher income the tax is relatively lower. No country opts for regressive taxes.

* there is also a classification between SURCHARGE & CESS

A Surcharge means Tax-On-Tax which is imposed on incomes above a certain level inorder to reduce inequalities further and make tax structure more progressive

for ex: In India, there is a surcharge of 15% on those individuals whose annual income exceeds One Crore.

A Cess is a temporary levy which is imposed to achieve a specific objective. Once the objective is achieved it may be withdrawn. for ex: Swachh Bharat Cess, Krishi Kalyan cess, Health & Education cess.

INDIA'S TAX STRUCTURE

It comprises of ⇒ i) Central tax ii) State tax

Prominent Central taxes are:

Income tax ; Corporate tax, Excise duty, Custom duty, GST

Prominent state taxes are:

GST ; VAT; Entertainment tax; Entry tax; Luxury tax; Tax on Betting, Gaming & lottery etc., CORPORATE TAX: It is a tax imposed on annual incomes of companies. It is imposed at a flat rate of 30% (statutory tax) on domestic companies & at a flat rate of 40% on foreign companies. In addition there is a surcharge of 12% on those domestic companies whose annual income exceeds 10 crores and a surcharge of 7% on those domestic companies whose annual income is between 1 – 10 crores. Also there is a surchage of 7% on those foreign companies whose annual income exceeds 10 crores and a surchage of 2% whose annual income btwn 1-10 crores

but actually after rebates concess. 23% Effective tax

Corporate tax rate on domestic companies has been brought down to 25% on incomes of these companies whose annual turnover is upto 250 crores. (Exp'

INCOME TAX: It is a tax imposed on annual income of individuals. There are 4 slabs:

upto 2.5 L – Exempted
2.5 – 5 L – 5%
5 – 10 L – 20%
> 10 L – 30%
< 2.5 L – Exempted

In addition there is a Surcharge of 15% whose annual income exceeds One crore and a surcharge of 10% for btwn 50L & 1 crore.

EXCISE DUTY : It is a duty imposed on goods manufactured within the country. It has to be paid by the manufacturer before he can take his goods out of the factory premises for sale.

↳ It is also called CENVAT — Central Value added Tax because it is imposed on the priciple of VAT as explained in foll. example :

A manufactures of shirts may manufacture shirts worth 10 lakh for which he may use cloth & other inputs worth 4 lakhs. If he is subjected to pay excise duty both on 10 Lakhs (Final output) and on 4 Lakhs (Input) it will mean that

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In 2006, Steel from S. Korea dumped in India

In 2001, US. rice - Basmathi dumped — $\boxed{\text{India}}$ (won) Vs US in WTO dispute ; Basmathi Geo. monopoly

WTO - 1995 — reduce peak rate of custom duty — Free trade

ASEAN — 5%

U.S — 15%

(wheat 30% now bcos wheat from Russia & Ukraine is cheaper than domestic)

In 2001, China dumped toys - batteries - electrical goods in India ⇒ India started sealing borders to prevent entry ; Directed those selling these must show MRP; A.D. duty

2003 — China become WTO member

he is subjected to double taxation. Hence, under CENVAT his liability to pay excise duty would be Excise on 10 L (output) − Excise on 4 L (Input) = Value added (6 L).

Thus under CENVAT he gets credit for tax paid on inputs which is technically called Input Tax Credit (ITC)

CUSTOM DUTY : It is duty which is imposed on goods imported by a country i.e) On Imports - also called Import duty. It is of following 3 types:

1] Basic custom duty 2] Anti-dumping duty 3] Counter vailing duty

Basic custom duty means that rate of duty which is imposed as a standard rate on most imported goods. It is popularly called Peak Rate of Custom Duty which in India @ present is 10%. 100% before 1995

Anti-dumping duty is a duty imposed to prevent dumping. DUMPING is a practice whereby some goods may be sold to a foreign country at a price below the price in home market in order to capture a foreign market. Hence to prevent this Anti-dumping duty is imposed.

Counter Vailing Duty is imposed on such of the imported products whose price may be lower than the price of similar domestic product due to export subsidy given by exporting countries. In such cases CVD may be imposed to neutralise & offset the price advantage enjoyed by the imported goods.

Other Central Taxes:

STT [Security Transaction Tax]

i) It is imposed on sale & purchase of shares in the
stock market   not IPO   companies   Chidambaram
secondary market. (shares of existing faces)   introduced it

ii) It is shared equally between buyer & seller. in 2004

Ex: Investor A sells shares of Reliance Industries to B for ₹.10 L. On this STT will be imposed at a very nominal rate of 0.125%.

Capital Gains Tax [CGT]:

It is a tax imposed on capital gains. (i.e) gains arising out of appreciation in the value of shares (financial asset) or real estate (physical asset) over a period of time. For ex: shares worth 2L bought by Investor A 2 years back are sold today for 4L resulting in capital gain of 2 L on which Long-Term Capital Gains (LTCG) tax is imposed at the rate of 10%. Similarly if shares bought by an investor for 2 L are sold within one year for 3L resulting in capital gain of 1 lakh which will be subjected to Short-Term CG (STCG) at the rate of 15%; For property:

- Arun Jaitley reintroduced (14 yrs back) LTCG in 2018
- May not be a healthy sign for stock market as shares are to be held for long-term.
- STCG already exists.

Only based on. ↲ ↳ No long term; No short term
today's property value.

MAT [Minimum Alternate Tax]:

MAT is a form of corporate tax which is imposed on those companies which earn profits and also pay dividends to share holders out of these profits and yet they may pay zero or very low IT (Income tax) as they may avail various rebates and concessions to bring down their tax liability. On such companies MAT is imposed @ rate of 18.5% of their book profits.

1) BOOK ACCOUNT

Profit or loss

2) IT ACCOUNT

@ corporate tax – 30%

– they apply rebates, concessions, etc.

Few imp. rebates:

⇒ Depreciation Allowance

⇒ charitable allowance

DIVIDENDS – part of profit of company to share holders.

Ex: Profit – 500 Cr.

Rebates & exemp – 250 Cr.

Corporate tax on – 250 Cr. (30%)

If 30% on 250 Cr < 18.5% on 500 Cr, then 500 Cr will be used as a basis of tax (18.5%)

Once: Ambani – brought it to zero tax – claiming high depreciation

STATE TAXES

1) State Level VAT (Value Added Tax): (Advalorem)

It was introduced from April 1, 2005 replacing age-old sales tax regime in India. The biggest virtue of VAT is that:

TAX EVADED AT ONE STAGE CAN GET CAUGHT AT NEXT STAGE BCOS IT IS MANDATORY UNDER VAT TO USE BILLS FOR EACH TRANSACTION TO CLAIM INPUT TAX CREDIT.

Empowerment committee – to convince states.

– States & Traders opposed initially – Traditionally we never used bills

(ITC)

In other words, Input tax credit is the tax that retailer has paid on Goods that he bought from the wholesaler. As such, at each stage, under VAT:

TAX IS PAID ONLY ON VALUE ADDED.

so that if there is a random check on a retailer to prove how he had paid tax to value added only, he would have to produce bills to show the price at which he bought from wholesaler. Hence, the biggest merit of VAT is : IT MINIMISES EVASION.

PREVENTS DOUBLE TAXATION

	Pre-GST	Post-GST
	2000	2000
Con Vat @ 12.5%	250	360
	2250	
Vat by consumer @ 12.5%	290	
Final price	2540	2360

360 → 9% CGST, 9% SGST } 18% GST

Tax on Tax. | No tax on tax } concept of GST

CenVAT - (Ganga)
↳ Revenue from manufacture - To centre

VAT - (Yamuna)
↳ Revenue from sales - To state.

under GST

Ganga & Yamuna merges - Tax is neither on Manufac. nor on sales but on $\boxed{\text{ENTIRE SUPPLY CHAIN}}$

Manufacture ⟶ Consumer

DESTINATION BASED TAX

$\boxed{\text{ITC}}$ at every stage of supply chain - $\boxed{\text{NATIONAL VAT}}$ - GST
⇓
At each stage tax is only on value added

DUAL GST

1] Canada
2] Brazil
3] India

All other countries have single GST

2 Main Apprehensions of $\boxed{\text{State}}$ - Crying Baby

Loss of Revenue

Loss of Autonomy

ALL INDIA GST

Recomended by $\boxed{\text{Khelkar Committee}}$ in 2004 set up for Implementation of FRBM Act, 2003 (Fiscal Responsibility & Budget Management). Acc. to this comittee, an ALL INDIA GST would mean the biggest Revolution in India's Indirect tax structure since independence. Such a tax will have several merits as follows:

It will reduce the huge cascading burden of multiple indirect taxes of centre & states on the final consumer.

Result in lower prices due to lower Cascading

Increase consumption & demand due to lower prices.

US ⇒ 22% of world GDP

↳ Doesn't have GST. It has only SALES TAX (6-8%)

CANADA ⇒ 13% GST.

$\boxed{\text{E-WAY BILL}}$ — (?)

-> 10km, 50,000 worth goods

GSTN - Crashed in August

[1 July - only implemented]

E-way - collapsed October, Jan - all deadlines

⇒ Exporters are the most affected by GST.

≈ 2L crores - ITC pending

BEST GST COUNTRIES

Canada, New Zealand

2016 - Malaysia got GST - only country to have clause $\boxed{19}$ - problems - Authoritarianism.

- Economic times Article

Increase Investment

Reduce cost

Increase production, productivity

Increase GDP

Raise Tax-GDP Ratio

Bring down fiscal deficit.

Improve India's competitiveness

Make India one common market with seamless movement of Goods & Services

Integrate Indian economy with rest of the world

Broaden India's tax base &

Have ONE COUNTRY, ONE INDIRECT TAX

According to this comittee, not a single Indirect tax should be left out of the orbit of GST.

Taking note of these recomendations, the Govt. set up an EMPOWERED COMITTEE of STATE FINANCE MINISTERS (2007) entrusted with a task of convincing states to adopt GST & bring about consensus ~~in~~ btwn centre & state.

As a result of efforts of this comittee, a BLUE PRINT of GST was prepared in 2015 incorporating various pre-conditions and demands of states to adopt GST.

This blue print was placed in both houses of Parliament in form of GST BILL.

After the passage of this bill in both houses & after the nod of the President, GST ACT was passed in AUGUST 2016.

Under the GST ACT,

An Apex decision making body was formed, called GST COUNCIL headed by UNION FINANCE MINISTER with members - Finance ministers of all States & UTs, so that any decision of council must have 2/3rd majority.

RNR - Revenue Neutral Rate

↳ similar revenue pre & post GST.

TN - 28% + 15% on Cinema

4 slabs - only in 4 countries - India, Pak, Italy, Ghana

28% on 4 goods:

- Luxury goods
- White goods
- Sin goods
- Capital goods

CESS over 28%

Cess - not shared with state as per Constitution

e-Way Bills

e-way bills ?

7/7/18 - Newspapers
⇒ Movement of goods/week - ₹.15000 ↓ To - 4000 ₹. through e-way bill.

Any movement of goods beyond 10 km and with value of G & S > ₹.50,000, inter-state & intra-state requires the generation of e-way bills.

KARNATAKA - 1st State - intra state e-way bill.

States have started dismantling of entry-check points.

Enables freer movement of Goods — Raw materials & fin. goods.

↳ Contributes greatly to ONE NATION, ONE MARKET, ONE TAX.

compromise / composite tax scheme

Traders ⇒ 20 lakh - 1 crore

↳ Not under GST

Trader - 1%

Man - 2%

- 5%

↳ Bcos small scale dealers / informal sectors don't get ITC (Input tax credit) properly as formal sectors get it.

↳ They, however, can come under GST when they wish.

Reverse charge mechanism:

For minimal evasion.

₹ 2000 crores evasion in GST detected - Fake ITC claims invoice

Get from customer but not pay

RNR (Revenue Neutral Rates)

Revenue post GST $\neq$ Revenue pre-GST

GST principal objective
- Cascading burden
- ↓ prices, ↑ consumption

⇓

But actually not happening.

$\underbrace{\text{28\% slabs}}_{\text{must go}}$ — $\underbrace{\text{1-to 15\% cess}}_{\text{must be uniform}}$ ⟹ ARVIND SUBRAMANIAM.

3rd component of Fiscal policy

BORROWINGS OF GOVT reflected in the form of deficits in the union budget every year.

There are 4 deficits reflected in union budget every year namely:

1. Revenue deficit
2. Effective Revenue deficit
3. Fiscal deficit
4. Primary deficit

These deficits can be understood only if we understand the composition of union budget which is explained as follows.

Composition of Union Budget:

The union budget is presented every year under two heads of account:

REVENUE account

CAPITAL account

Revenue account of the budget also known as CURRENT account shows Govt's current income throughout the year. (i.e) what government earns on a day to day basis throughout the year. Similarly, Revenue account also shows CURRENT EXPENDITURE (i.e) what govt. spends on a day-day basis throughout the year.

Hence, Revenue account shows on one hand Revenue receipts (current day to day receipts) & on the other, Revenue expenditure (current day to day expenditure). The composition of R. receipts & R. expenditure is:

Revenue Receipts	Revenue Expenditure
I. Account ONE:	II. Account TWO:
These receipts comprises tax & non-tax receipts.	It comprises Developmental & Non-Developmental expenditure
- TAX RECEIPTS are by way of direct & indirect taxes.	DEVELOPMENTAL Expenditure is on providing various social & economic

NON-TAX receipts comprises mainly fees, fines, user charges, interest income on loans given by govt, dividends of PSUs, profits of departmental undertakings (of Railway, Post & Telegraph), Grants received from time to time from various sources, Income from mint.

services on day to day exp. health, education, Transport, communication, exports promotion, irrigation, flood control, services to Agri, industry & a whole lot of such services which are essential for smooth functioning of economy.

NON-DEVELOPMENTAL expenditure
L&O, Defence, Civil admin, Interest payments, subsidies,
New pension scheme, 2004 ← Pensions, grants to states & other sources etc..

Capital Account of budget also shows capital receipts on one hand & capital expenditure on other hand.

Capital receipts are not day to day but long term & lump sum receipts most of which may have repayment obligations.

Capital expenditure is not day to day but long term & lump sum expenditure.

The composition of Capital receipts & Capital expenditure are

III. Account THREE

CAPITAL RECEIPTS

These mainly comprises of following items:

a) Disinvestment

b) Sale of its assets by Govt.

c) Recovery of past loans

d) Borrowings ~~from~~ by Govt (both internal & external)

2017-2018

Taitely collected ≃ 73,000 crores through disinvestment

– Air India issue

IV. Account FOUR:

CAPITAL EXPENDITURE

This comprises mainly of foll. items:

a) Infrastructure (social & Economic)

b) Repayment of past loans.

c) Loans given to states & UTs.

① REVENUE DEFICITS (RD) ⇒ (RE−RR) II−I

This deficit shows that Govt. is not able to meet its day to day expenditure with its day to day income. Even for this expenditure it may borrow & this borrowing is for CONSUMPTION, rather than for productive purposes.

The centre has been running high revenue deficit year after year & even in 2018-19 UB, it is projected to ≃2% of GDP.

A major reason for this deficit year after year is NON-DEVELOPMENTAL EXPEND., Most of which is not only socially & economically compulsive but also inevitable on the country's security & defence.

② EFFECTIVE REVENUE DEFICIT (ERD)

ERD = RD − Those grants given to states which are used by states for developmental purposes.

This concept was given for the 1st time in the union budget for 2012-13 by the then Finance Minister Pranab Mukherjee

③ FISCAL DEFICIT (FD)

FD = TE − (RR + Non debt creating capital receipts)

= (II + IV) − (I + a, b, c of III)

FD = Borrowings by Govt

High fiscal deficit has following implications on Indian economy:

1) As govt. borrows more, its INTEREST BURDEN rises which increases RD (Revenue Deficit) bcos interest is paid of Revenue receipts.

ii) Higher borrowings by Govt brings down

CPI − 46% weightage on food items, so MSP ↑ will ↑ FD & Inflation

Ayushman Bharat:
— IMA told cost enough
— NITI Ayog investigate

its CREDIBILITY & more importantly its GLOBAL CREDIT RATING bcos of which it may end up borrowing at higher rate of interest from abroad.

2016-2017
FD - 3.3%
RD - 1.8%
= 1.5%

iii) As govt. borrows more, it borrows within the country from Banks & financial institutions against securities to that extent it leaves less with banks to lend to the corporate sector which in economic jargon means that Government CROWDS OUT the private sector. As such, private sector borrows from other sources at higher interest rates so that corporate sector goes up leading to inflation.

iv) High FD is largely due to high RD which means that a large part of borrowing is used for NON-DEVELOPMENTAL purposes so that while it may create income & demand, it doesn't result in output which has potential to cause Inflation.

Due to implications mentioned above, a high FD in India is treated as an ALARMING SITUATION.

(4) PRIMARY DEFICIT (PD)

PD = FD − Interest payments

A low PD is not a healthy sign bcos it shows a large part of FD is due to

2017-2018 UB
PD = FD (5,46,000 cr) − 5,23,000 cr

interest payment of loans taken in past which have their impact in the budget in current year.

On other hand, a high PD will show that FD ~~is~~ may be due to some STRUCTURAL & PRODUCTIVE factors rather than just interest payments.

FRBM (Fiscal Responsibility & Budget Management) ACT, 2003

It was passed in 2003 & its principal objectives were:

"That the Government adopts a path of FISCAL CONSOLIDATION by being responsible, Accountable & Transparent in its fiscal operation (i.e) in managing its Revenue & Exp."

Certain rules were laid down under the act to be followed by Govt for achieving Fiscal Consolidation. 2 of the most important rules were:

'Statistics are damn lies'

2017-18 ⇒ FD - 3.5%

i) Beginning 2004-05 & Ending 2008-09, the govt. shall bring down its RD from over 2.5% in 2004-05 to 0%

ii) Beginning 2004-05 & ending 2008-09, the govt shall bring down its FD by 2008-09 to not more than 3% of GDP.

Govt shall cease to borrow from RBI from 2006.

This act has been reviewed by N.K.SINGH committee (chairman of 15th FC) which submitted its report in early 2017. Major recommendations of this committee are:

i) Govt. should bring down its RD from 2.1% in 2016-17 to 0.8% by 2022-23.

ii) Govt's FD should not be more than 3% (of GDP) for 3 years (17-18, 18-19 & 19-20). Thereafter it should be brought down by 0.25% each year so that, by 2022-23, it is not more than 2.5% (of GDP).

iii) Total outstanding debt of the Govt. should be brought down from 70% (of GDP) in 2016-17 [49% of centre & 21% of states] to 60% (of GDP) by 2022-23 [40% of centre & 20% of states]. Acc. to the committee, the main focus of the act should shift from FD to total outstanding debt because Global Credit Rating Agencies adopt Total debt as the principal criteria and not FD.

iv) There should be an 'ESCAPE CLAUSE' which would provide flexibility to Govt to overstep its targets in the

not >0.5%.

event of abnormal conditions in economy (in case of war), structural reforms resulting fall in GDP, natural calamities etc.

There should be an autonomous body set up by govt 'FISCAL COUNCIL' for constant monitoring of fiscal situations preparing multi year fiscal targets & making recommendations from time to time.

The act should be renamed DEBT MANAGEMENT & FISCAL RESPONSIBILITY and Rules.

The report has been since accepted by government.

GOVT. EXPENDITURE

- REVENUE EXPENDITURE
  - Consumption expenditure
- CAPITAL EXPENDITURE
  - Exp. on Investments.

This distinction was for the 1st time made in Union Budget 2017-18. Prior to this, there was distinction btwn.

- PLANNED EXPENDITURE
- NON-PLANNED EXPENDITURE

This was abolished after the completion of 12th FYP on 31st Mar, 2017. Hence, budget for 2017-18 was the 1st budget to distinguish btwn Revenue & Capital expenditure.

With abolition of PC & setting up of NITI Aayog, the entire approach to govt. exp. has shifted from centralised approach of PC to Bottom-up approach of NITI Aayog based on CO-OPERATIVE FEDERALISM. From time to time, NITI Aayog makes recommendations for development agenda of govt. including measures to govt. expenditure. In this regard, it has recommended closing down of 30 sick & loss-making PSUs.

It has also recommended cutting down the no. of autonomous organisations under UG.

NITI Aayog has also been entrusted the task of preparing a realistic cost structure for AYUSHMAN BHARAT program.

Govt. expenditure has been rationalised in the last decade by way of
- DBT for subsidies;
- Pension reforms;
- Reducing oil subsidies by making petroleum products' prices market determined.

⇒ In context of govt. expenditure, the govt. has adopted the technique of OUTCOME BUDGETING since 2004-5.

Outcome Budgetting

Outlay on different projects is evaluated on the basis of their qualitative outcome to justify every penny spent on the project.

Ex: If 500 Cr are set aside for construction of 2 Health centres in a district, its qualitative analysis in outcome budget has to be carried out on the basis of:

- Decline in MMR
- Diseases & epidemics
- Overall improvement in health indices of ~~go~~ district.

Every govt. department has to prepare Qualitative outcome for various schemes.

⟹ Some countries adopt Zero Based Budgetting

Zero Based Budgetting

Each year's budget is prepared assuming that there was no budget in the past (i.e) Base was zero, so as to prepare an unbiased budget on merits of each item of expenditure.

Ex: UK, SWEDEN & a few others.

Gender Budgetting

Started in India 2004-05; 1984 - 1st by Australia

Every min^ry & dep, must keep view of sensitivities & impact ~~of~~ on social & economic factors of ♀.

FOREIGN INVESTMENT

DIRECT — PORTFOLIO

(FDI) — (FPI)

DIPP – Nodal

$\boxed{FDI}$ → A foreign company, generally an MNC will invest in a country, say INDIA with the objective of manufacturing a product, providing some service, engaging in construction or merely giving Tech to India.

Prominent ex. of FDI in India

Manufacture: HUL; NESTLE India; HERO HONDA; MARUTI SUZUKI; CADBURY India; COLGATE Palmolive & etc.

They manufacture all from Consumer goods, capital goods, automobiles, machinery, locomotives etc.

Services: Telecomm (VODAFONE); Aviation (TATA Singapore airlines)
Insurance (BAJAJ alliance; TATA AIG; ICICI prudential, BIRLA Sunlife
Banking (HDFC 74% FDI, ICICI 61% FDI)
Courier; Shipping & a host of such services in which MNC are investing in India

1986-87: 7th FYP

VP Singh tried 0 bugetting.
- Severe drought
- Disint of USSR
- Gulf deportation of Indians

Hence zero-budgett was given up.

INCREMENTAL BUDGETING Vs ZERO-BASED BUDGETING

Based on merit.
- entire budget need not be based on 0-based as it can't be applied to social schemes, salaries, etc..
- To rationalize govt. expenditure.

Construction : Japanese companies engaged in Smart City;
MNCs engaged in modernising airports;
Construction of Highways, Ports, Bridges, etc.

Hence FDI is the best form of foreign capital.

Because a foreign company invests at its own risk w/o anything in return given by the recipient country.

It is considered the best also becos it is long term in nature as MNCs have the intention of staying in here for a long time, investing & making profits & sending part of their profits to parent company

It is considered best also bcos it gives several benefits to recipient country like: latest tech; precious forex; export promotion; employment generation; latest business acumen; Increase in productivity & production & above all infusing a spirit of competition among domestic industry.

UN report 2018:

To 10 countries in FDI:

1. CHINA - $70 Bn
2. BRITAIN - $65 Bn
3. USA -

10. INDIA - $22 bn

FPI

A foreign investor, generally FII's invest in a country's stockmarket by investing in shares, bonds & mutual funds of various companies in country.

The principal objective of FII is to make capital gains in the stock market so that as & when they find a country's stock market less attractive, they have a tendency to move to other country's stock market in search of quick profits.

As such, unlike FDI which is long-term, FPI is essentially short term & has the potential to cause volatility & turbulence in financial markets due to which FPI is popularly called 'HOT MONEY' (or) 'FLY BY NIGHT MONEY'

1992

Bombay club

↳ Top industrialists

→ Go slow in opening the economy to FDI to give time to develop competitiveness.

INDIA's FDI POLICY

2 principal features (aspects) of India's FDI policy:

(i) Routes of FDI (ii) Caps on FDI.

ROUTES OF FDI:

3 routes to attract FDI into India

① Automatic route ② Govt. approval route ③ NRIs

Automatic route: It implies that a foreign country wishing to invest in India doesnot require to obtain a prior approval of any agency before investing. It can straightaway come to India & bring its capital that it wants to invest in India & it has to inform only to RBI within one month of bringing its capital & again within one month of issuing shares to non-residents. The GOI notifies from time to time all those sectors in which a foreign company can invest under the automatic route. This info can be accessed by a foreign company to decide in which sector it wants to invest in India under automatic route.

In recent yrs, keeping in view EDB & MII initiative, more and more sectors have been brought under automatic route to the extent that 92% of total FDI in India at present is attracted via this route. (Before June 16'-55%)

Govt. Approval Route: It implies that a foreign company has to seek prior approval before it could invest in India. This was being granted by an APEX BOARD setup in India in 1992 called Foreign investment Promotion Board.

However as 92% of total FDI now comes via automatic route, the board has become redundant & was abolished in 2017. As such approval is now to be granted by concerned Ministry or Department.

NRI Route: It implies that GOI provides some incentives from time to time in selected sectors to NRIs to invest in India. It also organises Pravasi Bharatiya Diwas every year to attract NRI investments.

CAPS IN FDI:

It implies ceiling of participation of a foreign company in the total share capital of a joint-venture enterprise in India. These caps have been fixed at 24% ; 26% ; 40% ; 49% ; 51% ; 74% ; 100%.

CHINESE FDI

Many from NRC, mostly settled in Hongkong.

But NRIs don't have good image of India.

I. FDI cap restricted upto 49% → ≤49% shareholding is that of a foreign company & 51% or more is that of an Indian company in a joint venture enterprise in India.

GOI policy is to restrict shareholding of foreign company upto 49% in sensitive sectors like: DEFENSE; INSURANCE; etc.

Ex: i) FDI in Defence ≯ 49%.

ii) FDI in Insurance companies like:

BIRLA Sunlife ; BAJAJ Alliance ; ICICI Prudential & others

share holding of Indian companies is ≥51% & that of for. companies is ≤49%. - Sensitive ensuring lives & health of ppl & if the track record of a foreign insurance company is not good in parent country, it can be a dangerous scenario if the company collapses in its own country & all those who have insured in this company are victimised.

iii) FDI in Aviation sector ≤49%.

II. FDI upto 100% → Entire capital is by foreign company w/o any Indian Joint Venture. Generally it may be permitted in such sectors in which India has scarcity of resources like > INFRASTRUCTURE

> Brownfield Airport

> Brownfield PHARMA.

& those sectors which req. latest tech & technical know-how.

⇒ Every country has caps on FDI bcos Caps provide checks & Balances in a country's overall FDI policy.

Moreover FDI caps are not static & can be raised or lowered depending upon changing economic & political conditions in the country.

DEMERITS OF FDI

i) It can threaten a country's economic & political sovereignity.

ii) Foreign companies may often indulge in practices of cut-throat competition.

iii) Foreign companies may bring to a country technology which is already outdated in their parent country.

iv) Foreign companies may take out of the country forex more than what they bring into the country. Ex: By way of profits, dividends, technical fees, Royalty, etc.

v) Foreign companies may prefer to invest more in sectors which give them quick returns rather than in sectors with long gestation period.

vi) Foreign companies worldwide may indulge in TRANSFER PRICING practices.

OFFSET CLAUSE

in Rafale deal → Components can also be later manuf. by that tech & sold.

→ Tech will be given which can be used to earn forex later.

1977-78

Janata party

George Fernandes (Industry min, former Trade union leader)

— Diktat: All foreign companies must reduce ≤40% & ≥60% to Indian companies. 2 MNCs packed up Cokacola & IBM. Came back after INC came.

Till 1997

→ Not WTO member

6 major agreements

TRIMs:

→ No caps as of how much profit can be taken back.

TATA AIG

collapsed in 2009. But TATA took over.

Insurance

way of life in abroad (Mortgauge).

1994:

only few insurance companies. So we opened but with caps

Sovereign Wealth Fund (SWF)

DUBAI, CHINA, TAIWAN, SINGAPORE,

MB. Salman — to setup largest SWF.

Huge forex is idle (India - in US & UK securities - safe)

other countries setup to invest in Africa, etc.

Montek Singh Ahluwalia

SWF for India.

But due to instability of Imports & Exports it may be risk for us.

In defence

Govt. can increase 49% → 100% but the 51% will go via Govt approval route

1951-91: Indian FDI policy was Ad-hoc (no guidelines)

Economy -02

→ Only after 1993 - FDI
Nehru's statement in 1st plan document:
we'll not look down upon FDI (EIC) & will attract them when in need.

→ 1951-75.
Huge criticism of India's FDI policy. We attracted only in tourist areas.

USA
NSA clearance needed for Infra FDI.
India is also now following it.

FDI MULTI-BRAND RETAIL

There has been a debate in India whether to permit FDI in Retail while permitting Global Retail giants - like Walmart, Tesco, Carrefour, - to set up their stores in India.

2 Major Arguments AGAINST:

i) The Livelihood of small retailers.
ii) Unemployment it may cause.

\# ICRIER

FOR: A study conducted by An Apex Consumer Org.ⁿ points out that in a diverse country like India with a huge 'unorganised' sector & more than 60% population in Rural areas, these global giants will not have adverse impact on small scale retailers. Also because these retailers enjoy inherent advantages for consumers like ✓Proximity ✓Convenient Timings ✓Catering to local tastes & above all ✓selling goods on credit.

On the other hand, the economy will have several benefits if FDI in multibrand is permitted. These benefits could be

✓ Latest technology – including Cold chain tech from farm to consumers.

✓ Diversification of Agriculture

✓ Boost to food processing industry

✓ Interaction b/w Agriculture & Industry

✓ Greater employment opportunities

✓ Precious Forex

✓ Integration of Indian economy with rest of the world.

✓ Besides it will generate a spirit of competition among domestic retail giants.

The govt. finally opened this sector in <u>2012</u> permitting <u>FDI upto 51%</u> with some <u>PRE-CONDITIONS</u>:

① They must bring in a min. amount of initial forex.

② Some % of products sold in these stores must be obtained from small scale sectors.

③ Some % of employment must be reserved for unemployed youth

④ Interest of farmers must be safeguarded in the event of CONTRACT FARMING arrangements.

The consumers are going to be the biggest beneficiaries in terms of the best quality & hygiene conforming products as global reputation of these stores is at stake.

100%	Nike – <u>Single Brand Retail</u>
51%	All brands <u>Multi Brand Retail</u>
100%	Bharti – Walmart <u>Whole sale Trade</u>

$\boxed{\text{FPI}}$

Participatory / P-Notes → Issued by FIIs to such of the foreign Investors who wish to invest in the Indian stockmarkets; But donot wish to be regulated & registered by SEBI.

[Physical shares are with FIIs while only details of purchased shares are in p-notes given to foreign Individual Investors]

In 2007, almost 50%+ of total Indian shares of FII's & hence SEBI brough 10% condition, so now only ~9%.

GDR (Global Depository Receits) → We started in 1990s.

Indian firms sell shares in foreign stock markets through a Depository mechanism, the trustee of that Depository will issue Depository receits with value of share. So it will be in € or $ there but its value is in ₹ (Rupee).

$\boxed{\text{FPI}}$ - Sources

I. FII

II. ADR & GDR

III. NRIs.

INFLATION

① Def ② Measurement ③ Causes ④ Measures to control ⑤ Consequences

① Definition:

Inflation is a situation characterised by a sustained, unchecked rise in the general price level observed over a period of time.

② Measurement:

Inflation in any country is measured on the basis of a PRICE INDEX. In India it is measured on basis of WPI & CPI.

The methodology used for constructing each of these indices is:

* WPI - wholesale Price Index → This index is constructed on a Monthly basis by the OFFICE OF ECONOMIC OFFICER, DIPP (DPIIT-new name), M. of. Comm & Industry.

The base year used in constructing index is 2011-12.

The index takes into account 697 commodities whose Price data is collected from Major Wholesale Markets in India.

This index doesnot include SERVICES at all. These 697 commodities are divided into 3 broad groups as follows:

[a] Manufactured Goods (64%) [b] Food & Primary articles (23%) [c] Fuel, Oil (Mineral), Electricity (13%)

The highest weight is assigned to Manufactured goods which is -64% followed by Food & Primary articles -23% & rest 13% to [c].

Thus whenever prices of manufactured goods undergo a change (↑ or ↓), this is adequately reflected in the index bcos their wt is 64%.

On other hand rising prices of [b] may not be adequately reflected as their wt is only 23%, because the index is weighted average of prices of 3 groups.

As such, inflation based on WPI doesnot adequately reflect food inflation. However WPI inflation is used extensively by STATISTICIANS, CORPORATES & BUSINESSES to reflect the prevailing rate of inflation.

* CPI (Consumer Price Index) ⟶ On Monthly basis by CSO. The base year is 2011-12. This index takes into account 908 commodities whose price data is collected on the basis of Consumer Expenditure Surveys conducted by NSSO.

As such, price data for this index takes into a/c Retail Prices. This index also includes selected SERVICES like Health, Edu, Banking, Transportation, etc. These 908 commodities are divided into foll:

[a] Food & Beverages (46%) [b] Clothing & Footwear (7.) [c] Housing 10% [d] Fuel, Light, Electricity

[e] Paan, Tobacco & other intoxicants (2.4%) [f] Miscellaneous (28%)

As such, this index adequately captures Food Inflation in country

The RBI has adopted this index to achieve the target of Inflation called "Inflation Targetting" adopted by MPC since 2016 as 4% Medium term target of Inflation with 2% + or − in short run. RBI constantly monitors CPI inflation to ensure that it doesnot exceed this target & treats CPI inflation as Headline Inflation.

$$\frac{\text{change in value of index}}{\text{value of last month index}} \times 100$$

$$\text{Ex: } \frac{166-160}{160} \times 100$$

More often the divergence b/w the CPI & WPI may be due to factors like:

> Composition of Index
> Wts. assigned
> One using WPs & other RPs
> One including Services & other excluding Services

PPI (Producers Price Index) - Other Countries

Most advanced countries have given up the use of WPI & have switched over to PPI. This index is constructed on the basis of prices received by producers for their commodities before these commodities reach the market. Hence these prices donot take into account MARKET COSTS which are merely transportation costs & Indirect taxes. Hence the index is constructed on basis of Producer's Prices with objective that any rise of prices at this level can be addressed by taking Corrective Measures so that impact of rising price is minimal on consumers.

In INDIA, an attempt has been made to construct PPI for which an expert committee was set up in 2014 under Soumitra Choudry. The committee observed that in a country like India ~~being a country~~ with a huge and fragmented unorganised sector, may not be possible to collect a RELIABLE PRICE DATA at producer's level due to which it may be difficult to construct a realistic PPI. As such, the committee recommended that Existing WPI can be treated as PPI as:

$\boxed{\text{WPI} - \text{indirect taxes} + \text{Subsidies}}$

CORE INFLATION ⟹ Inflation which doesnot take into account Inflation in 2 groups of articles (i.e) Food & Fuel because their prices are not policy determined but depend on external factors. Hence Core inflation means Inflation confined to Non-Food & Non-Fuel Articles. (Dec: 2019 — Core infla > WPI & CPI infla) (Health & Edu)

③ CAUSES :

Inflation in any country can be caused by 2 Sets of factors

I- DEMAND PULL → those due to which there may be overall increase in demand for G & S.

II COST-PUSH → Those due to which there may be increase in cost of production & distribution and/or a shortfall in supply.

ECONOMICS

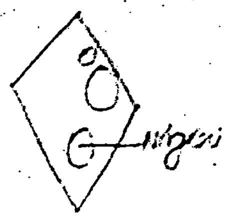
Class-1 FOOD PROCESSING & RELATED ISSUES - HANDOUT

GS Qn → 1 to 10 = 150 words (10 marks)
→ 11 to 20 = 250 words (15 marks)

In answers — Focus more on example explanation than Definition/Concept.

Agro-climatic Zones (ACZ) – 127 in India

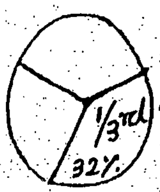
Ex: o Tea – (20°c - 33°c) — Ideal Temp for cultivation
– (>35°c ; <10°c) — Unsuitable
o loamy soil
o Precipitation ⇒ >150 cm rainfall



⇒ Based on factors like Temperature, soil, precipitation, climate, we identify areas suitable for cultivation of certain crops. These are called agro climatic zones.

⇒ It has been given by NARP (National Agricultural Research Project)

Food Market in India:



8.8%

≃ 14% – 2017 – share in manufacturing

≃ 21% – Rate of growth of sector in 5 years (last) - consistently

Labour Intensive Industry:

The use of labour per unit of capital in these Industries is relatively high.

Food processing	Automobile ⇒ Nowadays Max. Mechanised
capital = 1	Capital = 1 — Esp in GURUGRAM, TN
labour = 5	Labour = 2 — (Invent of AI)

India waste in Agricultural produce:

- Food processing in India: ≃ 10% (avg) ⇒ Range 2–35%
  (Fruits & veg. = only 2%)
  CHINA = 25%
  USA = 65%
- Wasted Fruits & Vegetables: ≃ 5 to 30%.
- Wasted Food Grains: ≃ 5 to 7%.
- States with max. losses: = WB; GUJARAT; BIHAR; UP
  ↳ Huge opportunities for them as their output is very decent
- Post-Harvest Loss:
  ₹ 92,000 Crore in INDIA
  - AVOIDABLE LOSS: 60%, 55,000 Crore
  - STORAGE LOSS: 40%, 37,000 Crore

Fact: MGNREGA's 2017 Fund = 92000 Crore exactly
↳ We can fund such programs without tax payers money.

Definition of Food Processing:

Food processing comprises of 2 processes:

i) <u>MANUFACTURED PROCESS</u>:- If any raw product of Agriculture or animal husbandry is <u>transformed</u> in such a way that its original <u>physical</u> properties undergoes a change, it is <u>edible</u> and it has a decent <u>commercial value</u>. <u>EX:</u> Maggi, choclates.

ii) <u>VALUE ADDED PROCESS</u>:- If there is a significant value already present and there is no need of manufacturing process, such products also come under processing.
<u>EX:</u> Roasted cashew

Examples:

Value chain in Food processing of Manufactured Food products

INPUTS → PRODUCTION → PROCUREMENT & STORAGE → PROCESSING → RETAILING

- INPUTS ↓ Seeds, Fertilisers, water, etc.
- PRODUCTION ↓ Farmers Individuals/ Groups.
- PROCUREMENT & STORAGE ↓ Warehousing facilities
- PROCESSING ↓ 3 types:
  - Primary - sorting, grading, packaging
  - Secondary - Reshaping
  - Tertiary - Value addition via processing

Constituents of FPI

↳ Country Specific

For INDIA: 6

1. Fruits & Veg (Rank 2)
2. Milk products (Rank 1)
3. Meat & Poultry [Cara Beef - 1; Eggs - 2; Poultry - 3; Goat meat - 2; Beef - 3]
(range R-1 to 3)

④ Food Grains

↳ 277 Mn Tons

⑤ Consumer Foods

↳ One of the fastest in the world

⑥ Marine products

↳ WB; AP are top producers;

↳ KARNATAKA; KERALA; GUJARAT follow.

SCOPE OF FPI IN INDIA / ADVANTAGES OF FPI IN INDIA

I) Reduce post Harvest losses:

Only 10% processed

92,000 Cr wasted in Post Harvest Loss

We have to increase the processing level from 10% and minimise the post Harvest losses amounting ≃ 92,000 crores. This can come about only with the Development of Food Processing Sector.

II) Farmer's Income & Improving Rural Economy:

Programs to increase output of agriculture and Investments in processing lead to more value addition and Increased Bargaining power of Farmers.

But, this will happen only when we develop Food Processing Industry which provides Relevant Market Information about new Technology, demand & Prices. This will enable farmers to reduce their dependency on MSP & get a good value for their product.

↑ Output + ↑ Investment in FPI ⇒ ↑ Value added ⇒ ↑ Bargaining power of Farmers ⇒ ↓ Dependency* on MSP ⇒ Farmers ↑ Income

↑ Output + ↑ Investment in FPI → ↑ Govt. Investment (Crowding in Effect)* ⇒ ↑ Supply chain → ↑ Bargaining power of Farmers

*Only 6% of crops procured under MSP. [Distress sale]

*Crowding out: Govt. displaces private sector in investment.

Crowding in: Both Govt & private sector putting in investment will happen

Farmer producer Organisation (FPO):

Small producers donot have high volumes of input & output. So, they are unable to take advantage of Economies of Scale. Through groupings like FPO, the farmers can increase their Bargaining power & distribute the profit in a fair manner.

iii) Forward & Backward Linkages

Backward Linkages ← Raw Materials — FPI → Forward Linkages

Backward Linkages		Forward Linkages
↑ FPO		↑ Market
↑ Individuals	← Raw Materials — FPI →	↑ Supply chain
↑ Transport		↑ Branding
↑ Storage		↑ Advertisement
↑ Co-operatives		

↑ Rail Factories

↑ R&D

Backward Linkages ← Raw materials ← TRANSPORT MONO RAIL → ↑ Tourism, ↑ Transport of products — Forward Linkages

A Forward Linkage is created when investment in a particular project / sector encourages investment in subsequent stages of production

A Backward Linkage is created when a project / sector encourages investment in facilities that enable the project to succeed.

IV) Investment, Skill & Technology Infusion Potential

Food processing constitutes 13% of export & it is the 13th Largest recipient of FDI in India. 6% of total industrial investment is happening in this sector. There is a lot of scope of 'crowding in' & 'Multiplier Effect' through Forward & Backward Linkages.

Why Umbrella scheme? $\boxed{\text{INTEGRATION}}$

If only output ↑, wastage will be there; also need Transport ↑

Supply chain ← Storage & Warehouses. ← Prevents Rupture of cell wall (happens when temp. is not optimum.) hence protecting Nutrional value.

↳ Market + Branding

SAMPADA (KSY):

✓ Integrating old schemes; to rectify old schemes

✓ New schemes too included.

vii) Migration/Absorption of labour from Agriculture & Industry:

Solution to DISGUISED LABOUR/EMPLOYMENT

↑

Marginal Productivity = Zero

↳ Role of each individual involved.

v) Contribution in Economic Growth:

→ Prior to 2009 & 2010; Growth of Manufacturing Sector exceeded FPI. The output of food grains was > Horticulture.

→ Post 2009-2010: Food Processing Sector has consistently maintained a double digit rate of growth (%) which exceeds Manufacturing growth. Also Horticulture output has consistently outpaced or surpassed the Food grain production.

[Note: Read w.r.t. 2008 - Economic crisis which affected Manufacturing; Industries; Employment; Exports. .]

Scope of FPI in India — Demand Side & Supply Side —

i) Strong Domestic Demand:

Over the period of time, disposable income of Indians have increased, the middle class population has also increased. Moreover the Tastes & Preferences of Indians have moved towards more protein & Fruits and Vegetables. All these factors create strong domestic demand.

ii) Supply Side Advantage:

- ✓ Favourable Climate
- ✓ Livestock Base
- ✓ Long coast line (
- ✓ Economical Labour
- ✓ Raw material
  - abundant & Economical

These create supply side advantages for India.
#127 Agro-climatic zones

iii) Rising Export Opportunities:

India's greater Global Integration; Proximity to labour Market & Increased Global demand — has created export opportunities for India.

iv) Untapped Market:

The fragmented market leads to lower processing and value addition. But, with public–Private partnership at a huge Population Base, there is a great potential to cover untapped Food market in India.

v) Potential Global Outsourcing Hub:

With favourable supply fundamentals like abundant raw material (127 Ag. cli. zones) & economical labour (↑ Disguised labour) along with Govt-support (100% FDI in FPI) can create India as an Outsourcing hub of Processed Food.

[Pulses - Mexico; cereals - Africa can be imported.

vi) Supply chain Infrastructure & Contract Farming:

Firms are increasingly using Contract Farming along with increased level of FDI to boost up Investment in supply chain infrastructure. This presents huge investment opportunities for Indian Industries.

CHALLENGES FACED BY FPI IN INDIA

SECTOR WISE CHALLENGES

Infrastructure
- cold chain
- certified labs

Innovation
- Tech Transfer.
- Demand based Tech.

Skill
- Lack of Training Infrastructure
- Lack of special Training modules

Branding
- Lack of platform
- Lack of Marketing facilities

Access to Credit
- High rate of Interest
- Lack of Venture Capitalists*

Dairy
- ▷ Low productivity
- ▷ High fodder cost

Fruits & Vegetables
- ▷ Perishable
- ▷ Low Value Addition (2%) but Rank-2 in production

Food Grains
- ▷ Storage & Distribution
- ▷ Traditional cultivation

Meat & Poultry
- ▷ Highly perishable
- ▷ Licensing Difficulties

* Venture Capital is an investment made into early stage of a start-up company which has good potential. It is also called as SEED CAPITAL.

CHALLENGES FACED BY MEGA

1. Lack of Economical Credit
2. Private Sector Apathy
3. State Govt. Clearances were difficult to get.
4. Lack of Market Facilities.
5. Availability of 50 acres of land.
6. Smaller units were doubtful of the new concept.

Handout 3.

① Govt. Bond

Bond price = Rs.1000/-
Interest = 2.5%
Rs. 25/year
Tenure = 8 yrs
Interest = 25x8
Rs. 200/-
Total = Rs.1200/-
FIXED
Completely safe

② S.G.B - Sovereign Gold Bond.

BP = Rs.1000/-
Cost of 1gm gold in 2018
Interest = 2.5%
Tenure = 8 yrs.
Interest = 25x8
Rs-200/-
Total = 1500 + 200 = 1700
(or)
= 700 + 200 = 900.
Risky

1gm Gold in:
2018 : Rs.1000
2026 : Rs.1500
or
Rs.700.

Calculated investor ⇒ will split maj. in ① & min. in ②.

NIRAV MODI SCAM / MEHUL CHOKSY

Importer in India needs dollars to pay for import Bill in US →

Scam box
Importer approaches Indian Bank (PNB)
PNB issues LoUs to a foreign bank branch
↓
Foreign Bank branch deposits $ in NOSTRO account of PNB in US
→
Dollars are transferred from NOSTRO account to supplier in US

Y this route? If he takes route of direct transaction from his a/c
- under purview of officials, monitoring
- less chances of manipulation.

So, he chose this route.

• Choices of Bank.

1. Collateral (Margin requirement) — Modi didn't pay anything.
2. Credit Limit assessment — PNB didn't do it
3. 90 days was limit. here [credit period expiry] — He was doing for 7 years - 8 yrs.
4. CBS (Core Banking system) / SWIFT
   ↳ Every transaction live recording
   System of communication (like up)
   Nothing physical / tangible is transferred here, but only info.

LOU is transferred to US bank as msg via SWIFT.
It is a choice to record in CBS or not from itself.
RBI notification since 2016: To integrate SWIFT & CBS.
Record any money transaction based on info in SWIFT.
But PNB didn't

4 Corrupt Bank ppl
1. Talk about LOU
2. Person who sends LOU
3. Manager
4. Guy supposed to integrate - Top management.

NOSTRO account → we call our branch in US (only btw Banks)
VOSTRO account → They (US) call the same in their name.

LOU [Letter of Undertaking]

An LOU is a Bank guarantee which allows the Customer of a Bank to raise money from another bank's foreign branch normally in the form of short term credit. (lue 90 days)

In return for LOUs, Banks ask for Collateral / Guarantee which could be in form of Fixed deposit or other assets.

What went wrong in NIRAV MODI's Case?

i) Loan was extended much beyond 90 days against PNB policies.

ii) Nirav Modi didnot pay the Margin money while procuring LOU.

iii) Credit limit is defined for a borrower while giving LOUs. But, for Nirav no credit limit was defined

iv) Under CBS (Core Banking system), all transactions pertaining to a bank are recorded. But, in this case, LOUs were issued using SWIFT Network (Society for Worldwide Interbank Financial Telecommunication)

As per RBI notifications & repeated reminders from 2016 onwards, all banks including PNB were supposed to INTEGRATE CBS & SWIFT.

But, in this case PNB had not integrated this system.

NOSTRO accounts → Generally held in a foreign country (like USA) by a Domestic bank (like SBI) the account is maintained in a foreign currency (like $).

Suppliers Credit (If Buyer in US & Seller in INDIA)

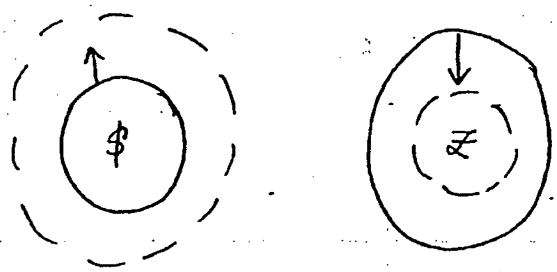
Importer in US needs ₹ to pay for import Bill in INDIA. → Importer approaches US Bank (BOA). BOA issues LOUs to a foreign bank branch (INDIA) → Foreign Bank branch deposits ₹ in VOSTRO a/c of BOA in India → ₹ are transferred from VOSTRO a/c to supplier in India.

ECBs [External Commercial Borrowings]

- External ↑ Foreign
- Commercial ↑ can't be Individual activity
  - ✓ Limitations on use of fund
    - ↳ can't pass on funds to anyone
  - New Investment
  - Capacity Augmentation.
- Borrowings ↑ Tools under this:
  1. Buyer's Credit (Nirav Scam) (also Supplier's credit)
  2. Bank loans – Transparent route
  3. Bonds – No SWIFT here
     etc., ↖ For foreign to buy this, interest must be attractive.

ECB Bonds Types

1. Type-I : 3-5 yrs, $
2. Type-II : 10 yrs, $
3. Type-III : 3-5 yrs, ₹ — (MASALA BONDS)



RBI - India

Dirty floating

Rate of Interest.

ECB is an instrument used in India to help Indian companies to raise money outside India.

Generally, ECBs are permitted for 2 reasons:

1. Fresh Investment
2. Expansion of Capacity

→ ECBs can be of different forms like

a) Buyer's credit (Supplier's Credit)

b) Bank Loans

c) ECB bonds

ECB Bonds:

They are divided into 3 tracks based on 2 criteria:

1) Minimum average maturity period.
2) Denominations.

3 TRACKS under ECB :

- Track-1 : 3/5 years - These bonds are issued in $
- Track-2 : 10 years - These bonds are issued in $
- Track-3 : 3/5 years - These bonds are issued in ₹.
  These are also called MASALA BONDS (or) RUPEE DENOMINATED BONDS (RDB)

Sep 19, 2018 Reforms of ECB

① The manufacturing sector has been given permission to raise funds under Track-1 ~~under~~ upto 50mn$ for 1 year against a normal of 3 years.

② Currently the Indian Banks can only act as ARRANGER of Masala Bonds. But, now RBI has increased their role whereby they can even TRADE in it when the masala bonds are issued outside.

[To internationalise the currency - this is 1st step.
Intn' finance corporation of INF introduced Masala bonds for us.

Depository Receipts (DRs):

MDH Hypothetical Example

1. sharing 3. May/may not
2. Part of Mngmt. Vote

Issues 100 shares in India

Shares are deposited in SBI [LCB-Local Custodian Bank].

US: Overseas Depository Bank (ODB)

Creates DR (in $)

10 shares = 1 DR

100 shares = 10 DRs

DRs are sold to investors in USA.

Questions:

✓ Our bonds there - IDR (Indian)

✓ Their bonds here (US) - ADR (American)

✓ In any other country - GDR (Global)

LCB - can't be a foreign Bank

ODB - must be in that concerned country.

DR is a mechanism through which an Indian company can raise funds from International market.

In this system, the shares of an Indian company are used to issue Receipts in other countries (like US) called as DR.

In general, there are 3 different types of DRs:

1. ADR - American Depository Receipts

An Indian company issues its shares & an American bank will act as ODB. The ODB will issue DRs in US called as ADRs.

2. IDR / BDR - Indian / Bharat Depository Receipts

Here, a foreign company (like US) will issue shares with its local bank and an Indian bank will act as ODB and issue IDRs in India.

3. GDR - Global Depository Receipts

GDR is an instrument to tap the financial market of various countries the receipts are issued by the depository bank in more than one country. In this case, prior approval of M.of Finance has to be taken by company before they issue GDR.

NPA
Manipulating tool to hide some ingenuinge act.

- Indian company can also sell shares by listing in their stock Exchange abroad. But it is tedious & demands huge reputation.
So far, only 2 Indian companies were able to do so.

BLACK MONEY

PANAMA

Mar 5, 2013 – Till this date any individual can take loan upto ₹.1.5 Cr & buy shares of existing company abroad.

→ RBI Notification → Can send this money outside remit it to invest in other countries

Aug 5, 2013 – From now on, anyone could legally
- Invest in new companies
- Buy shares in existing companies

→ Any new company before this date created abroad is illegal.

But CAs opposed as RBI notification didn't mention it.

Dr. RAGHURAM RAJAN:

Accepted the mistake of RBI & told need to examine.

Black Money (BM)

FACTORS LEADING TO BM

1. Socio-Cultural factors
2. Illegal activities

DEFINITION

IT + Criminal Jurisprudence → Illegal Activity
1. Crime: Illegal outcome
   - Drugs trade
   - Financial fraud
   - Kidnapping
   - Murder
2. Corruption

IT Act → Legal Activity, Illegal outcome (Unaccounted Income)

METHODS TO CREATE BM

1. Crude approach
   - a) Out of Book } Karol
   - b) Double Book } Bagh.
2. Sophisticated way
   - Transfer pricing

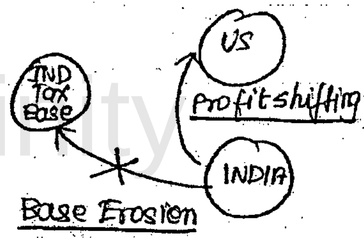
TRANSFER PRICING:

↳ One ex. of BEPS

TRUMPET ENTERPRISES

- Trump-IN
  - Metro-rail project ← Rs.1 Cr. / Rs.1 L — Engine spare parts
  - Profit: 10 Crore
  - Tax: 30% (3 Cr)
  - Transfer Profit: 50, 9 Crore → But US tax = 15%
  - Tax: 2.7 Crore.
- Trump-US
  - Engine spare parts

BEPS



⇒ 60% MNCs in world are ASSOCIATED Companies

Who will decide if this is abnormal or not? Discretion of Indian Authority

How? By comparing it with normal. Ex: France - Engine 64 L

Avg. price of many - ≈ 2 L

Enterprises

ASSOCIATED

a) Direct / Indirect ownership / control

b) Mutually beneficial relationship.

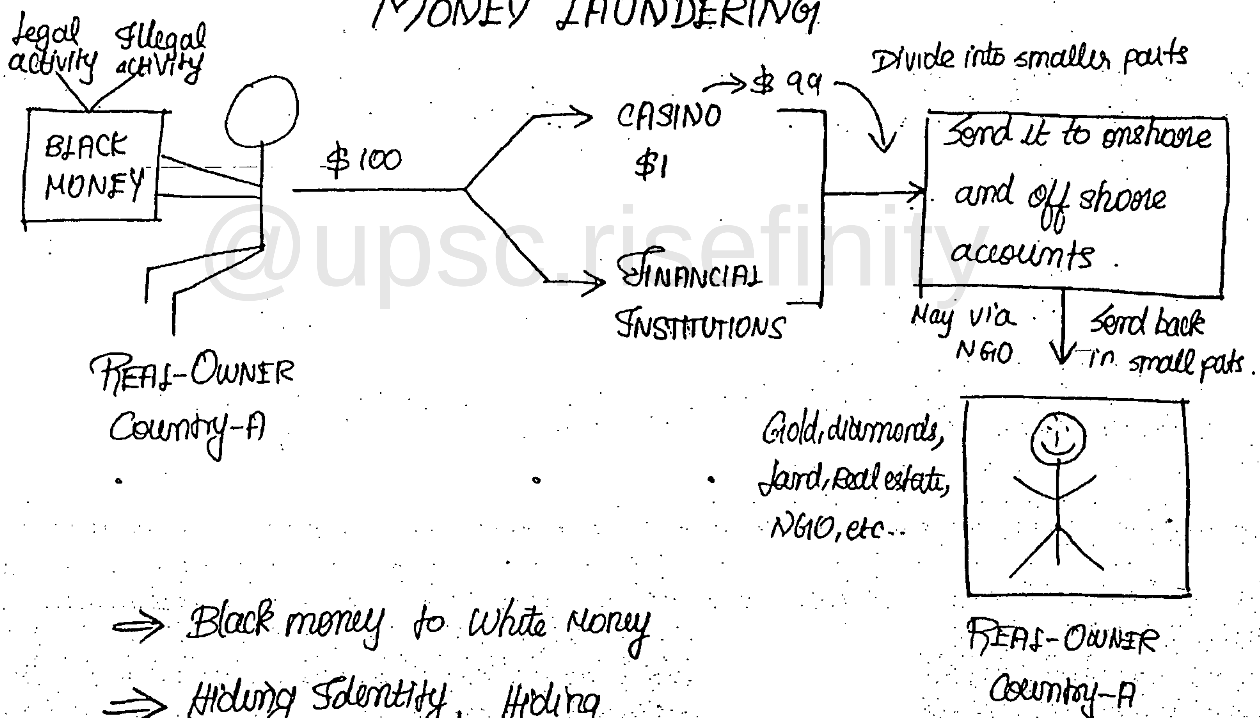
→ Possibility of Transfer Pricing.

UNRELATED

Don't fall in a) or b)

→ Arm's length prices. (Normal market price)

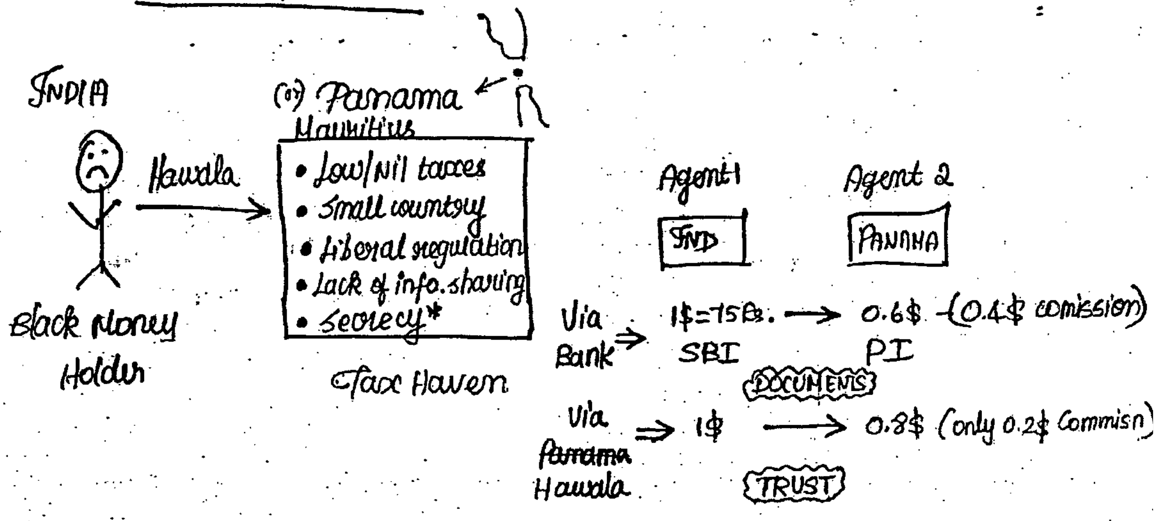
MONEY LAUNDERING



⇒ Black money to White Money

⇒ Hiding Identity of owner + Hiding origin

TAX HAVENS



* Secrecy in terms of Economic activities, accounts of companies, businesses.

PMGKY - Pradhan Mantri Gareeb Kalyan Yojana

Hawala is a system which is almost like a PARALLEL REMITTANCE SYSTEM. It exists & operates outside the traditional banking system.

It is currently a major remittance system across the world. In HAWALA network, money is not transferred PHYSICALLY.

The advantage of Hawala network compared to Banking system is that there is no need to open a bank account under Hawala. Moreover the commission charged under Hawala is less compared to that of Banks for remittances.

DTAA [DOUBLE TAX AVOIDANCE AGREEMENT]

Mauritius ←No Tax Treaty→ India

Mauritius	India
1. Firm X →	2. Invests in India (FII)
	3. Makes profits
5. Returns & pays IT in Mauritius ∴ Double Tax [same tax twice] ←	4. Taxes are paid by X

DTAA : Agreement to avoid taxing same income twice → 1983 [M-IND]

Mauritius ←TAX TREATY→ India

Mauritius	India
1. Firm X →	2. Invest in India
	3. Make profit (by selling shares)
5. No CGT on any firm here ←	4. CGT (Cap. Gains Tax) not imposed on foreign companies

1980s
structural Transformation of Indian Economy
- DTAA
- Liberalisation
- NABARD.

Rate of Growth >5%

Somalia — Mauritius ←TAX TREATY→ India

1. Firm X → 2. Invest in Mauritius firm 'S'-Home company → 3. Invest in India
4. Make Capital Gains But no CGT
5. No CGT → Firm X

TREATY SHOPPING

Mauritius — India

2. Start Firm Y $\xleftarrow{\text{Hawala}}$ 1. Firm X

Re-routing-channel → 3. Invest in India (FII)

5. No CGIT + other taxes also low ← 4. No CGIT

ROUND TRIPPING

Round tripping is a special case of TREATY SHOPPING.

SHELL COMPANIES

1. Firm X → 2. Invest → 3. Profit + No tax

Firm X ⇒ Mauritian — DTAA

⇒ Somalian — TREATY SHOPPING

⇒ Indian — ROUND TRIPPING

Firm X $\xleftarrow{\text{cash}}$

Re-routing

2 Qns:

1). Mismatch btwn Revenue & Bank accounts.

2). Money is not invested by them.

Prominant characteristics of shell companies (From World)

-> Multiple companies on same address

-> Almost negligible manufacturing or services

-> Almost no assets are held

-> They generally don't indulge in economic activities.

-> Mostly indulge in Financial transactions.

India: There is no precise official definition of shell companies in India. Govt. has set up a TASK FORCE under HASMUKH ADHIA to define shell companies & define (devise) a mechanism to identify them.

How to Rectify the loopholes in DTAA?

2003: SC - UOI Vs Azadi Bacho Andolan

SC ruling meant -> In absence of legal provisions, to exploit the loopholes of DTAA, using Treaty Shopping + Round Tripping, would not be considered illegal.

India then started to re-negotiate the existing DTAAs and insert a new clause called as LOB-Limitations of Benefit-clause.

LOB: Under this, a foreign investor who seeks tax exemptions in India should produce documents that they are a resident of that foreign country. LOB clause is attached by Treaty parties in their DTAAs. Benefit of tax concession will be limited only to such entities that produce those documents.

Ex: India & Mauritius renegotiated DTAA in 2017:

New LOB Clause: Under this, some criteria has been est^d to identify shell companies. For instance, if the annual expenditure on operations of company is < 27 lakh Rs* in India, it will be called as a shell company. Also if the company is registered on Stock Exchange of Mauritius or India, it will not be called as shell company.

* The amount depends on the other country. Diff for England [50L]

FATF [FINANCIAL ACTION TASK FORCE]

→ FATF was established in 1989.

→ Aims
  → Anti-money laundering
  → Anti-Terrorist Financing

→ Members: 35 member countries + 2 Regional groups
  * EU
  * GCC [Gulf Cooperation Council]
    – (1) S.Ar, (2) Kuwait, (3) Qatar, (4) UAE, (5) Oman, (6) Bahrain* –

* Acc. to #World Economic Outlook Report,
BAHRAIN is the most vulnuable GCC member in 2010-18
a) V. High debt.
b) Low oil production

→ 2 lists by FATF

a) Grey list: Countries having deficiency but they have a blueprint and commitment to improve the deficiency.

Ex: PAKISTAN (2018)

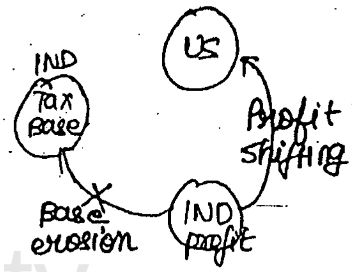
b) Black list: Countries that don't fulfill their commitment.

Ex: N. KOREA; IRAN

BEPS [BASE EROSION & PROFIT SHIFTING]

Ex 1: Transfer Pricing

Ex 2: DTAA



Firms use legal ways [TAX PLANNING] to shift Profit to a low/nil taxation country.

Control mechanism : BEPS Package : 108 members

→ 15 Action plans ; Divided under 4 minimum standards.

1. Harmful Tax Practices like Transfer Pricing.
2. Round Tripping & Treaty Shopping
3. Country-by-Country Reporting
4. Dispute Resolution Mechanism

Ex 3: Preferrential Tax Regime – could be an example of Harmful tax practice under which country gives tax concessions only to foreign companies from a particular set of companies.

Also concessions could be limited only to finance companies & not to service or manufacturing.

Qn. What are the steps taken to tackle Black Money in India?

STEPS → PREVENTIVE 1,2,3,4,5,IV
(To prevent future creation of BM)

→ CURATIVE I, II, III
(To unearth the already existing BM)

(Pg: 10 of H-3)

Domestic Effort

I. Black Money Act, 2015
Jul-sep 2015 ; 60%

II. IDS, 2016 ; 45%

III. PMGKY - last opp.y
50% tax, 25% into PMGK Deposit scheme (will come back later)
If not ↓
85% penalty in future

⇒ Whistle blowers, e-mail

IV. PAN mandatory

International Effort

1. DTAA
2. LOB
3. FATF
4. BEPS
5. TIEA - Tax Info Exchange Agreement

- India's innovation
- Tighter than other 4

BENAMI TRANSACTIONS

Context: Land records are poorly kept, not computerised due to absence of Land Reforms.

Why LR not done? Political, pressure groups, etc. . .

Not every concept here can be answered only from Eco. perspective.

Mr. X	Mr. Y
Paying for land	Owner of Land
If caught:	If caught:
Investigated even if refused	Earlier: Set Free
	Now: Examined. Start of investigation

4 Officers:

1^{st} off: Issue notice
2^{nd} off: Verify notice
3^{rd} off: Implement notice
4^{th} off: Take charge, maintain records & property

- Property will be retained by Govt

Benami transactions – Definition (Dynamic)

① A transaction where a property is held or transferred to a person but has been provided by another person.

② The transaction is made in fictitious name.

③ The owner is not aware of and denies the knowledge of ownership of the property.

payments
④ The person providing consideration for property is not traceable.

The punishment for Benami transaction is imprisonment upto 7 years & a fine which can go up to 25% of the fair market value of the property.

This act prohibits the Recovery of Benami property by the real owner. The Govt. can confiscate the benami property w/o paying any compensation to any party.

It provides for 4 Authorities under the Act:

1 – The Initiating Officer who issues notices

2 – Approving authority who approves notices.

3 – Adjudicating authority – examines details of case.

4 – Administrator – takes care of property after it has been taken over by govt.

Apart from these, there is a provision for an APPELLATE BODY to hear appeals against the decisions under act. The appeal against Appellate Body lies at the High Court.

DEMONETISATION

Def: Demonetisation occurs when a currency ceases to have legal tender. In this case, currency is stripped of its legal tender status.

Demonetisation usually occurs when there is a change of National currency. In such case, old currencies are replaced with new currencies.

India is a truly unique case where demonetisation was carried out not to solve an economic crisis but as a POLICY TOOL aimed at tackling issues like Corruption & BM.

Demonetisation is like an Extreme form of Monetary Policy Tool in the nature of CONTRACTIONARY MONETARY POLICY which is rarely used.

Aims

- ✓ Corruption
- ✓ Counterfeit Currency / FICN [Fake Indian Currency Notes]
- ✓ Terrorist Financing
- ✓ Black Money

2011-15	2016
₹.167 Cr FICN recovered	₹.400 Cr FICN recovered

FICN

As per RBI → The FICN detection in 2016 was 20% higher w.r.t. 2015.

→ Rs.500 & Rs.1000 FICN almost doubled in 2016 compared to 2015.

Terrorist Financing

As per RBI → 2011-15. All currency supplied ↑ by 40%.

→ ₹.500 ↑ by 76%.

→ ₹.1000 ↑ by 109%.

Operation Clean Money under Black Money

a) OCM-I: Nov 9-30 2016 ; e-verification of cash

b) OCM-II: Identify BM in banks & divides indiv. in 4 categories

$\underbrace{\text{1. High risk} \quad \text{2. Medium}}_{\text{ED - Aggressive INVESTIGATION}} \quad \underbrace{\text{3. Low risk} \quad \text{4. Very low risk.}}_{\text{NOTICES}}$

Helicopter Drop of Money : - Theoretical, none has done

- by Milton Friedman in 1969

It is an aggressive form of EXPANSIONARY MONETARY POLICY. It is usually undertaken when the economy is experiencing UNUSUAL situations like a Prolonged & sustained crisis & other severe form of economic instability.

Normal form
Recent MSME packages
- loans via PSBs.

Reverse helicopter drop of Money :

- Also called as Helicopter Hoover.

It is an aggressive form of CONTRACTIONARY MONETARY POLICY which is undertaken under EXTREME economic situations like HYPERINFLATION, economic instability, etc.

Ex: India's DEMONETISATION was in the nature of Helicopter Hoover.

- by Arvind subramaniam, invented by GoI.

Q1 Define Demonetisation. why do countries pursue Demonetisation normally?
why did India pursue demonetisation?
Critically evaluate the success of demonetisation.

H-3
Do MCQs in it

Q2 Critically evaluate the success &/or failure of Demonetisation in India.

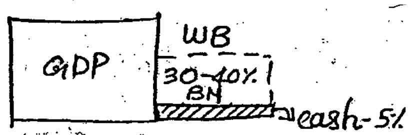
RBI Report, Aug 2018

[1]. 99.3% currency returned:

Our conclusions

a) Most of BM is not in cash (cash is hardly 5%)

b) Not all the returned currency is white money.



c) Now it is Govt's & RBI's responsibility to find out how much of 99.3% returned cash was actually Black money

What should've been done?

Most BM is not in cash

Failed to plug the loopholes. Should've audited gold stores, car stores or big ones 1 week before to identify any abnormal surge on the particular day or after demonetisation.

[2] FICN – This phenomenon increased after some time as they had cash crunch & started printing more – Wait for report of M.HA

[3] HVC – High Value Currency

Why 2000 rs note then?

To provide HVC for wholesale sector

Printing capacity of RBI

	HVC	
2016 →	86%	[500, 1000 Rs]
2017 →	72%	It did go down, But
2018 →	80%	Then it started increasing & now too increasing

If you compare the period around demonetisation (2016), with present (2018), the use of HVC has come down. But, if we compare 2017 with 2018, the use of HVC has increased and in fact it is showing an INCREASING TREND

Currency to GDP Ratio (CGR)

	CGR
2015-16 –	12%
2016-17 –	8%
2017-18 –	11%

Qn 1 Is CGR a good indicator of development?
Is low CGR necessarily a sign of developed economy?

Qn 2 Why do we find high CGR on an average in India?

Acc. to RBI, the CGR depends upon factors like:

(i) Inflation and Rate of Interest
(ii) Informal economy — ESI, 2018
(iii) Extent of migration (internal, highest in the world) — construction
(iv) Economic structure (wholesale Vs Retail)
(v) Regulations on Various Modes of payment.

Just after demonetisation, the CGR came down drastically. It should not be used as a sign of development.

- The INFORMAL SECTOR,
- the DAILY WAGE earners
- The Agricultural labourers
- The Retail market

were impacted -vely after demonetisation & the low CGR could be a sign of that. So, we must not make sweeping generalisation that this ratio is an indicator of development.

<u>Note:</u>

DeMo
↓
30 Cr New Tax payers
↑
GST

Update with reports bfr exam
Not sure if it is an effect of DeMo or GST or both.

<u>Note:</u> Normally countries undertake DeMo when they want to discontinue old currency & introduce new currency.

<u>Ex:</u> EU introduced € between 1999-2002 after making the necessary preparations.

<u>India:</u> used DeMo as a normal POLICY TOOL which has been unheard of so far.

Tried DeMo seeing India but failed: PAK, AUS, VEN

(H-4)

TRADE

Trade + Intn'l Org

12-15 MCQS

BASICS OF TRADE

① AUTARKY : Closed Economy

An autarky only in Domestic Trade & not in International Trade.

② TRADE OPENNESS : Trade to GDP ratio

$$\frac{\text{Trade}}{\text{GDP}} = \frac{\text{Exports} + \text{Imports}}{\text{GDP}}$$

Not an actual factor to say a country is open/globalised

Ex: USA trade war

overall ↑ $\left\{ \frac{\text{Exports}\uparrow + \text{Imports (not}\uparrow)}{\text{GDP}} \right.$

③ TERMS OF TRADE (TOT)

(Indian case)

$$\frac{\text{Price of Exports}}{\text{Price of Imports}} = \frac{\text{Services}}{\text{Oil}}$$

Logic of $\frac{\text{Trade}}{\text{GDP}}$

Int. Trade
DT

GDP

If TOT ↑ – Benefit for India

If TOT ↓ – Loss for India

TRADE AGREEMENTS / MODELS

I] PTA [Preferential Trade Agreement]

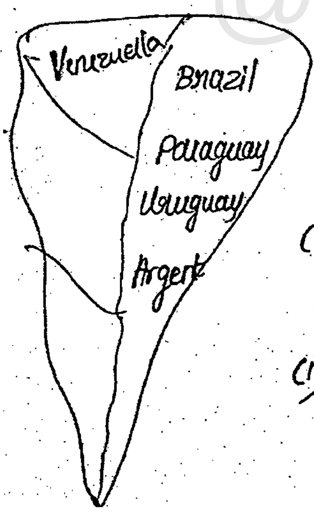
Country A (INDIA)	Country B (S.KOREA)
a_1 (potato)	b_1 (electronics)
a_2 (org.che)	b_2 (electrcells)
a_3 (services)	b_3 (manuf.)
a_4 (Yoga)	b_4 (Taekwondo)

7. EU
6. SM
5. CU
4. CEPA
3. CECA
2. FTA
1. PTA

↑ progress in Trust & Relationship

→ Hi: Select some items (say a_1, a_2 & b_1, b_2) & Reduce the tariffs of that alone (↓ Import duties) } +ve list

Level of tariff: Mentioned in PTA.



Earlier: B+P+U+A+Ven → Mercosur

Now: B+P+U+A −(Ven HR violations)

India's interest with South America why?

(i) New Market
  - Make In India.

(ii) Diversified trade partners
  - policy uncertainity w/ USA but not here

(iii) India is seeking UNSC support from BRAZIL

(iv) Resource Rich.

* **India-Mercosur PTA**: was signed in 2009. The no. of items covered is 400. It was revised in 2017. Items ↑ to 3000.

* **India-chile PTA**: was signed in 2007 & revised in 2016.

2] FTA [Free Trade Agreement]

Country A — Country B

a_1 — b_1 → Items of substantial trade - tariff eliminated

a_2 — b_2

a_3 — b_3 → -ve list; No ↓ in tariff

a_4 — b_4

→ 1st they will make a list for which No tariff reduction } -ve list

→ Items of substantial trade are selected ~~& tariffs are~~ eliminated.

→ A & B have Independent trade relations with non-members.

→ Normally in FTA, GOODS are traded.

Ex: (i) NAFTA [North America FTA, 1994]

USMCA, 2018 [US, Mexico, CAnada]

Aim: To liberalise Trade in:

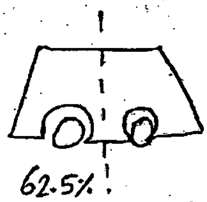
- Agriculture
- Textile
- Automobile
- Manufacturing
- IPR
- Technology
- Labour: special case

- And maintain Environmental standards across regions.

US was unhappy with NAFTA due to job losses in USA (Labour)

New deal:

C, G, F, J, K



a) 75% parts in N.A. region

b) Out of 75%, major parts must be manufactured in High wage factories → ≥ \$16/hr.

Earlier: 62.5%
Now: 75% & not from china

✓ Contain China

✓ Increase Jobs in US

ii) SAFTA, 2006 ← lack of trust, delay

SAARC → In 1985

[Ind; PAK; BAN; AFG; SL; BHU; NEP; MAL – 8 countries]

a) Economic progress
b) Regional co-operation

} More holistic, futuristic than NAFTA which was Materialistic

Issues: Ind-PAK; Ind-SL; Ind-Pak-Afg Tussles.

3] CECA [Comprehensive Economic Co-operation Agreement]

Country A	Country B	
a_1	b_1	→ Tariffs eliminated on wide range of items
a_2	b_2	
a_3	b_3	
a_4	b_4	→ -ve list; Tariffs not eliminated
a_5	b_5	

Unique: Legal aspects are also incl. Legal certainities are provided in policy in terms of Exporters & Importers.

Ex: India-Malaysia, 2011 – CECA
India-Singapore, 2005 – CECA

4]. CEPA [Comprehensive Economic Partnership Agreement]

✓ It has integrated package of Goods, Services, Investments & IPR.

✓ Domestic regulations are taken care under CEPA. (i.e) the countries which had signed agreement assume that domestic policies lead to strengthening of Trade relationship b/w countries. (Domestic policies to facilitate even more aspects;

CECA's legal certainity difference < less no. of aspects; Integrated in CEPA, loose in CECA; may/may not incl S, I, IPR.

Ex: India-Korea, CEPA – 2009

– Revived recently in 2018.

– To strengthen CEPA, 35 new items were added in list & unique provisions were made for VISA FREE MOVEMENT of some of the selected service providers across India & Korea
Ex: Yoga & Taekwando instructors – visa & duty free.

5] CUSTOM UNION

Country A

Eliminate custom duties

Eliminate/reduce other admin. requirements

Same custom duties are applied by A & B to a 3rd country.

Ex: South Africa Custom Union, 1910

SA; Lesotho; Botswana; Swaziland; Namibia

Oldest one

6] SINGLE MARKET

✓ Here, entire trade Barrier is eliminated

✓ 4 Freedoms are provided

- GOODS
- SERVICES
- LABOUR
- CAPITAL

✓ Same trade barriers are applied by A & B to 3rd country.

Ex: Mercosur

(Prepare a Formal chart)

PTA	FTA	CECA	CEPA	C.U	SM	EU
Some items	No. of items ↑	Items ↑	Integrated		4 Deg. of F	
T→↓	T→X	legal assurance G & S	G, S, I+IPR	X-C.D	1) G 2) S	
Only G	G & S open			C.D for others	3) L 4) C X.T.barriers	
+	+/-	+/-	+/-			

7] ECONOMIC UNION

✓ Advanced form of Single Market

✓ Harmony → in terms of

↳ Ideal – may not include all 6 all time.

- F.P
- N.P
- Critical areas
- shared institutions
- Health & Edu
- Environment

European Union:

1957/58 → Treaty of Rome (European Economic Community)
EEC

1985 → Schengen Agreement: ease in movement of people

1992-93 → Single Market / Interna~~tiona~~l Market

1992-93 → Maastricht Treaty / Treaty of EU

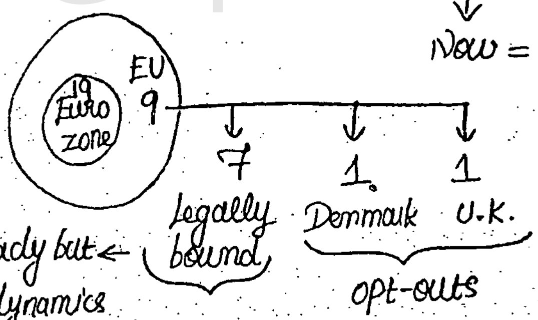
EEC $\xrightarrow{to}$ EU (But, only in 1997 Amsterdam treaty – Visa free)

1999 → Eurozone

Foundation to stop war : Improve INTERDEPENDENCE (esp Eco)

1999-2002 → Preparations made to introduce EURO

2002 → € introduced (12 members)
↓
Now = 19 members



were ready but internal dynamics didn't let them to do immediately

Shared Institutions / Shared concept Sovereignty:

→ In EU, the countries have agreed to create common institutions like:

ECB – European Central Bank : which conducts the Monetary policy in EU.

→ We also find Shared > Executive
> Legislature
> Judiciary

EU has a common Monetary Policy but :
EU has a Harmonized Fiscal Policy.

ASEAN : 1967 $\underbrace{\text{P M T I S}}_{}$ (Founding) ; $\underbrace{\text{B C L M V}}_{}$ (New)

Aim → Economic, Social, Cultural | Peace

AEC – 2015

AEC – VISION : 2015–2025
↓
Aim is to create Single Market
✓ 4 L of Freedom
✓ X-Trade barriers
✓ Common Tr-barr for others.

ARF – 1993
1). ASEAN (10)
2). Dialogue Partners (10)
3) 7 others.

AIFTA
– Signed in 2010
– Specifically signed for Goods.
– In 2015 AIFTA was extended to cover Services & Investment also.
– This is integrated yet not CEPA bcos every Trade agreement can be customised.

Dialogue partners → They participate in meetings of ASEAN at working level & Senior level to give policy inputs & guide the development of regional relations.

ASEAN 10 members → CHINA JAPAN KOREA → INDIA AUSTRALIA NEW ZEALAND → USA RUSSIA

ASEAN+3 (Individual FTA) - alive

ASEAN+6 (Individual FTAs) - gaining momentum

→ CEPEA
- Economic co-op
- Trade & Investment
- Liberalisation

[Comp. Eco. Part in E-Asia]
→ G
→ S
→ I+IPR

→ RCEP (2012)

[Regional CEP]
→ G
→ S
→ I+IPR
→ Labour

But not SM bcos they'll still behave like Custom union → with just 1 feature of SM (testing the idea)

EAST ASIA SUMMIT

> No FTA, hence no CEP & no RCEP
> Just for condusive, peaceful environment

BRETTON WOODS CONFERENCE

(WW-II) July 1-22, 1944

Concep — GS2, GS3
Facts — Prelims

- Reconstruct
- Restore
- Development

[Men & Material]

(WB) IBRD
Institution

Identify & Solve Crisis

IMF
Institution

Restore Trade

ITO — not accepted by USA
Institution

↓

GATT — Just a Contract

↓

WTO — Institution
(Derived from GATT)

World Bank Group [WBG]

1). IBRD - 1945
2). IDA - 1960

} WB — [Original WB institutions
Principle of WB carried on]

3). IFC - 1956

4). MIGA

5). ICSID

Read

* URMIT PATEL *

IBRD → Loans to ✓ Middle Income countries

✓ Credit worthy low Income countries

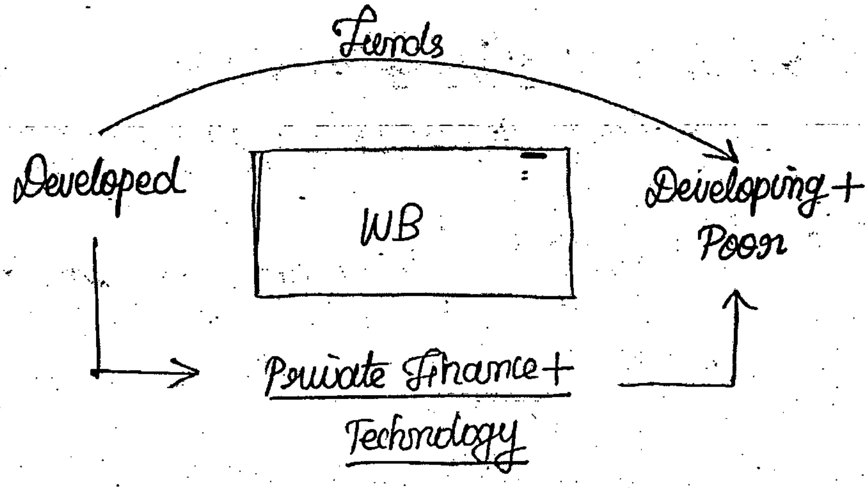
IDA → Interest free loans, Grants (specific purpose only + No need to pay back) } to extremely poor countries.

IFC → Funds Private projects for a COUNTRY & $\underbrace{\text{not for the World}}_{\text{criticism}}$ } ✓ Manufacturing ✓ Textile ✓ FPI (Food process Ind) ✓ Financial Market (Masala Bonds)

MIGA → To ↑ FDI

WB gives guarantee for FDI in countries, in case of crisis or problems, after talking to Govts.

ICSID → Dispute Resolutions



(Integrated) — Diff. b/w WB & normal Bank ✓

Criticism	Defence
1) Excess focus on Middle Income countries →	40% of world poverty lies here. Relatively easy than poverty in extremely poor countries + To make them partner in WB.
2) Mostly focussed on Private projects in specific countries. →	To help economic growth + Sustainable Economic Growth
3) No Global Goods →	No defence from WB
4) Hardly 5% of private capital in developing + poor countries is by World Bank. →	Countries are more capable now because of us. Private finance + Tech + Improving local markets via. IFC, MIGA, etc.

Conclusion:

Acc. to. WB, it has 2 distinct advantages which makes it even more relevant in today's context:

(i) They've gained experience in designing & implementing multi-sector projects across the world.

(ii) They have the Best Global think Tank for project design and Implementation.

The WB is heavily criticised for dominance of USA, which needs to be balanced out by giving more power to emerging economies & WB has not opposed to this suggestion.

The WB is important today for global governance, Poverty reduction & Global development Agenda.

IMF

Aims → BOP + Exchange Rate crisis Info gathering old job — Know. Collector
→ Global Macro policies — Dat. Collector

3 roles:

1. Surveillance
2. Lending → Concessional
→ Non-Concessional: Rate of charge + Surcharge (for hefty loans)
3. Technical assistance

a) RFI – Urgent BOP needs + No/min conditions — Oxygen
b) SBA – BOP issues + WC (Washington Consensus)
c) FCL – Pre-set conditions + strong economies — For strong & good economy: ↑ imports, ↓ subsidies
d) PLL – a slightly weaker form of FCL — Not exceptional but good economies
e) EFF – Very long term loans + Structural reforms
MPC, GST

WASHINGTON CONSENSUS

IMF loans come with attached conditionalities in the following form :

(i) Increase in exports – to pay back in future

(ii) Increase in Foreign investment – new foreign policy, FDI policy etc...

(iii) Reduction of subsidy – ex: Greece

(iv) Control of wasteful Govt. expenditure (Austerity)

(v) Devaluation of currency – to ↑ exports

(vi) Balancing the Budget – Revenue = Expenditure

(vii) Privatisation

(viii) Reforms in Governance: Including Fight against Corruption. + Anti-Black money policies

(ix) Liberalisation of Trade.

IMF Quota :

Maximum contribution that a member is expected to make.

TOTAL QUOTA (TQ) = 25% in globally acceptable currency or SDR + 75% in domestic currency

$, €, Renminbi, Yen, Pound sterling

USD - 41% Ren - 10% P.S - 8%
€ - 30% Yen - 8%

a) GDP

b) Openness = receipts + payments (Exp + Imp)

c) (Variability) Volatility = of receipts + net capital inflow — must be stable & not volatile
FII, FDI

d) Forex

2 Factors to decide SDR :

1) Country should be one of the top 5 exporters of the world
2) Currency should be freely usable globally.

Once TQ is paid:

$\boxed{\text{VOTING RIGHTS}}$ = 250 Basic votes + 1 extra vote for every 1 lakh SDR quota

- ✓ USA → 16.5 %
- ✓ CHINA → 6 %
- ✓ INDIA → 2.6 %

BRICS [Brazil. Russia India China S.Africa]

Why only these 5 countries?

Features

i) Emerging Market Economies (EME)

ii) Newly Industrialised Economies

Fortaleza Summit - 2014

Compet- to WB.

New Development Bank (NDB)
(available to all countries)

Contingent Reserve Arrangement (CRA)
(As of now, available only to members)

competition to IMF

NDB

→ Created with an authorised capital \$100 bn.

→ Initial subscribed capital is \$50 bn.

Authorised capital → Maximum capital that can be raised by a firm by issuing shares.

Initial subscribed capital → Actual capital that a firm raises by issuing shares.

Note: Companies registered in MCA (Min. of. Corp. Affairs)

Ex: Permission for Rs. 1 shares no.500. – AC

Now I need only 200, so only 200 shares I sell – ISC

In future ISC can be increased till AC, then have to get more shares to introduce, all shareholders must agree & MCA permit.

The contribution of 5 members of BRICS is equal in the subscribed capital & hence they have equal voting rights as of now.
↳ In future, scope for change.

Objectives of NDB:

i) Infrastructure & Sustainable development related funding.
ii) Funding for both public & private projects.
iii) Co-operation with other international bodies.
(WB → Also funds pvt. projects : IFC . So NDB emulating WB)

CRA

→ Total fund under CRA as of now is \$100 bn.
→ Under CRA, Financial assistance will be given to countries facing BOP & ER-related crisis.

Total capital of CRA = \$100 bn
CHINA – \$41 bn
B, R, I – \$18 bn each (\$54 bn)
S. AF – \$5 bn

Why not Equal?
◦ China demanded it to be so & India had no other choice to not to go to IMF.
◦ India → Reforms in IMF is very difficult due to no. (190 countries) but here only 5 countries.

Currently it is used as a threat tool to IMF. But just begin, may develop further & expand

Future prospects of IMF:

If at all, IMF & WB's role is diminished or dismantled, NDB & CRA would already create a base for replacing IMF & WB.

[To be in NDB or to get fund, a country has to be UN member]

G-7

→ Because of OIL SHOCK OF 1970s, Countries like:

1. US 2. UK 3. CANADA 4. JAPAN
5. GERMANY 6. FRANCE 7. ITALY

Came together & created G-7 in 1975.

→ It was created in reaction to oil Crisis so as to keep an eye on International Economic & Monetary issues.

G-7 : 1975
↓
G-8 : 1998 – RUSSIA joined → G-20 : 1999
↓
G-7 : 2014 – Russia removed

These are the industrialised countries & use oil most & is affected by oil fluctuations more & hence oil shocks exposed the global fluctuation of market, this G-7 came up to keep an eye on market.

G-20

The G-8 countries felt the need to bring in - 1999 Developing economies in the DISCUSSION FORUM of Global economic issues. So, they created G-20, which consists of:

> EU + 19 other countries

* 1999–2007
  - i) Global Economic Issues (GEI)
  - ii) Fin. Min & Governors of Central Banks
* 2007 Onwards
  - i) GEI
  - ii) Financial Market (Money Market, Capital Market)
    Trade & Development (Exp, Imp, BOP)
  - iii) Head of state

Note: RUSSIA

Geo-politically it is proactive. But,
Economically its might is limited & not diversified.
In IMF too, India's voting share is higher than Russia.
Since ~~India~~ Russia broke up, it lost most resources.

11th NCERT

Revision

INVESTMENT

Economic Investment

Real Assets
- Roads
- Tools
- Bridges
- Machinery
- Equipments

[Tangible]

Financial Investment

Financial Assets
- Shares
- Bonds
- Debentures

[Only ownership changes, share doesn't change
Non-tangible]

By default, we would take investment in the economic sense, unless otherwise mentioned to be financial.

INDIA'S GROWTH MODEL

→ Entire argument on this Problem: Y not export-led instead?

2nd FYP → Mahalanobis Model → ↓ Import by creating Heavy Industries

(i) Import Substitution (ISI) Industrialisation
+
(ii) Infant Industry Protection

(Requirement of time. But, should've stopped by 3rd or 4th FYP but extend till very long)

Increase the Role of State $\xrightarrow{to}$ ↑ GDP & Employment.

1960s = Export led Model .

Export Processing Zone (EPZs) – 1965

↓

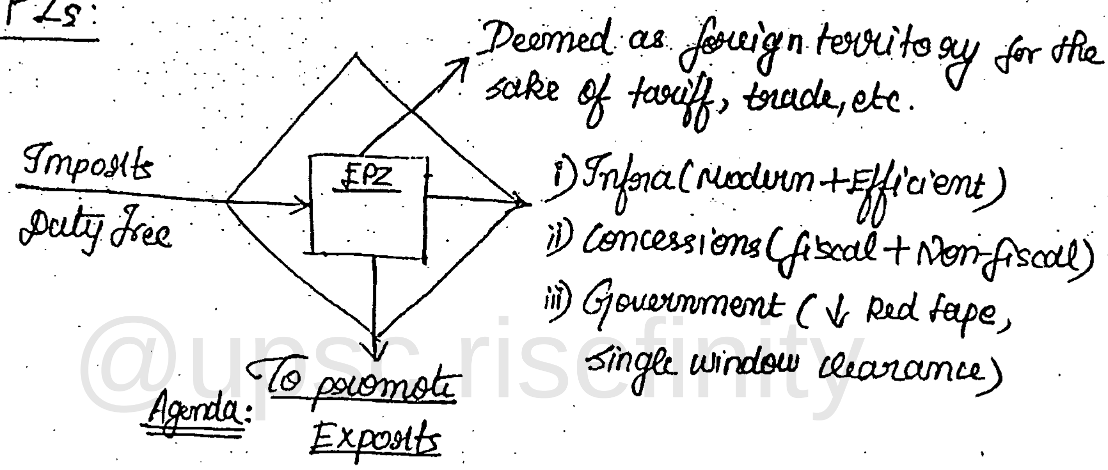
Special Economic Zone (SEZs) – 2000

↓

Coastal Economic Zone (CEZs) – 2015

(To be renamed as Coastal Employment Zone)

EPZs:



In 1950s, china & ASEAN started experimenting the zone model to ↑ exports & they started succeeding & India too started following.

→ Specific Geographical Area

→ Manufacturing units + offices → Duty free imports.

→ Good Infrastructure.

→ Governance (↓ Bureaucratic Interference)

Began only with GOODS & NOT SERVICES

EPZs are special enclaves separated from domestic tariff area [DTA] by Fiscal Barriers.

The aim is to provide Internationally competitive duty free environment to promote export.

3 Benefits of EPZ

i) Infra (Modi + Eff)

ii) Concession
- Fiscal → No import duty
- Non-Fiscal → No import license

iii) Governance (↓ Red tape, sing. W.C)

Characteristics of Indian EPZs

EPZ carries those stages of production that have high import content & require greater unskilled labour force.

Ex: Success of Electronics export from India proves this.

Critical evaluation of Indian EPZ

> Exports, Forex Earnings & Employment – All of these increased in absolute terms but their rate of growth reduced over time. (why? Lack of diversification)

> No Backward Linkages were created with Domestic market.

> Their export performance also deteriorated over a period of time.

> EPZ failed to promote non-traditional exports & they only promoted traditional – electronics, Gems & Jewelry.

> Engg. goods Industry couldnot succeed in India's EPZ.

> Single Window Clearance was not actually available because a lot of restrictions were imposed in day-to-day operations of industries under EPZ.

(Engg. goods :

To be viable, need Economies of Scale – Efficient tech & so on. But EPZ didn't facilitate this)

By 2000, we realized the limitations of EPZ & we started to focus upon the idea of SEZs.

$\boxed{\text{SEZ}}$

→ Sub-contracting is allowed → Domestic supplier allowed

Imports → No Licenses req.

Imports → No Imp. duties

Supply of RM → (No taxes)

High Class Infra for : → Both mfg + Services

a) Commercial

b) Residential purposes → They need to earn Forex. ↓ Depends on interpretation of Govt. authorities (Assessment every yr)

Tax Concessions

a) 1st 5 years = 100%.

b) Next 5 years = 50%.

c) Next 5 years = 50%.

of reinvested export earnings

Note: when EPZ Policy was formulated, the govt. didn't explicitly mention the objectives of EPZs other than ↑ Exports.

1st 1965 - Gujarat (Kandla)
2nd 1973 - Mumbai (Santa Cruz)

In 1989, in the CAG report, the objectives of EPZ were mentioned for the 1st time in great detail.

- ↑ Export
- ↑ Forex earnings
- ↑ Employment
- ↑ Investment

Unique Feature of Indian SEZs :

Globally SEZs were created by govt. agencies with their active role not only in creation but also in promotion of SEZs. But in India, SEZs were created with Active role of private Sector, where the role of govt. & pvt. sector are precisely defined. (Onus on pvt. sector to promote SEZ)

(2005) SEZ Approval Mechanism

Developer Submits proposal → SG → (45 days) → Board of Approval under M. of Commerce & Industry

Directly can also send if urgent

1. Companies
2. Individuals
3. Partnerships etc.

Board of Approval under M. of Commerce & Industry ↓

Approval Committee
a) Development commissioner
b) Custom officials
c) SG representative

↓

CG is informed

CHINA – Turned border villages into huge (10,000 acres) SEZs. Lenience in restrictions. Attracted Chinese & foreign investors. Growth was huge. ✓ Strategic Location ✓ Size (huge)

INDIA ⟶ × Location × Size (Limited)

Note:

Handout – For understanding
Notes – For memorising & revision.

SEZs

* SEZ 2000 Scheme

→ Launched under Foreign Trade Policy of India.
→ Fiscal incentives were given.
→ It was not a separate Act.
} ≃ EPZs. No dedicated details.

* SEZ Act 2005

→ Not a part of a running policy but a separate act with drastic simplification of procedures like: SWC w.r.t. both SG & CG. Aims:

i) To ↑ GDP
ii) To ↑ Exports of Goods & Services
iii) To ↑ Investment
iv) To ↑ Infrastructure
v) To ↑ Employment

Assessment of SEZ in India

① Taxation

i) Domestic sales from SEZ are imposed with or subjected to custom duties. During a time when we observe trade war, Financial Crisis, Economic slowdown & other such external factors which affect our exports negatively, imposing custom duties is considered as problematic by SEZ units.

They are demanding that GoI should sign a FTA b/w SEZ units & the govt.

Min. Alternative Tax ; Divident distrib. Tax.

ii) SEZs have to pay MAT & DDT, which is in excess of 40%. SEZ units have been demanding the removal of these 2 taxes

P&L account of company

(≃21%) MAT → is imposed on Book profit of companies. It was basically started against the so-called zero-profit companies which were distributing dividends despite showing zero or -ve profits.

$$\text{Net Income} = \underbrace{\text{Revenue}}_{\text{Book profit}} - \text{Expenditure}$$

(≃21%) DDT → It is imposed on firms when they distribute dividends to shareholders.

The current rate of DDT including Cess & surcharge is 21%.

MAT+DDT → 42% } Inside SEZ

Corporate IT → 30% } outside SEZ
↳ For MSME – 25%

iii) There are grey areas & uncertainities in the tax rate & the tax nature inside SEZ.

· MAT & DDT started in India inside SEZ units since 2012. It led to the withdrawal of licences by 100s of firms.

② Labour Reforms have not happened in a significant way in SEZ. Labour laws inside SEZ are very stringent.

Ex: HIRE & FIRE Policy is not allowed - to substitute inefficient workers.

③ The investment inside SEZ, esp in Manufacturing is not coming in a big way.

GoI has started to focus on a new policy called as COASTAL ECONOMIC ZONE.

COASTAL ECONOMIC ZONE

SAGARMALA [2015-35]

Sagarmala
- Port
- Roads, Railways, Inland waterways
- CEZ
- Local communities

Rs. 8.7 lakh Crore ; 577 projects

Context of Sagarmala:

i) Indian ports handle 90-95% of our export import.

ii) Contribution in GDP by:

a) Ports = 1%

b) Roads = 6%

c) Railways = 10%

Make In India – 25 Sectors

a) ↑ Manuf

b) ↑ Exports

c). Jobs

Capital intensive sectors were also included – mistake.

Make In India 2.0 – 10 Sectors

✓ Labour Intensive ———— Jobs

✓ Potential to ↑ Exports

✓ Potential to ↑ GDP of India

Linkage: When MII succeeds, there will be goods for Exports & then we need ports to export them – Hence Sagarmala.

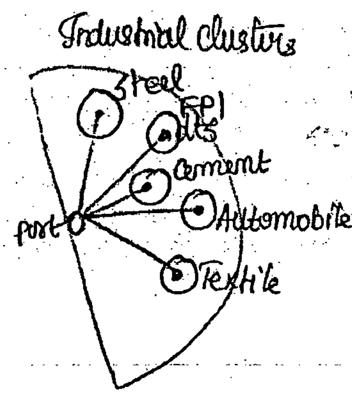
4 PILLARS OF SAGARMALA

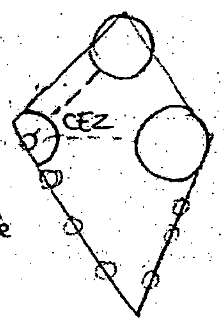
I. Port Construction & Enhancement

II. Port Connectivity through Railways, Expressways & Inland waterways

III. Port led Industrialisation through SEZ

IV. Skill enhancement of coastal & island communities





⇒ Definition of CEZ: CEZs are economic regions spread over multiple coastal districts with strong sea port linkages. Each CEZ would have Multiple Industrial clusters.

⇒ The Industries picked up in initial phases of CEZ are:

- Electronics
- Textile
- Furniture
- Automobile
- Food Processing
- Steel
- Cement

} Sectors overlap with NII 2.0

⇒ The states to be given priority in 1st phase of CEZ are:

- GUJARAT
- MAHARASHTRA
- ANDHRA P.
- TN

<u>Short Note</u>: GOI is planning to change the name of CEZ to Coastal Employment Zone.

This would mean that the principle to be followed to give licences inside CEZ would be the potential to create jobs & not just bring foreign currency through exports.

<u>CHINESE CEZ</u>

Mandatory to bring Tech:
- ↓ cost of production
- Min. environmental Impacts.

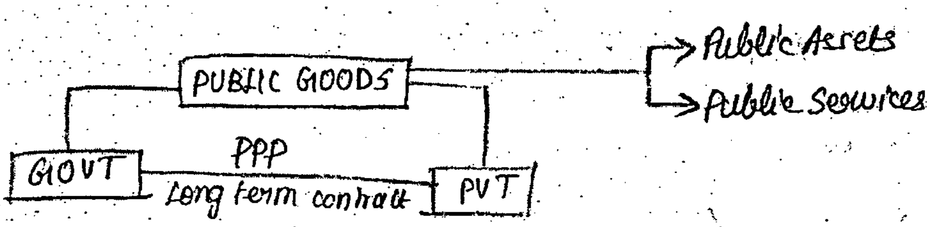
PUBLIC PRIVATE PARTNERSHIP

Definition → PPP is a long term contract b/w govt on one hand & private sector on the other. [~2 yrs to ~40 yrs]

Aim – The ultimate aim of PPP is the creation of public goods which are of 2 types:

a) Public assets – Like Roads

b) Public services – Like Health & Education



Aim

i) ↑ Value addition

ii) ↑ Quality

iii) ↑ Cost

iv) Operations & Maintenance

v) ↑ Tech

Need

i) Industries & Urban Area

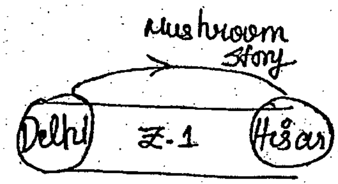
ii) Budget constraint

iii) Multiplier effect

iv) ↑ Rural Income [Health, Edu, Roads]

Multiplier Effect

A ₹1 investment in infrastructure increases the GDP by more than ₹1 (Sometimes by upto 3-4 Rs.). This is called as effect of Investment in Infra on GDP termed as Multiplier Effect.



IMF & WB – ₹3 to ₹4
Gita Gopinath.

Qns

1. What do you mean by PPP?
   What is the aim of PPP?
   What is the need for PPPs in India?

2. What are the diff. types of PPPs in India?

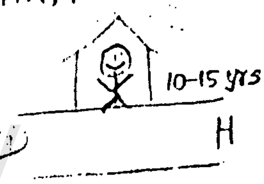
WEF
India in top 3 in Urbanisation

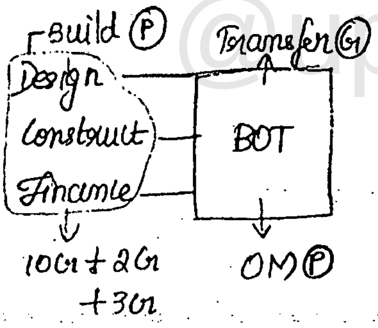
Note: What do you mean by MAKE IN INDIA? Critically examine the performance of MII policy. Has it succeeded? If not, why? Suggest some ways to make it a success. In this context, discuss MII 2.0.

TYPES OF PPPs IN INDIA

BOT → BOOT → BOO → EPC → TOT → HAM

→ I BOT (Build-Operate-Transfer)





BOT Variants

BOT Toll	BOT Annuity
Toll = Pvt	Toll = Gov;
Toll risk = Pvt	Toll risk = Gov
	Pvt. sector gets 6 monthly payments.

⇒ BOT Annuity

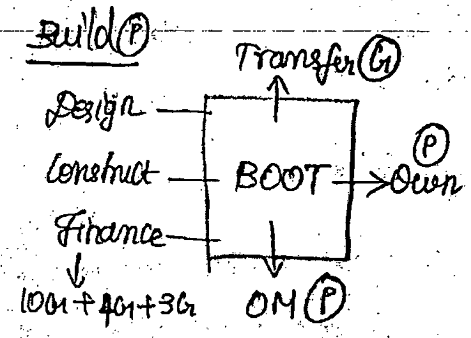
Under this, 2 kinds of projects are undertaken:

Risky project
Critical Social Infrastructure

⇒ GOI decides whether to use BOT Toll or BOT Annuity

GOI is the owner.

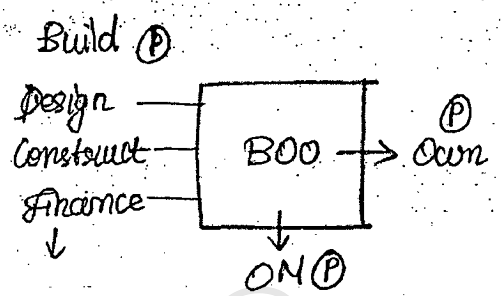
2] BOOT [Build-Own-Operate-Transfer]



4> Pvt. Sector is the owner
Pvt. Sector collects Toll.

4> More amount of profit as risk is double as it arranges finance completely on own.

3] BOO [Build-Own-Operate]



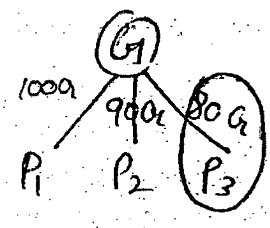
4> Public good as in contract, so not privatisation — But ppl need to pay user fee.

→ Govt. cannot force the pvt-sector to return the property. Also the govt. is not obliged to take back the property.

4] EPC [Engineering-Procurement-Construction]

→ Pvt. constructs; leaves after sometimes.

→ Govt — Finances
— Collects Toll
— OM

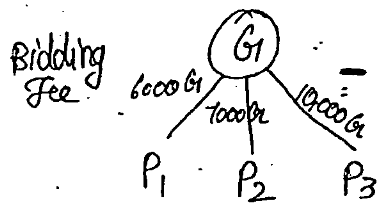


✓ Good Toll collection (atleast for 2 yrs)

✗ Damage to road — heavy usage.

5] TOT [Toll-Operate-Transfer] / Asset Recycling

- → Contract = 30 yrs
- → Toll = Pvt
- → GoI = Compensation if Toll collection falls



Mar : 2018 — Greenfield Airports UDAN.

9 roads – 10,000 Cr

Australian company (100% FDI in Infra)

6] HAM [Hybrid Annuity Model]

- EPC
  - GOI Finances = 40%
- BOT Annuity
  - Pvt-Sector = 60%
    - Pvt-Sector Own Capital 20-25%
    - Banks, FIs 35-40%

- → Toll = Gov (NHAI)
- → Pvt-sector gets Fund Transfer by Govt
- → Contract period = 30-40 yrs (Mostly 40 yrs)

NITI Aayog's Proposed HEALTH MODEL

→ NITI Aayog has proposed a PPP Health Model with 2 Components:

a) A model for District Hospitals b) A Model for Fee Collection

→ There are 4 Entities in model.

i) Dt-Hospitals in Non-Metros ii) SG iii) Pvt-Sector iv) UG.

District Hospitals → Cancer; Respiratory; Cardio

Non-metros

District Hospitals —Fee→ SG

SG —Funds→ Pvt sector

Pvt sector: Upgrade + OM

Payor Mix

1. Concession
2. Non-concession

If there is a delay in fund transfer from SG to private sector, NITI Aayog advocateds severe punishment for SG.

FINANCIAL MARKET

- Money Market (<1 year)
- Capital Market (>1 year)

EQUITY
- Equity shares
- Preference shares

Primary	**Secondary**	**Derivative**
1. IPO	1. BSE	1. Forward
2. FPO	2. NSE	2. Futures
3. Pvt. Placement	3. OTCEI (Over The Counter Exchange of India)	3. Options (call, put)
a) QIP		
b) Pref. shares		

DEBT
1. Bonds
2. Debentures
   a) CD
   b) NCD

→ FIB
→ FRB
→ ZCB
→ IIB (2013)

→ Primary & Secondary

Financial Market:

FM is a market for Financial Assets.

Ex: shares, Bonds, Debentures, etc..

BONDS

Bonds offer fixed stream of Income for a fixed time interval.

Fixed Interest Bond

Bond Price = Rs. 1000
Interest = 4 %
Time = 1 yr (for easy calc.)

Interest Income $= \frac{4}{100} \times 1000 = 40$ Rs.

Floating Rate Bond

Bond Price = Rs. 1000
Interest = ?
Time = 1 yr

Interest = 2% (say) + Repo Rate (say)

Reverse repo (or) BR (or) MSF, etc.

Zero Coupon Bond

Bond price = Rs. 1000
Discounted price = 700/-
Time = 1 yr.

Return on Bond = Bond Price − Discounted price
= 1000 − 700 = 300 Rs./-

In ZCBs, there is No Interest Income. Hence, there is No TAX on interest income. So the nature of tax on ZCBs would be Capital Gains Tax.

Coupon is the return in terms of interest income.

Inflation Indexed Bond

It was introduced by RBI in 2013 when India was reeling under double digit inflation. RBI is planning to introduce IIB again in 2019. IIB gives compensation for inflation in both principal & interest.

Bond Price = Rs. 1000/-
Interest = 4%
Inflation = 3%
Time = 1 yr

Effect of inflation on Bond Price

$= \frac{3}{100} \times 1000 = \text{Rs. } 30/-$

Inflation adjusted Bond Price = Rs. 1030/-

Interest Income $= \frac{4}{100} \times 1030 = \text{Rs. } 41.2/-$

Return = 1030 + 41.2

Hear

HH $\xrightarrow{\text{3 years}}$ Bonds, Shares etc. → Firm

HH → Land, Gold

Land: RERA, DeMo

Gold: KYC

DEBENTURES

These are the tools which are used by big companies with reputation & a good will.

Face Value = Rs. 1000
Interest rate = 4%
Time = 10 yrs

The return (interest income) on debentures is paid prior to dividends.

Debentures are of 2 types

Convertible Debentures (CD)

After a fixed time interval, the debenture can be converted into share (Equity share). A premium has to be paid for that.

Non Convertible Debentures (NCD)

There is no option to convert to shares.

The rate of return on NCD is little higher than CD.

⇒ If there is increase in tax also, big companies will compensate in case of debentures.

SHARES

Equity Shares (Family)

> Ordinary shares
> Real owners
> Get dividends
> Voting rights

Prefer. Shares (Guests)

> Precedence in dividend over equity
> Precedence in Capital over equity in case of liquidation
> Limited voting rights

PRIMARY MARKET :

It is a market where NEW SHARES are issued.

Savers/Investors → P.M → Firms

Underwriter
1. Price
2. Risk
3. No. of shares
4. Info.
5. Time

Savers/Investors → Info. ← Firms

1. IPO = New + 1st time shares
2. FPO
3. Pvt. placement
   a) QIP (Qualified Instit.l Placement)
   b) Pref. shares

P.M.

100 shares
share prices = Rs. 300/-
Capital = Rs. 300 × 100
= Rs. 30000/-

share price = Rs. 310/-
Capital = Rs. 31,000/-

IPO (Initial Public Offering)

New shares are introduced for the 1st time.

FPO (Further Public offer)

Existing shareholders are given shares based on the % of shares they already hold. They get shares at a price less than market price.

Pvt. Placement

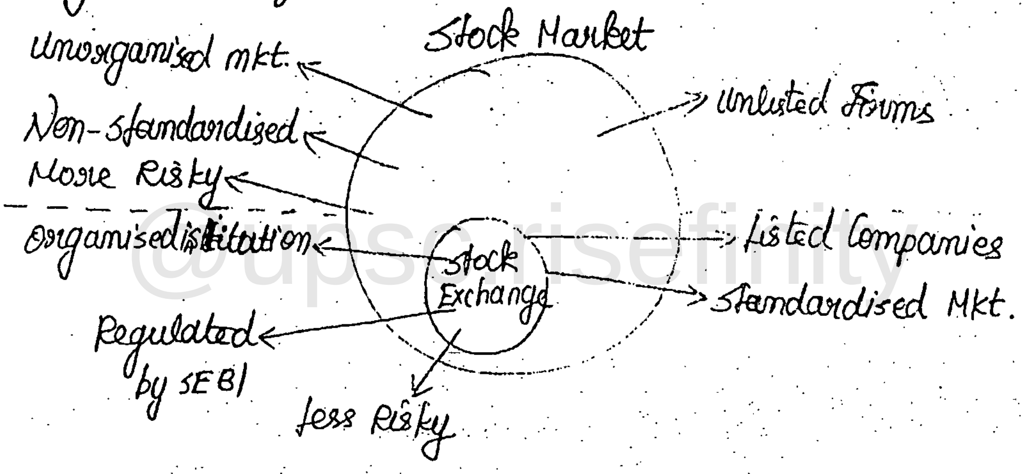
Shares are directly sold to big investors like Banks & FIs.

In case of QIP, the shares are sold to the institutions who have expertise & strength to invest in large markets.

SECONDARY MARKET

Sale & Purchase of existing financial instruments takes place.

In primary market, capital formation occurs for the company, whereas in secondary market, capital formation occurs for the existing holders of (shares, bonds, etc.) Financial assets.



Process of Listing in India

	BSE	NSE	OTCEI
Paid up Capital	3 Cr	10 Cr	30 lakhs
Tools	FM	FM	CM
No. of firms	~5000	~1800	120 Sponsors + Market Makers

OTCEI

When you enter OTCEI as a small & Medium sized company, they are assigned sponsors who help in the appointment of market makers.

Job of market maker is to create demand for the shares of new companies. They try it for 18 months followed by another 18 months. It is like a handholding support for new firms.

STOCK MARKET INDEX (SMI)

SMI reflects the performance of selected companies in stock exchange.

Ex: BSE Sensex (30) NSE Nifty (50)

The top 30 or 50 industries are picked based on foll-conditions:

i) Market Capitalisation (M-Cap)

M-cap = No.of. shares x share prices = 100x310 = Rs.31000/-

Free Flow M-Cap = No.of. easily available shares x share price

= 90x310 = ₹.27,900/-

Captive shares: Shares not easily available in market. May be held by employees themselves / trusted, loyal ppl who won't sell.

(BSE) 5000

Energy Edu Health IT

Picking the tops from each sector based on ~~M~~ Free Flow M-Cap.

ii) Diversity of sectors.

iii) The past record of companies must be untainted.

⇒ SMI gives a good idea about the health of the economy as well as consumption pattern of the economy.

BSE Sensex-30

$\uparrow GDP = \uparrow C + I + G + NX$

$\boxed{\text{DERIVATIVES}}$

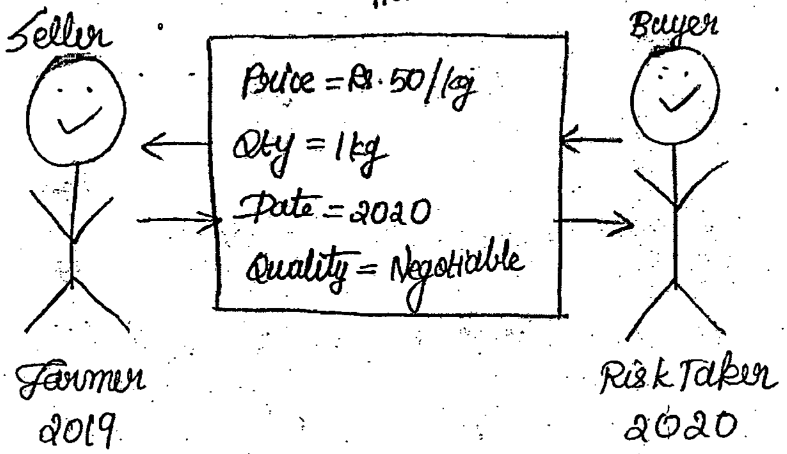
A derivative is a contract whose value is derived from another asset like share, commodity, currency, Rate of Interest, etc. These assets are called as underlying & the value of derivative depends upon them.

Forwards

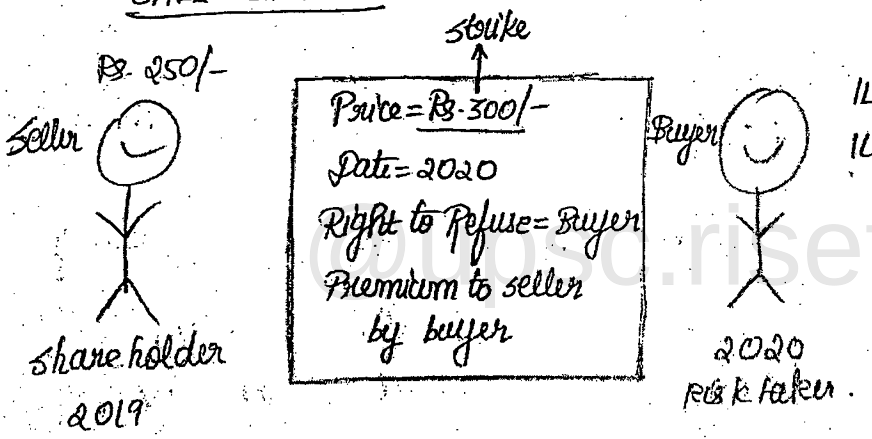
In unorganised mkt
stock Mkt
Not tradeable in SM

Futures

In organise mkt
stock Exchange.
Tradeable in SM.

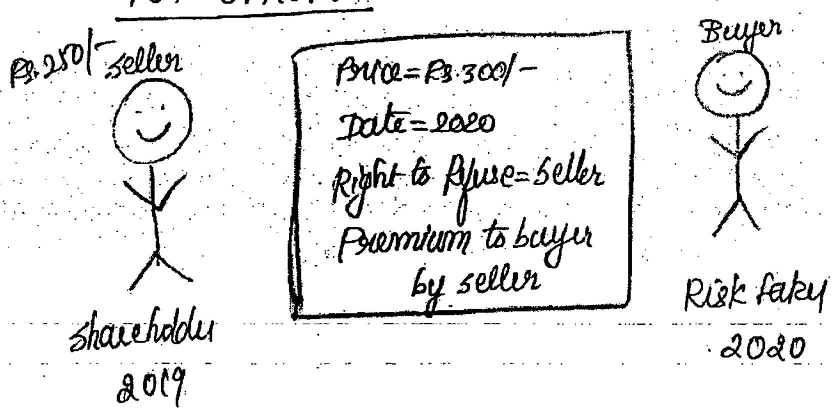


CALL OPTIONS



ILFS saved = Rs. 600/-
ILFS confused = Rs. 150/-

PUT OPTIONS



ILFS saved = Rs. 600/-
ILFS confused = Rs. 150/-

To Firms

VENTURE CAPITAL

i) Group of professionals / Institutional Investors
ii) Contact
- Corporations
- Provident Funds

iii) Decision are time taking
iv) Less Risk
v) Investment = huge

ANGEL INVESTOR

i) Individuals
ii) Quick Decisions
iii) Big Risk
iv) Capital + Mentorship
v) Equity (now or in future)
↳ No compulsion

ANGEL TAX

Extra Income

= (1000 − 200) × 100

= 80000

↓

30% tax.

Firm

100 shares

Price = Rs. 1000/share

Capital = Rs. 1,00,000

Cadbury India

= Rs. 200/share

ECONOMY

Reliable Source: RBI website

REFERENCES:

1) NCERT – XI th – Indian Economic Development
   – XII th – Introductory Macroeconomics

2) Reference material from Vajiram → Indian Economy
   → Current Affairs (Economy)

3) Newspaper → Indian express – 'Explained' Page
   → Hindu Editorial
   → Hindu – 2 pages selectively

Don't
- Avoid performance of financial markets
- Avoid profit/loss of Individual companies
- Avoid mergers & acquisitions (except on Nationally important)

Do
- Nationally important issues
- Class topic hints
- GS 3 syllabus

4) Websites – PIB, Ministry websites (Occassionally)

5) Economic Survey → Selected topics (Before 3-4 months of exam)

6) Text Books – If referred by professor – for Mains

How to approach the Subject?

Prelims: Concepts ⟹ Factual Details
Mains: Viewpoints

$\boxed{\text{Concepts}} \Longrightarrow \boxed{\text{Factual Details}} \Longrightarrow \boxed{\text{Viewpoints}}$

Concepts ↓
Like
- Repo Rate
- NPA
- Money supply

Factual Details ↓
- Policy details
- Govt. Schemes
- Figures

Viewpoints ↓
2 types of Qns:
Factual details from memory + taking standpoint justifying the stand

---

LIST OF TOPICS:

1. Introduction to Indian Economic structure and Policies
2. Open Economy concepts
   - BOP [Balance of Payment]
3. Employment & Unemployment
4. Poverty
5. Agriculture – 4 qns in mains (Geo + Econ)
6. WTO (World Trade Organisations)
   [IBRD & IMF]

Factors of Production:

1. Land
2. Labour
3. Capital [HH $\xrightarrow{\text{deposit}}$ Banks $\xrightarrow{\text{Borrow}}$ Firms; HH $\xrightarrow{\text{Indirect}}$ Firms]
4. Entrepreneurship
   - Risk taking ability (Intangible)
   - Also from some household

Real Economy
↓
Adjusted for prices
- Real production

Nominal Economy
↓
With prices
- Value of production

Ex: when a company produces 500 cars - each 4 L

500 cars	500 × 4 L
Next year 450 cars	450 × 5 L

So, we must not go to conclusions with nominal economy alone

Microeconomics: – No need to read NCERT on this - Not imp. for GS Mains

Predominantly decisions of Individual Viewpoints of individual households, firms etc.

Macroeconomics:

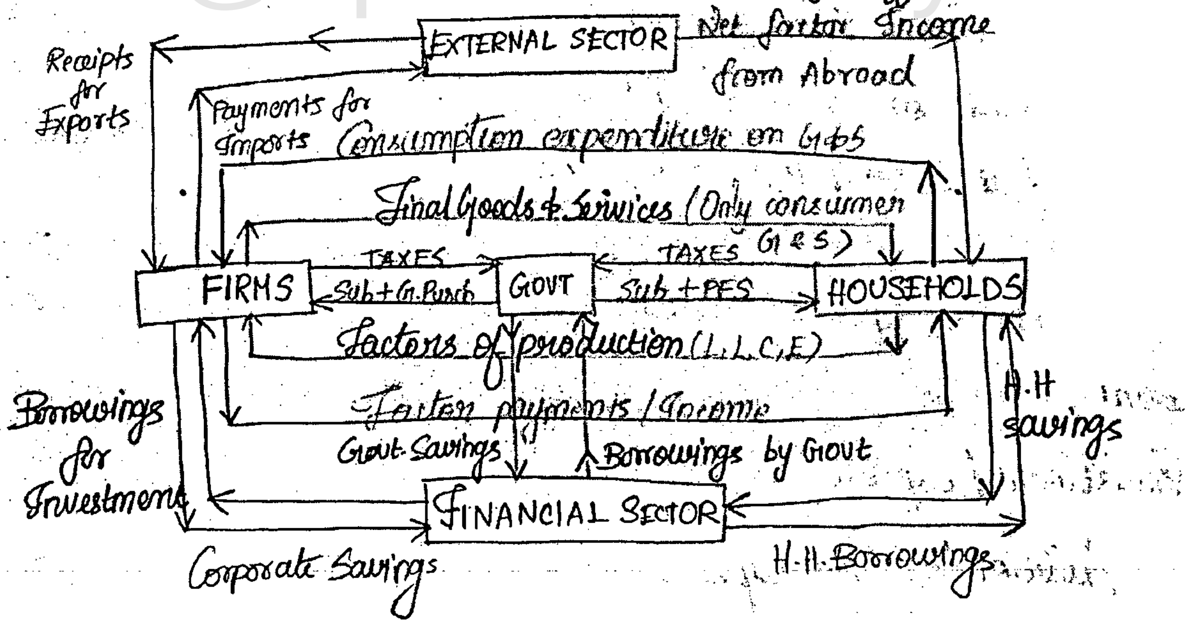
'Macro' - 'Aggregate'

The branch of economics which looks into the behaviour of Economic aggregates.

1. Introduction to Indian Economic Structure & Policies

CIRCULAR FLOW OF INCOME

It talks about interdependence among diff. economic sectors.



Consumption expenditure

It means payments made by H.Hs for final g & s (only consumer g&s) to Firms

Factor Payments / Income

Payments for factors of production by firms to H.Hs.

Payments — for firms

Income — for H.Hs

1. Land - Rent 2. Labour - Wages

3. Capital - Interest 4. Entp^ship - Profit

House Hold Savings:

→ What if a country's Exp > Income ?

↳ FDI dependent

$\boxed{\text{Factor Income - Consumption Exp.}^{re}}$

In India, Factor Income of H.Hs always exceed consumption exp.^re of H.Hs & that is why H.H. savings are present.

Like: Bank deposits, share purchase, Bond purchase ...

Investment / Capital Formation:

→ Speculation - (!)

Read

Addition of New Capital

↳ This is ⊗, because it determines long term economic growth.

Today's capital (Inputs) → Tommorow's production (Outputs)

Corporate Savings:

Next to H.H savings (→ leader in savings in India), Corp. savings are crucial. In recent years Corporate savings are increasing.

Household Borrowings:

H.H savings > H.H. Borrowings

Corporate Savings < Corporate Borrowings (leader of borr. in India)

Govt. Borrowings:

Next to Firms, Govt. is the leading borrower.

Govt. Payments:

Payments by Govt for G&Ss purchased from the firms.

PFS [Payments for Services]:

Payments by the govt for services from Households

Ex: Salary of Govt. Servants.

Transfer Payments: [TPs] – No one on one correspondence

Refer to any type of one-sided payments (or) unidirectional payments. Ex: Subsidies, Taxes

↳ This is unique bcos most payments in economy are two-sided [Payment done for reciprocating goods or Services]

Ex: Govt. purchases, PFS, etc.

↳ Transfer payments may receive long term repays but not reciprocal payments.

* Subsidies are TPs from Govt. either to Firms or H.Hs

* Taxes are TPs from H.Hs or Firms to Govt.

Those who pay maximum taxes receive minimum subsidies.

Those who receive maximum subsidies pay minimum taxes

} Hence it is more clear that subsidies & Taxes are TPs.

[Grants, Pensions, Donations, Scholarships etc. are also forms of subsidies]

CLOSED ECONOMY:

Only the domestic ~~economies~~ sectors are interacting with each other

Ex: Only Indian Firms, Banks, HHs.

External Sector

Refers to any foreign firms, foreign Banks, foreign Govt, foreign Fin. sector. (i.e)- Anything which is foreign.

Net factor Income from abroad:

Factor Income from Indian H.Hs bring from abroad − Factor Income of foreign HHs take from here (Ind)

Bonus — May / may not be TP ?

Interest — Not TP

Savings } Not payments.
Borrowings } Just ways of mobilising finance

Toll taxes — Weak examples of TPs bcos (ex: truck & cycle pays diff. taxes for same service)

Remittance <-> Net factor related Income ?

Open Economy:

Where domestic sectors also interact with the External Sector.

Roughly from 1991, we've been following open economy

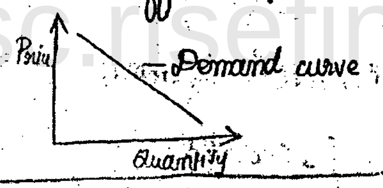
MICRO ECONOMICS

* Relationship b/w Quantity & Price of Goods & Services:

DEMAND : Quantity of a good that consumer is willing to buy at different prices.
(from P.O.V of consumer)

SUPPLY : Quantity of a good that Producer is willing to sell at different prices.
(from P.O.V of producer)

LAW OF DEMAND



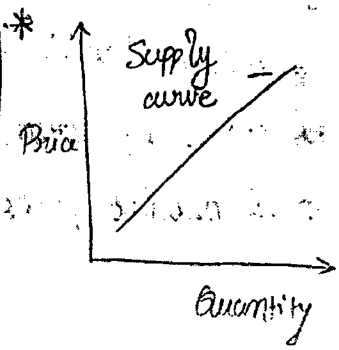
$\boxed{\text{Quantity demanded} \xrightarrow{\text{Inverse}} \text{Prices}}$ *

* – Other factors constant

Other factors – Any factor influencing the qty demanded other than price.

LAW OF SUPPLY

$\boxed{\text{Quantity supplied} \xrightarrow{\text{Direct}} \text{Prices}}$ *

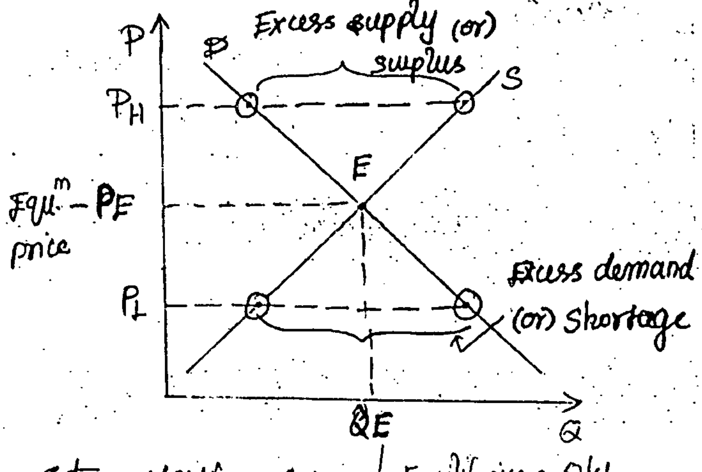


* – Other factors constant

Conditions needed for law of D&S:

1. Homogenous quality of G&S. } More appropriate in Agriculture
2. Large no. of Buyers & sellers.

Interaction between Demand & Supply: (or) among Market Forces:



E ⇒ Market Equilibrium

The pt at which the consumer is willing to buy the quantity the producer is willing to supply at the same price.

Interpretation 1:

Equilibrium is desirable because of Optimal usage of Resources.
↓
Zero wastage & Zero Scarcity.

In Public Vs Private sector
- If private sector is given greater role, there is more probability of having equilibrium. (?)

---

* When there is surplus, if assumed no intervention by Govt, the prices will fall ⇒ if market forces interact freely
* When there is shortage, if assumed no inter. by Govt, the prices will rise. ⇒ if market forces interact freely.

⇒ In most countries, Govt procures grains @ Market price

⇒ WTO doesn't allow export of subsidized goods (MSP is a kind of Govt subsidy, so it becomes subsidised good & can't be exported)

Interpretation 2:

- In case of surplus or shortage (i.e) a disturbance in equilibrium, if the market forces are interacting freely without govt intervention, Invisible hands of Market (Demand & supply) will lead to Equilibrium automatically.

Adam Smith

When Govt Intervenes...

Market forces no longer interact freely & hence we will not be able to reach equilibrium.

Ex: When Govt announces MSP (Min. Support Price) at a greater price then there is a surplus coming (Law of supply) but the price can't go down naturally (Law of Demand can't work) & hence can't reach equilibrium → No optimal use of Resources.

↳ But MSP is good for Farmer's Welfare. So, in order to tackle this crisis it can do: Management of Surplus/shortage

Adequate storage & Distribution

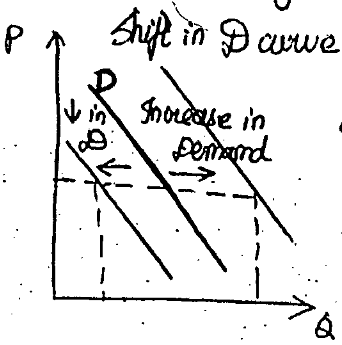
CHANGE IN DEMAND & SUPPLY:

It is the change in other factors (which were assumed constant in law of D&S) which are bound to change & not remain constant always.

1. Income:

Increase in Income
↓
Increase in Demand
[Increase in Qty demanded @ All prices]

Shift in D curve

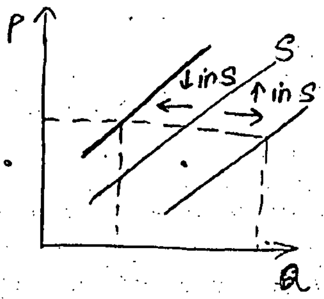


↑ income, more quantity at same price
↓ income, less quantity at same price.

2. Input Prices:

↓ input prices ⇒ ↓ avg. cost of production leading to Increase in Qty supplied @ All prices

shift in S curve



↑ input prices, less supply at all prices
↓ input prices, more supply at all prices.

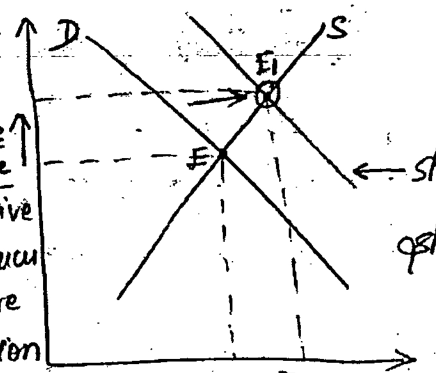
Nx is -Ve for India as we import more than we Export ⇐

3. Better Technology:

Better technology means more easy production (even if tech. costs, it would still be efficient in saving labour, time, resources etc..) hence ⇒ ↓ in avg. cost of production ⇒ ↑ in Qty S @ all prices

Ex: 7th pay commission ⇐ will ↑ GDP with ↑ Inflation

Equilibrium Shift:



Increase ↑ in price [Incentive for producer for more production since cost of production has not ↓ even though income ↑] ⇐ Empherical interpretation.

Increase in Qty

← shift in D curve due to ↑ income hence shifts Equilibrium too.

— — — — — — — — — — End of Microeconomics

ECONOMIC GROWTH & INFLATION:

↳ Economic growth → measured by GDP

↳ Inflation: It is the Rise in General price level of G & S.

General price level → CPI, WPI

⇓ Average of prices of diff G+S

↳ GDP by Expenditure method: (or) $\boxed{\text{DEMAND SIDE OF GDP}}$

GDP = C + I + G + NX

C ↑ Cons. EXP; I ↑ Invest. exp; G ↑ Govt. EXP; NX ↑ (Export − Import)

If GDP ↑ due to:

1. ↑ Consump. exp. ⇒ Reflects ↑ in Income → R.shift in D curve → ↑ General price level → ↑ Inflation
2. ↑ Invest. exp ⇒ More produce → due to more demand → due to more income [again into same flow]
   ⇓ One more interpretation at back
3. ↑ Govt Exp ⇒ Most of Govt. EXP goes to HHs → so ↑ in Income

When Economic growth takes place due to Demand side of GDP particularly due to ↑ in consumption expenditure, it will also be associated with Increase in Inflation. } Consumption led Growth.

In Japan, more elderly people – So ↓ econ. growth bcos of ↓ consumer expenditure ⇐

— So Japan govt. put –Ve. interest for deposit on banks.

↳ INFLATION – GROWTH CONFLICT

⇓ Not always bad

⇓ Always Good

↓ As long as it is under control – lower inflation

↓ Incentives to producer — Zero Inflation hurts producers.

Problems with ↑ Inflation:

→ Bad for consumers in general

→ Worse for low-income consumers.

Lower Inflation: (In case of India) ← differs from country to country

As long as Below 5% per annum.

Types of GDP Growth / Economic Growth:

* Consumption led Growth

* Investment led Growth.

→ In India we've seen mostly Consumption led Growth because of Size of Population, Age-Structure

↓ Demographic dividend = More young ppl (< 35 age)

✓ As pop. ↑, more consumption is bound to happen, hence growth.

⇒ The future strategy in India must be to drive Investment led Growth; Bcos

↳ cons. exp. naturally happens, No worries there
(naturally happens: Demand is always ↑ [R. shift of D. Curve])

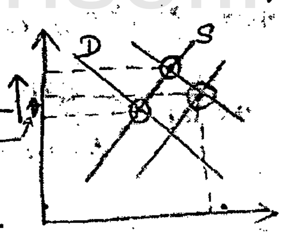
↳ there is more scope to improve Investments.

↳ It is less Inflationary than Cons. led Growth.

↳ Better technology will come & better productivity (through more human capital formation etc.,) which reduces the Avg. Cost of Production ⇒ Increase in Supply

R. shift in S curve (already R shift in D curve is there).

Supply of qty increases without much rise in price than in cons-led-growth



↳ In India, however Consumption is more than Invest-led growth so prices will be higher — but ↑ in investment will help control inflation.

If ↑ investment
- ↓ avg. cost of production → less Inflation.
- No change in avg. cost of production → More inflation.

TYPES OF ECONOMIC CRISIS:

1. Slowdown ⇒ Decrease in GDP growth rate

2015
→ Q1 - 7%
→ Q2 - 6.8%
→ Q3 - 6.5%

} GDP still increases only growth rate ↓

2. Recession ⇒ -Ve GDP growth rate for 2 consequtive Quarters.

2016
→ Q1 + 1%
→ Q2 - 0.4%
→ Q3 - 0.5%

} GDP itself decreases. No growth, rather worse.

SOLUTIONS FOR CRISIS

INDIA HAS NEVER FACED RECESSION. only slowdown.

Even after $\boxed{\text{2008 crisis}}$ — (?)

1. Fiscal Policy:

Any policy related to Govt. expenditure & Revenue.

⇒ Types of Fiscal policy:

(i) Expansionary - Govt. Exp > Govt Revenue ⇒ C ↑ I ↑ ⇒ ↑ GDP growth ↑ Inflation

(ii) Contractionary - Govt. Exp < Govt. Revenue ⇒ C ↓ I ↓ ⇒ Lower GDP growth ↓ Inflation.

*. Fiscal policy can't solve Inflation - Growth conflict; but can manage it by following (i) or (ii) situation specific.

* Should take Expansionary:

→ Slow down/Recession

→ Lower inflation - shouldn't take during higher inflation.

* Should go for Contractionary
  ↳ During High Inflation.

Expansionary policy:

But, generally India follows this because
→ Socio-economic reasons
→ Political Gains.

MONETARY POLICY

Any entity in Economy except Banks & Govt.

Related to **MONEY SUPPLY** ⇒ Amount of $\boxed{\text{money}}$ with $\boxed{\text{Public}}$

Liquid cash ← ↓ Currency + Demand Deposit.

⇒ **Demand Deposit:** - Readily available for purchase

It is that part of bank deposits which can be easily demanded / withdrawn.

Central Bank is responsible for this Monetary Policy.

⇒ RBI – India ; Federal Reserve – U.S.

⇒ Now - MPC (Monetary Policy Committee) < 3 members (RBI) ; 3 members (Govt. Appointed)
  ↳ Chairperson – RBI Governor

Types

EXPANSIONARY

RBI encourages banks to give cheaper credit to Public → ↑ Money supply → ↑ Investment Exp, ↑ Consump. Exp → GDP growth + Inflation

CONTRACTIONARY

RBI encourages banks to give costlier credit to public → ↓ Money supply → ↓C, ↓I → ↓GDP + ↓ Inflation

Ex: DENOMETISATION

Fiscal policy	Monetary policy
- Focuses more on consumption	- Focuses more on Investment
- Through Govt exp. & Revenue.	- through credit
- Generally Expansionary * (subjective to situation)	- Generally contractionary * (subjective to situation)

⇒ sometimes they will support each other: (all this is rare)

Ex: post 2008, Both FP & MP were expansionary — to pull up from slow down.

↳ ⇒ $\boxed{\text{RBI}}$ Vs $\boxed{\text{Govt}}$

RBI → priority - control inflation.

Govt → concerned more of growth.

Inflation Growth conflict

SUPPLY SIDE CONSTRAINTS / BOTTLENECKS

⇒ Not much in NP or textbooks

It refers to any factor that leads to the increase in overall cost of production in entire economy.

Reasons:

→ Higher prices of crucial inputs. → Everyone gets affected

Ex: ✓Crude Oil – transportation costs
✓Coal – Electricity
✓Iron ore – steel

Affects all of us

→ Lack of technological development.

→ Poor agricultural performance → ↑ Food price → Demand for higher wages esp. from Informal sector (maj. work force in India)

↳ Here labour is also crucial input.

⇒ Monetary policy doesn't influence this directly

Impacts:

⇒ Higher $\boxed{\text{inflation}}$

[Until now (till NP) we were talking about INFLATION called "DEMAND PULL INFLATION" (DPI) caused due to consumpt. exp. predomin.]

↳ But this inflation here which is due to ↑ COP is called "COST PUSH INFLATION" (CPI) (or) "SUPPLY SIDE INFLATION"

CPI – is out of compulsion of higher COP – supplier not happy

DPI – supplier/producer was happy.

⇒ Slow down/Stagnation (may lead to Recession – but rare)

↳ Because less incentive for producer to ↑ production.

↳ Consumer will have lower purchasing power → ↓ Demand

↳ This is the worst form of crisis ⇒ SLOW DOWN + HIGH INFLATION

↳ Before we had types of crisis:

- Slowdown + low inflation
- GDP ↑ + High inflation.

↳ Such worst situation is rare & was seen so far ~~only~~ in 1970s:

⇒ OPEC Crisis

↑ crude oil prices (due to political crisis in Middle East countries)
↓
↑ C.O.P in global economy (as most countries were ~~export~~ importing crude oil)
↓
↑ Inflation + Slow down

$\boxed{\text{STAGIFLATION}}$
⇓
Stagnation (slow down) + Inflation ↑

↳ 1991 – BOP crisis – somewhat similar

* Worst affected ⇒ Zimbabwe – last decade
⇒ Venezuela – Recently

Solutions:

FP & NP can solve this crisis only to a very limited extent.

↳ It can solve only stagnation but at cost of worsening Inflation. (Expansionary policy)

Hyper Inflation (HI)
↓
Surpassing 100% Inflation rate

Ex: Germany – Great depression – 1000%.
Zimbabwe – last decade – 500%.

↳ Decline in Currency Value is the worst effect in HI after which economy can't continue ⇒

⇒ public will loose faith in Govt ⇒ Econ. Disaster ⇒ Social Unrest

Summary:

- Too much of Expansionary policy is undesirable.

- Contractionary MP & FP is even worse. It will take stagnation to Recession & will not counter supply side inflation (It may be good only for demand side inflation).

So what is the solution?

* Policies to Decrease the C.O.P in the Economy.

Ex: ⇒ Better technology in all sectors. (in one is not enough)

* Some degree of Expansionary policy is needed.
  - Loans; Subsidies

↳ Only those Expansionary policy which is clearly linked to ↑ productivity

* Anything to ↓ crucial input prices. - ↑ Agri. production (to ↓ wages)

Ex: - Get more Reserves
  - Substitutes of resources
  (Shale gas — Subs. for Crude Oil)
  U.S

India's Case (2008 - 2014)

Stagflationary condition, even though not worse case.

From 2008: Gradual slow down

2013-14: Peak inflation in India

Reason ⇒ Crude oil prices ↑ (Global factor)

$\underbrace{\text{↑ Coal, Iron ore price}}$

⇓

Non-transparent allocations in coal block & Iron block auctions.

So SC went on to Ban mining of Iron ore. (Recently SC acquitted those ppl of all charges.)

2014 :- Reduction in crude oil prices.

- Govt increased mining & prices went down.

2018 : - Gradually again crude oil prices are going up.

- Fears of stagflation are back.

So we are going to (RBI) ⇒ (MPC) contractionary MP.

Govt - ↓ tax on petrol & Diesel is the simplest what can be done.

Crude Oil Prices :

Determined by a mix of Economic & global political factors.

Economic ⇓	political ↙	political ↘
Limited production by OPEC & non-OPEC countries. Russia	uncertain US policy	Turmoil ↓ - Middle East - Venezuela

$ is the most globally accepted curr. ⇒ Iran Nuclear Deal - US out - sanctions on Iran

—— × —— × ——

i) Definition

ii) It results in both Slow down + Cost push Inflation called STAGFLATION.

iii) India also went through such situations during 2008-2014 & it is emerging again with recent increase in crude oil prices along with lower agricultural growth.

iv) FP & MP alone can't solve this problem unless it is increasing Productivity. Some other policies which can solve it are:

a) Economy wide Technological Reforms

b) Adequate supply of crucial inputs by finding new reserves + by finding substitute for crucial inputs.

c) Productivity driven Agri. growth to keep wages under control.

OPEN ECONOMY CONCEPTS

* Foreign Currency Exchange rate
  - Rate @ which a foreign currency ($) can be exchanged for Domestic (₹) currency. (Rs/$ exchange rate)
  - Price of 1$ given in Rupee terms.

Determination of Exchange Rate

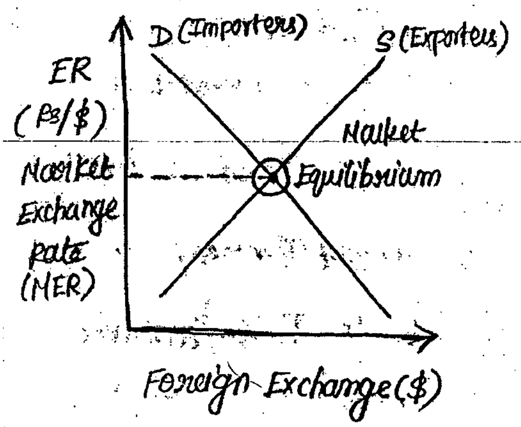
3 systems:

1). Fixed Exchange Rate: By central bank in consultation with Govt. (Till 1970s this system was followed globally; In India till 1991)

Both exact opposites

2). Flexible / Floating / Market ER system: Market forces playing their role
↓
Demand & supply for foreign currency ($) in the domestic economy (India)

- Main demand — Importers - Purchase $ ~~get~~ give ₹. ⇒ Will prefer Lower ER
- Main Supply — Exporters — Sell $ get ₹. ⇒ Will prefer Higher ER



- The dynamic D & S causes fluctuations in Equilibrium & hence by MER.

3). <u>Managed Floating Exchange Rate system:</u>

- ER is generally market determined. But sometimes it is managed by RBI.

- India at present follows this system.

where MER is used:

1. In all International Transactions.

[International Comparison of GDP ⇒ MER can't be used for this purpose as Import is not part of our GDP & only 12% of our GDP is exports] ⇓ poor reflector it will be

PPP ER (Purchasing power parity based ER)

⇓ Equality of PP b/wn Indian & American.

↳ common consumption Basket [MC Donald's Burger] - Book Roopa Pal

↳ This is complex & time consuming as common consumption Basket is dynamic.

↳ This PPPER is very useful when in need except for International transaction. [EX: GDP comparison].

MER (Rs/$).	PPP ER (Rs/$)
relatively much higher (Rs.67/$) ⇓ less exports	relatively much lower ≈ (Rs.30/$) ⇓ common consumption Basket is cheaper (Cost of living is lower)

⇒ MER > PPP-ER

⇒ $GDP_{MER} < GDP_{PPP}$

GDP_{MER} ⇓ Not even in top 5

GDP_{PPP} ⇓ 3rd largest Economy after US & China

NER : NER is the ER determined by the interaction of demand & supply of a foreign currency in the domestic economy by the exporters, importers etc.

PPP-ER

PPP-ER refers to the price level in rupee terms needed to buy the same consumption basket that can be bought with 1$ in U.S. To calculate it, the ratio of expenditures on common basket in rupee to dollar terms is taken.

BOP Accounts

Accounts ⇒ Summary of Receipts & Expenditures

↳ Account mainted by India w.r.t. International transactions.

↳ No domestic transactions.

NET RECEIPTS – Corresponding Receipt – Expenditure

NET EXPORT – Export – Import

India is a global leader in IT net service export; Also BPO.

BALANCE OF PAYMENTS ACCOUNTS

- BOP Accounts:

Receipts & expenditure summary.

Account maintained by India w.r.t. International transactions.

NET RECIPTS = Receipt - expenditure ↳ No Domestic transactions.

NET EXPORT = Export - Import.

Parts of B.O.P Accounts:

1) Current Account: (short term) < 1yr

↳ (i) Net Exports (of goods only)

⇓

Merchandise trade (or) Visible trade.

↳ (ii) Net Invisibles

⇐ – a) Net services Exports

(value of services export - val. of ser. Import)

– b) Net factor income from abroad. ⟸ More often -ve for India. GNP < GDP

(factor income Indian residents bring – factor income foreign residents take)

- Net Compensation of Employees (+ve for India) (salaries in – salaries out) WAGES
- Net Investment Income (-ve for India) (Any type RENT, INTEREST, $\boxed{\text{PROFITS}}$ Indian res – foreign residents) ⇐ In India; Profit outflows > Profit inflows

4 Factors of income – Wages, Rent, Interest, Profit

c) Net Transfers ⇐ One sided payments – but all are international transfer payments

Net official Transfers

(Grants coming in - Grants going out)

Net private Transfers ⇐ Ex: NRI transfers ; NGO grants
Non government transfers.

Similarity
Indian households receive forex
~~Diff~~ Residents vs Non-residents

NET RENITTANCES:

↳ Net private transfers
+
↳ Net compensation of Employees

Remittances:

Total amount of foreign currency received by Indian households from abroad.

Deficit: Receipts < Expenditure.

Surplus: Receipts > Expenditure.

* INDIA *

1) We get highest Remittances in the world.

2) We lead in Net Service Exports

I) Trade Deficit:

- Imports > Exports (value of goods)
- Net exports < 0 ⇒ -Ve

Also called – B.O.T. deficit
– Merchandise trade deficit

} ⇒ Trade Surplus → Reverse to deficit.

2] Invisibles Surplus:

- ✓ Net invisibles > 0 ⇒ +ve
- ✓ Sum total of:
  - i) Net services exports
  - ii) Net factor income from abroad.
  - iii) Net transfers

3] CAD - CURRENT ACCOUNT DEFICIT

$$\left.\begin{array}{l}\text{- Net Exports} \\ + \\ \text{- Net Invisibles}\end{array}\right\} -\text{ve} < 0$$

Total Receipts on current account < Total exp. on current account

↳ In India:

- ✓ CAD ⇒ -ve
- Trade deficit >> Invisibles surplus.
- Exceptional cases:
  - ↳ 2002 - 2004 ⇒ we had good economic growth till 2008.
  - ↳ CAS - current account surplus. till 2005 we had surplus.
- Recently:
  - CAD regularly increased

Invisibles deficit

Reverse of I. surplus.

INDIA

✓ Trade deficit ⇒ -ve

- except for ancient times, we always had trade deficit.

Why?

i) Import dependent country
↳ Crucial inputs [crude oil]

ii) Not a renowned exporter of goods apart from being known for service exports.

✓ Invisibles surplus ⇒ +ve

Why?

i) Services exports
ii) Remittances

- Even before 1991, we had good invisible surplus - Remittances.
  - ↳ Skilled & semi-skilled migrants from 1970s.
  - After 91, it increased
  - ↳ Remittance + Services

__Why?__

Crude oil price hike

⇓

Trade deficit

⇓

CAD

__Generally:__

* CAD < 2% of GDP.

__Now:__ we have > 2.5% of GDP.

__Higher deficit?__

- Increasing economic dependence
- unstable.

__NCERTs__

Macroeco – B.O.P chapter.

↳ follow nomenclature used in class – that is outdated.

⇒ __Economic survey__ – B.O.P chapter

__2nd Part of B.O.P Acc.__

2] __CAPITAL ACCOUNTS:__ (long term)

__PULAPS__

FDI, FPI, ECBs, NRI deposits

i] __Net external Assistance:__

↳ Official loans (coming-going)

- From governments — Ex: India gets from Japan
- From International organisations — from world bank, IMF

(centre or State Govts)

↳ Loan repayments (deducted)

__Ex:__ India gets loan from WB.

- Loans given in installments,
- After certain years interest, debt payment starts.
- If 10 years is maturity period ⇒ (1 to 9th year payment) ⇒ in (i)

(10th year) ⇒ in (ii)

ii] __Short Term External Debt:__

- the final year repayment

→ that part of external official debt which should be completely repaid in the current year ←

Reason of separation:

- this debt can't be postponed – to be paid immediately.

→ Govt needs clear reflection of what is to be paid soon.

↳ If not paid, we will become **Defaulter.**

↳ Credit rating will go down.

we won't get foreign investments

we won't get official loans.

Why not net?

It doesn't get anything; But only pay.

Generally:

(ii) must be as low as possible.

Ex: Greece crisis

- (ii) kept on increasing.
- started taking more loans to pay past loans – $\boxed{\text{DEPT TRAP}}$

∠ Additional liabilities – Vicious circle.

$\boxed{\text{ERs}}$ – will play role in entire B.O.P

RBI will have direct or indirect role in all B.O.P issues.

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iii) External Commercial Borrowings (ECBs):

- Commercial loans – mostly by private companies.

→ ECBs means commercial loans taken by Indian companies from the Foreign Banks

Why from outside?

- Lower interest rates – Cheaper loans.
- PSUs generally don't take.

IMF – makes general laws

RBI – within India will regulate ECBs of private companies

↳ ECBs usually undergo multiple regulations – IMF, RBI, ...

↳ Not all companies can take – only sizeable economy companies can get – check by RBI as well as IMF.

iv) Net Banking Capital: (NBC)

Interest rates (both domestic / international) play important role in B.O.Ps (ECBs / NBC) exist b/cos of it.

NRI Deposits:

→ The long term bank deposits kept by NRIs in India ←

↳ why keep here? ↑ interest rates.

↳ Incoming deposits − Outgoing deposits.

Banking capital:

→ Residents of one country have long term Bank deposits in other country ←

v) Net Foreign Investment:

↳ Most important part − (Separately also)

Net FDI (Foreign Direct Investment)

↳ Foreign firm invests in specific Economic sector of India ←

Ex: POSCO − South Korean steel company − invested in Odisha.

Net FPI (Foreign portfolio Investment)

- FII − FDI in India is almost FII.
- QII − negligible in India.

↳ Foreign Financial institution invests in a portfolio of financial assets / instruments ← (Banks, MFs − combination or variety of things)

⇓

(shares, bonds)

Which is better?

Generally FDI.

Why? Benefits of FDI over FPI:

i) Technology transfers:

- FDI can bring better technology ⇒ Posco in Odisha - better quality of steel production.
- But not so easy as that country will have worked hard to develop that tech.
- FPI — No tech transfer - pure financial investment/gains.

ii) Employment:

- Job creations.

iii) Long term:

- serious investments — specific sector focus

Serious problem of FPI:

- Short term in nature.
    - ↳ Come in quick - go out quick

⇒ This results in VOLATILITY in financial markets.

↓

Enter & exit in great amounts

HOT MONEY ⇒ Negative/derogatory term referring to FPI. (due to volatile nature)

INDIA

Economic performance

↕ poor co-relation

share market hike

↓

Due to

⇒ FPI - Bring in lot, goes out when other countries become favourable.

But....:

- Not every FPI is short term;
  - particularly BONDS.
- We must not call it Hot money
- Generalization is bad

Change of FDI in India:

change started roughly from 2000.

Before 2000: Most FDI in industrial sector

Post 2000: Gradual increase in FDI in Services sector ⇒ Banking, Retail, etc. Insurance, Telecom.

Services FDI (mainly retail)	Industry FDI
Not much physical capital.	Brings physical capital.
Money through share market - after targeting a particular company, buys major shares -	More & better quality jobs
	Long-term.

FDI in Retail:

Best ex: Walmart bought Flipcart.

- ↓ physical capital
- ↓ Job-creation; eat up jobs in case.
- No tech-transfer
- Not long term.

Problem:

→ Once FDI enters share market, the Difference between FDI & FPI gets narrowed down ⇒ Both through share market.

→ We can't force companies to get from many companies.

FPI: If they decide to buy share from only one company, similar to FDI it becomes. ; → FDI in services has weaker benefits than traditional FDI ⇒ No tech transfer; ↓ Job creation.

Indian rule:

- As long as foreign company has ≥10% shareholding in a company, it will be considered ⇒ FDI

- ≤10% ⇒ FPI.

why 10? Just for a threshold; <10% - means financial gain. Indication - serious involvement;

But on the whole:

FDI still better than FPI

* FIIs (Foreign Institutional Investments)

As long as FPI is made by Financial Institution, it is called FIIs.

* QFI (Qualified Foreign Investment)

Investment made by Foreign individual/group of individuals.

⇒ Surplus & Deficit:

Capital Account
- Surplus → (i)+(ii)+(iii)+(iv)+(v) >0
- Deficit → (i)+(ii)+(iii)+(iv)+(v) <0

INDIA

Surplus: - Destination country

- More ~~FDI inflow~~ \$ inflow than \$ outflow

* BOP Surplus: — INDIA

(Current + Capital) Account Surplus — 2013 – BOP deficit

* BOP Deficit: — 1991 – severe BOP deficit (BOP crisis)

(Current + Capital) Account Deficit

- Not good for economy
- Less foreign currency earned than ~~sold~~ spent.

3rd part of BOP Acc:

3] International Reserves Account: (IRA) ⇐ Forex reserves.

* Balancing Account ; Regulated by RBI

- ↑ BOP surplus ⟹ ↑ Put in Intun. Res. Account.
- BOP deficit ⟹ ↓ IRs.

How to tackle BOP deficit?

- Through IRs
- IRs is a cushion

⇒ A country should maintain sufficient International reserves which is stable.

Composition of IRA:

- → Foreign Currency Assets — \$, €, £, ¥ (Renminbi) Yuan
- → Gold
- → SDRs (Special Drawing Rights) — Currency of IMF — Avg. value of 5 currencies (Yuan the most important)
- (RTP) → Reserve Tranche Position with IMF — Part of IMF quota that can be accessed by IMF member country

International Reserves must be STABLE which is ensured by the above composition (5 currencies, SDRs, $\boxed{\text{Gold}}$) so that it can be considered as safehold in case of BOP deficit.

BOP Crisis: When International Reserves (Forex reserves) are not able to support or balance BOP DEFICIT.
[BOP deficit + Inadequate international reserves]

↳ In such a case we will be borrowing from IMF and there are other ways to deal with it also.

INDIA - BOP Crisis: (1957-65, 1981, 1991)

① 1957-65

2nd FYP, (1956-61) (Mahalanobis Mo) — Heavy Industrialization Iron & steel

→ Dependent on Imports — But → lack of Exports promotion
- → Machineries
- → Raw materials

↓ Receipts, ↑ Expenditure → CAD → BOP Deficit + ↓ Forex reserves → BOP Crisis
- Severe
- lasted 8 Years

IMPACTS:

① Stop Industrialisation in heavy sectors

② Stop the basic Industrialisation itself $\xrightarrow{\text{TO}}$ Agriculture (GR - 1964)

② 1981 BOP crisis:

→ Mild, less serious crisis

→ ↑ Import ; ↓ Export

↳ We took loan from IMF & paid before maturity & relieved decently

LESSON:

Post-1985 ⟹ Increased exports promotion.

↳ lesson from ① & ② crisis.

⇓

Even then led to 1991 crisis.

③ 1991 BOP Crisis:

Indian economy made pathbreaks after & due to this crisis.

Why this crisis despite exports promotion post-1985?

① ↑ in External debt of Government (since 1987) → started BOP deficit.

② Gulf war (1990-91) - Iraq, Kuwait (Sadam)

(i) ↳ ↑ in Crude oil prices → ↑ Imports

(ii) ↳ ↓ in Remittances (More Indian diaspora there)

→ ↑ CAD → BOP Deficit + ↓ Forex reserves → BOP CRISIS

⟹ Most severe BOP crisis of India ever.

⟹ Our capital account too was less then.

Note: In $\boxed{\text{2013 BOP issue}}$ → More BOP deficit than 1991 / → But we had enough Forex Reserves } → So no BOP Crisis

SOLUTIONS: (Applicable to both BOP Crisis & BOP Deficit).

Why crisis? RECIPTS < (Regularly short of) EXPENDITURE

So solution? ↑ Receipts and ↓ Expenditure

① Improvement in current Account Balance (or) Reduction in Current Account Deficit (CAD):

* Export promotion
  - Started post-1985
  - We've been good in SERVICES export
  - Still lacking in the GOODS export.
* Reducing Imports Dependence.
  - Difficult for India all the more bcos our imports are CRUCIAL - $\boxed{\text{Crude Oil}}$
  - Even if we reduce it will affect economy
  - We can reduce — less crucial imports (or) Find substitutes for less crucial imports.

② Improvement in Capital Account Balance:

- FDI
- FPI
- ECBs
- NRI Deposits.

FPI, ECBs → Introduced after 1991

- Strictly post 1991 phenomenon.

⇒ Capital account surplus may not be always good for economy

Why? INCREASE IN LIABILITIES for Economy — loans are always a liability (ECBs) & we pay in dollars back.

ECB → \$ in, but \$ out while repaying with interest.

NRI deposits → We pay more interest to them.

FPI → Now they are moving to US for better interest rates

FDI → Indirectly a liability sometimes. (Shares, bonds)

<u>Why</u>?

↳ In <u>services</u>, they may behave like FPI — short term (through share market)

↳ Profit outflow possibility

Implication intended:

→ Despite all these, FDI remains a preferred type of investment

→ Capital account balance improvement is not bad, but over dependence on it is bad (due to ↑ in liabilities)

⇒ Any country in CAD deficit will have to seek help from Capital account for financing.

\$ 425 Billion OUR FOREX

→ Mainly from Capital account — so we (FPIs, ECBs) need to be careful of the risk of liabilities.

Current Account	Capital Account
✓ Permanent	✓ Temporary — we need to pay back.
✓ Very Good always.	✓ Good but over-dependence bad

③ & ④ th related to IMF loans → IMF Conditionalities

③ Contractionary Policies:

↳ It is one of the IMF conditionalities

Contractionary policies → Lower GDP growth → ↓ Per capita Inc → Lower growth in purchasing power → Lower Demand in Imports → ↓ Expenditure

PROBLEM / CONTROVERCIES:

↳ IMF is telling a country to go into SLOWDOWN when it is already in BOP deficit/crisis — No country will voluntarily do it.

↳ It will hit WELFARE activities of Govt in immediate & in future -- Painful for nation.

✓ In 1991 → we too followed contractionary policies for IMF loan.

✓ GREECE CRISIS → It too adopted Contractionary policies — CHAOS

↳ Medical welfare activities

↳ Empty banks

↳ Pension etc...

Why IMF doesn't understand it ?

Bcos IMF is run by western economists — same western economic theory can't be applied to all countries.

IMF approach —— You did something wrong leading to Crisis
So I will give a loan but DISCIPLINE you

But actually, in most BOP cases, a country is not at major fault but were due to EXTERNAL FACTORS. For ex:

In 1991, Gulf war was the prime reason.

* So the basic premise of IMF is wrong.

[Ex: LATIN AMERICAN nations will never go to IMF ?]
VOW – bcos they were past victims.

4 Currency Devaluation:

- Relative to other currencies.
- Done by central bank (RBI) of the country.

$$Rs. 67/\$ \xrightarrow{RBI} Rs. 69/\$$$

$$₹1 = \$\frac{1}{67} > \$\frac{1}{69}$$

→ With devaluation, Exports are likely to increase (or)
Exports become cheap.
↓
Bcos. Exporters are happy with ↑ Exchange rates.

→ will reduce Imports.

→ Simultaneously ↑ Receipts ; ↓ Expenditure ; So,

IT IS THE BEST SOLUTION FOR BOP PROBLEM.

Despite, being a good solution, it is NOT AN IDEAL SITUATION for INDIA – Why ?

1. Dependence on Crucial Imports – so we need to keep importing at high prices.
2. Exports-Oriented Sectors dependent on Imported Raw materials

↳ Production costs of exporters will go up — ↑ Costs

EX:

IMPORT	EXPORT ← we are good at it
– Crude petroleum	– Refined Crude petroleum

So, we have to buy crude oil to export refined crude oil

— Gold	— Processed Jewellery

So, we need to buy gold, to export jewellery

Ideal solution for INDIA:

$\boxed{\text{* Promote those EXPORTS where Raw materials are domestically available *}}$

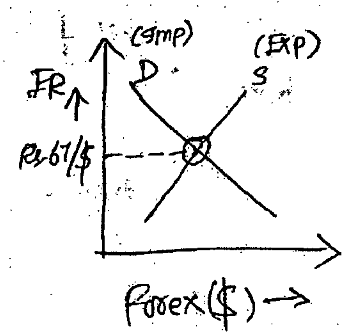
EX: Agriculture, Allied sectors, Small & medium enterprises (SME)

Overally, ① & ② better than ③
① better than ②
Ideal, however, is — ↑

EXCHANGE RATE MANAGEMENT
(BY RBI)

① Mechanism of Currency Devaluation:

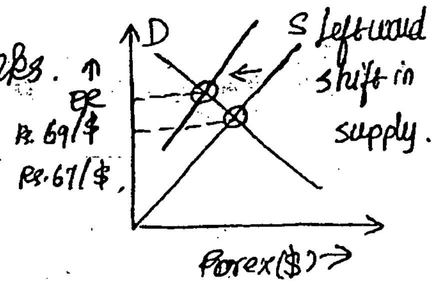
Forex Market
↓
Exchange banks (Commercial banks)



RBI will Buy $ from Exchange Banks.

↳ Result in less circulation of $.

And sell ₹ to Exchange Banks (EB)



$$RBI \underset{\text{Buy \$}}{\overset{\text{sell ₹}}{\rightleftarrows}} EB$$

↳ Result in $\boxed{\uparrow \text{LIQUIDITY}}$ (Ex. Rs. 50,000 × 67) in EBS

$\boxed{\uparrow \text{Money supply - Loans}} \longrightarrow \boxed{\uparrow \text{Inflation}}$

How to tackle Inflation arising from trying to devalue Rs..?

* <u>Contractionary Monetary Policy</u>.

STERILISED* INTERVENTION BY RBI

currency Devaluation + Contractionary Monetary policy

<u>RBI</u>
- Monetary policy regulator
- Foreign currency market regulator

} linked in above case.

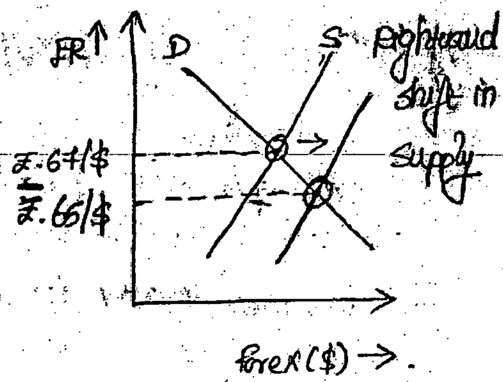
[*<u>Sterilized</u> - Anything to control inflation]

② Currency Revaluation:

$$RBI \underset{\text{Buy ₹.}}{\overset{\text{sell \$}}{\rightleftarrows}} EB$$

} Exact opposite of ①.

↳ Increased supply of $.



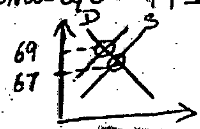
③ Currency Depreciation:

Rs. 67/$ ⟶ Rs 69/$

— Market Determined Completely — No RBI intervention —

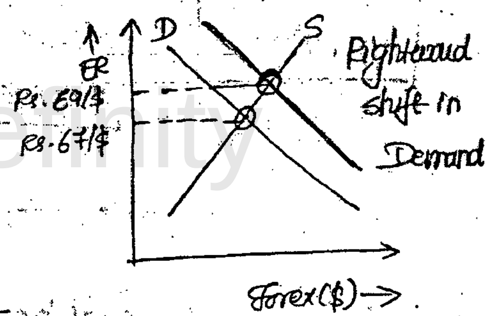
CAUSES:

I. ↓Supply
- Foreign capital outflow [outflow in capital a/c — FPI outflow]
  - ↳ Now happening in India.



- → No hand of RBI (other countries give better interest) — fully market determined.

II. ↑Demand
- More Imports
- → India is a dependen of imports



- ⟹ Higher CRUDE OIL prices — ↑ demand of $.

2010-2013 Heavy ₹ depreciation

⟹ 1) ↑Foreign capital outflow
2) ↑ Crude oil prices

④ Currency Appreciation:

Rs. 67/\$ ⟶ Rs. 65/\$.

— Completely market determined — No RBI. —

MAINLY due to:

- Foreign Capital Inflows (↑FPI)
- ↑ Export

→ ↑ \$ supply → Currency Appreciation

2014-2017	2003-2008
Better Rupee appreciation	Very good Foreign Invest. ↑ Rupee appreciation

—— x —— x —— x ——

Currency devaluation:

Under this process, RBI decreases the value of ₹ with respect to \$ by PURCHASING \$ and SELLING ₹ in the FOREX MARKET.

It increases the ₹/\$ ER making

Exports cheaper

Imports costlier

And VICE VERSA for Currency Revaluation.

Devaluation results in Higher Money supply as the Exchange banks can use excess ₹ to give loans to public. Therefore RBI follows a CONTRACTIONARY MONITARY POLICY to control Inflation. It is called STERILIZED INTERVENTION by RBI

Currency Depreciation:

It is a MARKET DRIVEN process under which ₹/$ ER increases either due to :

Higher demand for $ (Ex: Increase in Import) (or)

Lower supply of $ (Ex: Foreign Capital outflows)

And VICE VERSA for Currency Appreciation

—— × —— × ——

Impacts of Currency Depreciation (or) Devaluation:
Weaker (or) Falling ₹

(i) Cheaper Exports – same as devaluation

(ii) Costlier Imports

Impacts of Currency Appreciation (or) Revaluation:
Stronger (or) Rising ₹

(i) Costlier Exports

(ii) Cheaper Imports

⇒ We can't choose which is good b/w these bcos one affects importers & the other affects exporters

⇒ So, it has a MIXED IMPACT on economy

$\boxed{\text{2010-13 Supply side constraints}}$ → ↑ Inflation → ₹ depreciation → $\boxed{\text{Costly Imports}}$ → ↑↑ Inflation

↳ Happening now too (2018).

$\boxed{\text{2003-08 Currency Appreciation}}$ → Costly Exports → Affects exporters.

⟹ Both Depreciation & Appreciation are good as long as they are MODERATE and not much fluctuations.

$\boxed{\text{2018 ₹ Depreciation > 2010-13}}$ ⇒ Record Worst Depreciation.

Politically ⇒ No govt. can do much about ₹ appreciation or depreciation.

Weaker ₹ — Doesn't mean bad economy
Stronger ₹ — Doesn't mean Good economy
} Moderation is the key.

2 TYPES OF ER MANAGEMENT BY RBI

1. Over-depreciation of Re ↓ REVALUATION OF Re by RBI	Happened in 2012-13 (Happens now too)
2. Over-Appreciation of Re ↓ DEVALUATION of Re by RBI	Happened in 2003-08. It was a very good move bcos if it had not been done so, our Exports wouldn't have gone up which it did then

Devaluation:

It is a management — which means it shouldn't be done regularly. Once management is done then we've to let the market work.

Regular devaluation of currency by CHINA:

Since 1997, for two decades china has been doing it — To ↑ Exports.

Now it is not doing so because now chinese currency is part of SDR & IMF rules don't allow devaluation.

problem with regular devaluation:

It will lead to GLOBAL issue bcos when 1 country does, the other (esp competitors) also tends to follow. Competitive devaluation (or) Currency War

↓

LESS POTENTIAL IMPACT OF DEVALUATION

✓ RBI had been very disciplined in case of devaluation and has done only in situations of true need.

Nominal ER / NER :

Most of the countries trade in multiple currencies, inc INDIA (i.e) Not only ₹/$, but also ₹/€, ₹/£ etc...

NEER (Nominal EFFECTIVE ER)

⇒ Calculated by RBI

⇒ It takes a WEIGHTED AVERAGE of atleast 5 ERs.

✓ Simple average = $\frac{2+3+5}{3}$ ⇒ equal weightage for all.

✓ Weighted average = Diff. weightage/importance to diff-currencies.

For ex: ₹/$ ⇒ 55% weightage
₹/€ ⇒ 30% weightage
₹/£ ⇒ 15% weightage

} Rates Just assumption (Trade value of that currency in India — based on)

REER (Real Effective ER)

(Nominal → Real means, Prices (adjustment for price))

⇒ Adjusted for Relative price Differential

GDP growth
Nominal → Real means
Adjustment for Inflation
GDP
Adjustment for prices

Ex: Nominal depreciation of ₹/$ → 10% >

Inflation in India → 5%

Inflation in US → 3%

Real depreciation of ₹ w.r.to $ → 10% − (5% − 3%)

= 8% <

Why do we calculate REER?

RBI doesn't revalue when Nominal depreciation is more but waits for Increase in REAL DEPRECIATION. Bcos Nominal depreciation also involves our own inflation & other country's inflation.

Inflation	Depreciation
Reduction in value of a currency with relative to itself.	Reduction in value of a currency with relative to another currency.

REER - similar to PPP-ER

↳ But not same; only conceptually same

Relative price adjustment

NEER } → Not practised in real life
REER } → Just for policy making & academic & research purposes.

NEER (Nominal Effective ER)

NEER is the weighted average of BILATERAL Nominal exchange rates between ₹ & other foreign currencies where the weights depend upon the share of each currency in Indian Trade value. It is relevant as INDIA trades in terms of multiple currencies & not just $.

REER (Real Effective ER)

REER. When NEER is adjusted for RELATIVE PRICE DIFFERENTIAL b/w domestic country & foreign countries, we get REER.

It is relevant as value of currency changes with both

Change in price level &

ER

Change in REER removes the Impact of Price change.

Indian Scenario:

In INDIA, when ₹ depreciates w.r.t $, this Nominal depreciation is often more than Real depreciation. ∴ RBI while deciding on Revaluation waits till Over-depreciation in Real terms.

Buying Rate

the ER at which Exchange banks BUY dollars.

Selling Rate

the ER @ which E. banks SELL dollars.

this is usually ↑ higher

Bcos: PROFIT ⇒ selling rate − Buying rate

Our perspective / Buyer's perspective

We buy at selling rate & we sell at buying rate.

Selling rate & Buying Rate are determined by MARKET FORCES. (although certain banks charge little more, it is negligible)

CURRENCY CONVERTIBILITY

Why important?

It is needed in every part of BOP, bcos every part of BOP required currency conversion.

(1) Current account Convertibility: RBI doesn't regulate conversion of currency. INDIA has CA convertibility since 1994 with an exception of OUTWARD REMITTANCES.

Exporters & Importers can do their own conversions using MER. (i.e) they can take / borrow any

---

Does India have Capital account Convertibility ⇒ NO

But India has PARTIAL CAPITAL ACCOUNT Convertibility — due to less Regulation by RBI gradually.

FPI — Is the most affected by this.

- → In shares — Here it is relief bcos RBI regulation is less here.
- → In Bonds — (esp Govt. bonds) — RBI regulates (They can't buy bonds more than a certain value)

Support for capital Acc. Convertibility

1. Increase in Foreign Investment ⟶ ↑ GDP growth.
   - Bcos foreign Inv. doesnot come easily into India as they know it is difficult to exit bcos of NO Cap. Acc. Con.
   [For ex: 2003-08 period where India got ↑ foreign capital flow]
2. Benefit for Indian Investors in Abroad
   - Now Indians buy share only in India. We are not able to buy from Hong kong or other share markets.
3. Reduce Illegal Foreign Currency Flows.
   Ex: HAWALA. Some genuine businessman may need foreign currency but legally there is NO possibility. So he goes for illegal method. (Not all illegal flows are for Terrorism etc.)
   ↳ this is like Allow liberal trade to reduce smuggling.

Criticism of Capital Account Convertibility (CAC)

1. Economic crisis → Volatility of Foreign capital flows.

Any time any amount can come in / go out. Esp. they go out massively during economic crisis.

It actually happened $\boxed{\text{post 2008}}$ – Massive outflow of F.cap from countries which had CAC. Esp. South Korea.

But in INDIA – Massive outflow didn't happen but only gradually bcos we don't have CAC.

CAC acts as a CUSHION during Economic crisis.

It is becoming more relevant as economic crisis is now becoming normal in the world.

2. Rumours of Crisis

__Ex:__ 1997 East Asian crisis → they say it is worse than 2008

Thailand → South Korea → Taiwan → China → Hong Kong → Japan

Why? Due to massive foreign capital outflow.

Recent studies showed that another reason is:

Outflow of Domestic savings → Bcos of rumours of crisis their residents started converting savings into \$ & sent out to keep it save. → Due to CAC → In India we can't do this bcos RBI won't allow beyond a certain amount of our Domestic savings. And India is more vulnerable ~~to~~ to Rumours.

3. CAC $\rightarrow$ loses Independent Monetary Policy

when for.cap. inflow comes in — ↑ money supply

goes out — ↓ money supply

Now, RBI can predict this coming in & out hence can have independent monetary policy.

But, if we have CAC, RBI can't predict it as it may come & go in anytime & any amount.

Indian scenario @ present

A country has to choose btwn CAC & Independent Monetary policy. It can't have both.

For a country which is often troubled by higher Inflation Indep. monetary policy is crucial to control it.

India can't go for CAC simply bcos CHINA or S.Korea has it as we don't export even a fraction of what they do & they have lower Inflation & their Banks are more stable.

TARAPORE COMMITEE, 1997 (on CAC)

↳ CONDITIONS FOR CAC

India should check its preparedness based on foll:

i) Lower Inflation (Regular trend of lower Inflation)

ii) Lower Fiscal deficit or $\left(\frac{\text{Fiscal deficit}}{\text{GDP}}\right) \Rightarrow$ It should be 3% or <.

keeps macro-economy stable

↳ Benchmark of domestic stability

iii) Lower $\left(\frac{\text{Current acc. Deficit}}{\text{GDP}}\right) \Rightarrow$ below %

↳ Benchmark for International stability.

Twin Deficit ⇒ Fiscal Deficit & Current account Deficit

iv) Stable Financial Sector (esp. stable Banking Sector)

Cap. AD will bring in more volatility hence B.S. needs to be very stable to handle it.

Case of India – Is India prepared for Cap. AD?

India has done better in i) & ii) since 1997. But still regular lower inflation is still difficult for us.

On ii) too we have been better but still improvement, consistency required.

But we are always having =s times of Cur. AD.

Banking Sector too is not good/stable right now.

So, We are not completely PREPARED yet for CAC.

CAPITAL ACCOUNT CONVERTIBILITY

Def: CAC refers to a situation when a domestic currency can be converted to a foreign currency & vice versa at MER for capital account transactions in BOP without central bank's Regulation.

For ⇒ Its supporters in India argue that CAC will bring in more foreign investment by removing Entry & exit barriers &

lead to higher growth

⇒ Indian investors will also get an opportunity to invest in foreign capital markets.

⇒ It is also likely to reduce illegal capital flows.

Against:

⇒ However, CAC can also increase volatility of foreign capital particularly during an economic crisis.

⇒ Even rumours of a crisis can result in volatility under CAC.

⇒ CAC will also impact independent monetary policy of RBI as RBI cannot predict impact of capital flows on money supply.

MONEY & BANKING

3 classes

※ for prelims ✱
✓ Fiscal policy
✓ Monetary policy & Banking
Half of eco. qns comes from these 2 topics (in today's trend)

NCERT chapter on Money demand

Money Supply:

⇒ Amount of money with public.
(money ↑ Liquid asset; public ↑ except Govt & Bank)

⇒ Determined by RBI

→ Explicit factor determined by RBI

Money Demand:

Money demanded by public.

→ TRANSACTION DEMAND: Money as medium of exchange (or) for buying G & S. +ve rel. with income

↳ Mainly dependent on Income ⇒ ↑ Income → ↑ Demand.

→ SPECULATIVE DEMAND: Money as a store of value (for investment etc.) ↳ But actually money in liquid form

-ve relati. with interest rate

is not a good store of value [Affected by Inflation]

The SUBSTITUTES of liquid money for store of value are:-

- ▷ BONDS (Interest rate)
- ▷ FD (Fixed Deposit)
- ▷ SHARES
- ▷ GOLD
- ▷ Real estate etc.

But we here discuss on Money Vs Bond as store of value:

Speculative demand of money from substitute is actually demand dependent on Return from substitutes.

(i.e) Higher the Interest rate of bonds, lower speculative demand of money.

INTEREST RATE on BONDS ⟹ It is 'PRICE' of Money

↓

OPPORTUNITY COST of holding money

↓

Return on next best asset / what we loose out while we hold that asset.

✓ when we hold money we loose out Interest rate ⟸

Market Interest Rate:

It is the Interest rate determined through interaction between DEMAND & SUPPLY of money.

↳ All interest rates in an economy are correlated.

(when Govt. bond int. rates ↑, fixed dep int. rates also ↑)

↳ when one goes up - all go up ; one comes down - all come down.

RBI's expansionary monetary policy means:

Interest rates will be reduced

due to ↳ Excess supply of Money

RBI's contractionary monetary policy means:

Interest rates will be raised

due to ↳ Excess demand of money

Higher per capita income means

Interest rates will be raised

due to ↳ Excess demand of money

BONDS

* Bonds → Like a loan

→ Issuer ⇒ Taking loan

(Govt, Firms)

→ Investors ⇒ Providing loan

(Banks, HHs)

Loan	Bond
Loan is strictly btwn Bank & borrower & after a maturity period repay it with interest.	Bonds are not always strictly between only two parties. It may involve others too.
Loans are not Tradeable*	Bonds are Tradeable

* Tradeable - can be bought & sold multiple times.

3 things related to Bond:

1). <u>Interest Rate</u> → Market determined [pre 1991 – not market determined]

But once the bond is purchased, interest rate is <u>fixed</u>.

↓

this is what makes BOND, <u>less RISKY</u> Investment than SHARES

2). <u>Bond Price</u> → Market determined (Dep. on $\boxed{D}$ & S for Bond)

Since bonds are tradeable, they'll have price.

Supply is relatively consistent as Govt/firms issuing bonds will need a particular amount. But Demand for bond by buyer makes the difference – he may go to buy share if that goes up – so fluctuating.

Higher demand → Higher Bond price

Generally varies between Loan Amount & Maturity value

<u>For ex:</u> (Rs.100 Interest rate: 10% — Rs.110)

Never beyond maturity value

Mostly not less than loan amount

3) Bond Yield = $\dfrac{\overbrace{\text{Interest Amount}}^{\text{Fixed}} \text{ on Bond}}{\text{Bond price}}$

Bond yield $\xleftrightarrow{\text{Inverse}}$ Bond price

Now, recently Bond price has gone down due to excessive supply due to sale by foreigners. Banks are worried as they are loosing out due to ↑ Bond yield or ↓ Bond price.

Expected Interest rate on Bond $\xleftrightarrow{\text{Inverse}}$ Bond price (current)

Because ppl postpone to buy in future as they'll get ↑ Interest rate & hence the current bond price reduces as most are not buying it now (↓ Demand; ↓ Price)

GOVERNMENT SECURITIES / BONDS

→ These are the bonds that are issued by the govt (centre/state) to acknowledge the borrowings from the financial sector (Banks).

→ They are also tradeable like other bonds

BONDS

- CORPORATE
  - Comparison to shares these are safe but not than Govt.
  - Regulated by SEBI
- GOVERNMENT
  - Safest Investment Instrument bcos:
    1. Bond - Fixed
    2. Promised by GOVT

→ **Gilt-Edged Securities** — Govt Bonds

↑ Best quality; directly/indirectly refers to Govt. bonds.

→ Govt. Securities Market is under the Regulation of RBI.

RBI goes for arranging PRIMARY AUCTION of Govt. Securities

▷ It generally means: Any tradeable instrument sold 1st time.

RBI also invites PRIMARY DEALERS who participate in auction.

✓ Financial Institutions ✓ Commercial Banks (Most) ✓ Foreign Investors

▷ There are lot other primary dealers on RBI website. They can apply to (buy bond) participate in auction & RBI will decide.

⇒ Classification of Govt. Bonds:

I. Treasury Bills (TBs) → Short term; Maturity < 1 years

II. Dated Govt. Securities → Long term; Maturity > 1 year.

Financial Market

MONEY MARKET

Short term loan markets

Ex: Treasury bills (TBs)

CAPITAL MARKET

Long term bonds / any other such instruments

\+ Share Market

Ex: Dated govt. securities.

Classification of Money Market (Maturity < 1 yr)

I. OVERNIGHT MONEY MARKET — Maturity of 1 Day

Banks experience sudden fluctuations of liquidity & may go for this type.

II. NOTICE MONEY MARKET — Maturity of 2-14 Days

III. TERM MONEY MARKET — Maturity of 15-365 days

INSTRUMENTS OF MONEY MARKET

① Treasury Bills (TBs)

② Call Money Market → Inter-Bank loans (or) call loans (or) call Borrowings

× Non-tradeable

✓ Its interest rate is called Call money rate (or) Inter-Bank offer rate (IBOR)

✓ A bank with less liquidity can give to High liquidity banks.

✓ IBOR is the BEST REFLECTOR of DAY-DAY LIQUIDITY in Banking sector. It is the Barometer / Warning of crisis in banking liquidity

* LIBOR (London IBOR) – The most important IBOR in the world. It is determined by the interaction between largest global banks (of world) in London (fin) Money Market. It is the Global minimum interest rate (Benchmark)

* MIBOR (Mumbai IBOR) – The most important in India. (Refer from yellow book)

③ <u>CERTIFICATE OF DEPOSIT (CDs)</u>:

✓ Issued by banks to raise short term loans from public.

✓ Tradeable; Has market determined interest rate.

④ <u>COMMERCIAL PAPERS (CPs)</u>:

✓ Issued by corporate sector to raise short term loans from public; Tradeable; Market determined interest rate.

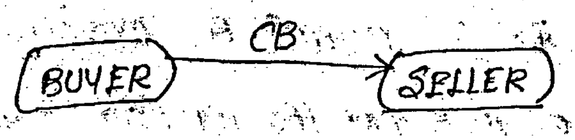
⇒ Banks are more flexible

⇒ They can issue both CDs & CPs as they are also part of corporate sector. However, CD is exclusive to them

⇒ CDs are less risky as they are under RBI regulation. CPs may or may not be regulated by RBI.

⇒ When corporate sector issues CP, there is a need, in general, listed on STOCK EXCHANGE – which is under SEBI regulation – to reduce the risk factor. Now, the listing has been made essential by RBI.

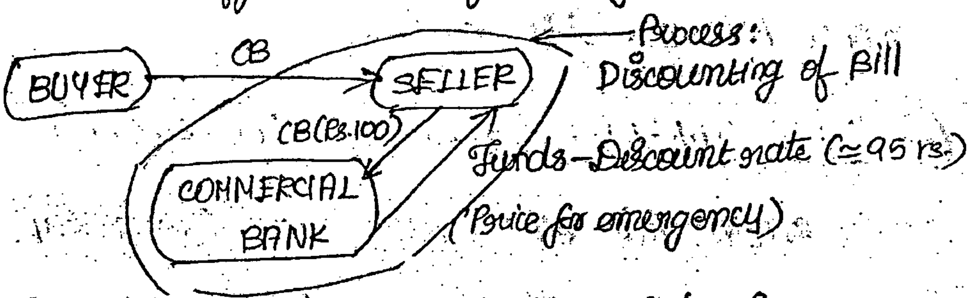
⑤ <u>COMMERCIAL BILLS</u>: Similar to Bills of Exchange. We used to have this even before Independence.



Short term loan by buyer from seller → 3 to 6 months.

The loan is repayed with interest. (1st scenario)

So far, no diff. btwn Bill of exchange & CB.

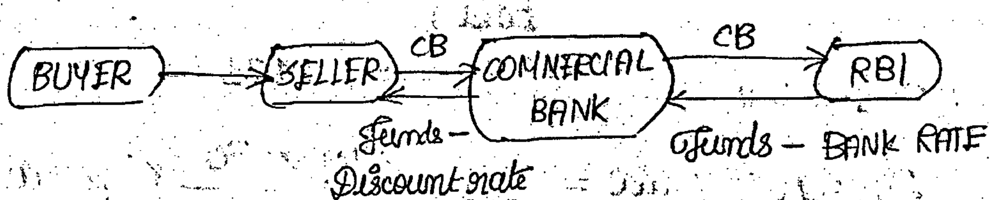


Now, it becomes a proper commercial bank.

Commercial bank offers guarantee for buyer that reduces the risk of it not repaying

Not any company can buy a CB, a commercial bank has to give guarantee.

It is Tradeable



An interest rate which RBI is charging on loans given to Commercial Banks. The rate @ which RBI is rediscounting the

In our country, the Commercial Bill market is not well developed. Hence, it is not the popular way of loans

CB is like a bond exchanged between firms guaranteed by Banks.

All instruments of money market except call money Bill are like bonds.

⑥ <u>REPO MARKET</u> : (Repurchase Agreement)

Banks take short term loan from RBI.

Banks will sell Govt. securities to RBI with a promise to repurchase it later at a <u>Higher price</u>

depends of REPO RATE.

Current value of Govt. security → Rs.100
(Including interest till 1 month)

Banks sells it for 1 Month to RBI
(with promise to rep. later @ high price).

After 1 month, G-sec Value ⟶ Rs. 101

now 0.065

$$\text{Repurchase price} = \underbrace{101}_{\text{Min. Interest rate.}} + \underbrace{\left(101 \times \underbrace{\frac{30}{365} \times \underline{\text{Repo rate}}}_{\text{1 month interest rate based on repo rate}}\right)}_{\text{Additional interest rate of RBI}}$$

* <u>Higher the repo rate, costlier the loans for banks</u>

REVERSE REPO MARKET

If any bank has to put SURPLUS MONEY with RBI, then RBI gives these banks REVERSE REPO RATE. (Now 6.25)

The banks will buy govt-securities from RBI with a promise to sell later when RBI has to buy at higher price.

The Repo & Reverse repo rates are marginal when compared to interest on public loans. RBI is liberal to banks. It is also fair to both Banks – those which need money & those which has excess money – gives & gets from both at similar rates.

BANK RATE:

It is the interest rate on which banks can take loan from RBI by Re-discounting the commercial bills.

REPO RATE:

It is short-term interest rate charged by RBI while giving loans to the banks. In Repo market, banks can sell Govt. securities to RBI with a promise to repurchase it later at a higher price calculated using REPO RATE.

REVERSE REPO RATE:

Reverse repo market is a market where banks can park their surplus fund with RBI by purchasing govt. securities from RBI & selling it later at a higher price inclusive of REVERSE REPO RATE.

CREATION OF MONEY SUPPLY

RBI never directly impacts money supply but through Commercial banks.

2 types of activities of Commercial banks

1. → Accepts Deposits from public (Pay deposit rate or Borrowing rate)
   - these are liabilities for banks
2. → Provides loans to public (charge lending rate)
   - these are assets for banks

⇒ Lending Rate > Borrowing Rate – Commercial.

DEPOSITS

DEMAND Deposits

✓ that which we can withdraw any time on demand.

Ex: Current account deposit

✓ mostly very less/no interest upon this

Ex: Demand liability of savings account deposit

✓ can withdraw

TIME Deposits

Fixed maturity deposits (short/long term)

Ex: Fixed deposit.

Ex: Time liability of Savings account deposit.

× can't withdraw

Both demand & time liabilities are subject to change as we withdraw today, next time...

NDTL (Net Demand & Time Liability) [of a particular bank] = Total Demand & Time Liability of Bank (Liabilities) − Bank's deposits with other banks (or) RBI (Assets)

CDR (Currency Deposit Ratio) [dynamic - person to person; time to time] = $\frac{\text{Money held by public as currency (CU)}}{\text{Money held by public as Deposits (DD)}}$ (Demand deposits)

(for public)

RDR (Reserve Deposit Ratio) = $\frac{\text{Total Reserves with Bank (R)}}{\text{Total Deposits with Banks (TD)}}$

(for Banks)

Reserves are that part of bank cash which will not be given as loans - Idle part of bank.

$R = \text{Vault Cash with Banks} + \underbrace{\text{Bank's deposit with RBI}}_{\text{compulsory}}$

Simplified Balance Sheet of RBI

Liabilities	Assets
i) Currency in circulation → Currency with Public → Vault cash with Banks	i) Loans to → Banks → Govt [Ways & Means Advances-WMA]
ii) Banks deposit with RBI	ii) Foreign exchange and other foreign assets (like For. bonds)
iii) Govt's deposit with RBI	iii) Gold
iv) Other deposits with RBI Financial institution, International organisation, etc. (Ex: IMF will maintain deposit with all member countries)	iv) Other assets with RBI

(In yellow book)

⇒ If RBI wants to ↑ money supply with public, it will start with ↑ Assets of RBI.

* If ASSETS INCREASE, LIABILITIES MUST INCREASE too, to maintain Balance *

High power money (H) / Monetary Base / Reserve Money (M_0):

→ It is the sum total of liabilities of RBI

→ Total liability of RBI towards everyone (public, banks, Govt, IMF etc...)

* BASE OF MONEY SUPPLY - ORIGIN OF MONEY SUPPLY.

Mechanism to Increase Money Supply (In NCERT)

1). To ↑ Money supply, RBI will buy any asset (ex: Gold) worth Rs. $\boxed{H}$.

2). RBI issues cheque worth Rs. H to seller

3). Seller will deposit cheque → Withdraw a part of H — Ex: H/2
→ Deposit a part of H — H/2

↳ This will be determined by CDR (currency deposit Ratio)

↳ If CDR = $\frac{1}{1}$ (half of H is put as deposit & half withdrawn)

Now the increase in money supply is 'H'.

Seller deposit cheque → H/2 → withdrawn as currency
→ H/2 → Deposited with bank 'A'

4). Bank A will use Deposits (H/2) → Reserves → 0.2 (H/2)
→ Give loan → 0.8 (H/2)

Based on RDR = (ex:) 0.2

5). Loan given to:
- → Firm → Ex: If given as wages, entire money to workers
- (or)
- → Household

6). Workers get 0.8 (H/2) → Deposited with Bank 'B' → Reserve
→ Loans

- This process continues as long as HH have Bank accounts — Chain starting with RBI buying asset - gradually the money supply generated is more than asset value

$$\text{Total Money Supply} = H + \underbrace{0.8\left(\frac{H}{2}\right) + \left(\frac{0.8}{2}\right)^2 H + \ldots\ldots \infty}_{+Ve!!}$$

$H \rightarrow H/2$ (Currency), $H/2$ (DD)

As long as it is +ve, $\boxed{\text{Total money supply} > H}$

— Hence it is called (H) → MONETARY BASE —

$$\text{Money Multiplier} = \frac{\text{Money Supply}}{H}$$

✓ Always > 1

✓ If MM is 2, then the money supply gets doubled (2H). as RBI buys asset worth H.

Assumption: that people will not come to bank to take out deposit at the same time.

- Banks give loans twice than their deposits.
- Ex: with 100 Rs. they give 200 Rs. loan.

Today's class need to read more on

NCERT + Yell. book

MONETARY AGGREGATES:

Different measures of money supply associated with Banking sector.

1. NM_0 [New Monetary aggregate ≃ Reserve money]

NM_0 = Currency in circulation + Banks' deposits with RBI + Other deposits with RBI

[No. Gov. deposits here]

2. NM_1

NM_1 = Currency with Public + Demand Deposits in Banking system + other deposits with RBI

Currency with Public doesn't include Vault cash in Bank. Hence it is diff. from currency in circulation.

3. NM_2

- $NM_2 = NM_1$ + short term time deposits of residents

4. NM_3 [Broad Money]

$NM_3 = NM_2$ + Long term time deposits of residents + Call/Term borrowings from Financial sector (whatever short term loans banks can raise)

Patterns in above:

① $NM_0 \longrightarrow NM_3$ —— ↑ in coverage of Money Supply.

② $NM_0 \longrightarrow NM_3$ —— ↓ in liquidity

→ Most widely used money supply is ⇒ NM_3 (Broad money)

→ Common way of Money multiplier = $\frac{NM_3}{H}$

→ Govt. deposits not included in NM_0, NM_1, NM_2, NM_3.

MONEY SUPPLY:

(Associated with Banks + Post offices + NBFCs) — Read from yellow book

↓

Broader Liquidity Aggregates [L_1, L_2, L_3]

NBFCs [NON-BANKING FINANCIAL COMPANIES / INSTns]

* Why they are like bank?

1). They provide Loans $\xrightarrow{\text{But only}}$ Specific loans.

- Asset Finance Companies
  ↳ Automobiles, Tractors, etc. (gen. capital goods, rarely for consumer durables too)
- Infrastructure Finance Companies
- Micro-Finance Institutions
  ↳ Imp. in poverty alleviation, agriculture — SHGs.
- Gold Loan Companies
- Some NBFCs — Buy Shares / Bonds issued by Govt/companies

* How are they different from Banks?

2). > NBFCs can't accept Demand Deposits

> They are not a part of Payments & Settlement systems (Cheque, DD issue)

> No deposit Insurance Facility

× Compared to banks, it is little riskier to deposit in NBFCs.

× But ppl are attracted bcos of higher interest rates — though RBI regulates it now.

3). NBFC's can't accept deposits < 1 yr $\xrightarrow{\text{But}}$ 1 yr to 5 years.

FUNCTIONS OF RBI

① Monetary Policy Regulator

② Regulator of Banking system & NBFCs → There are some unregulated NBFCs but RBI won't take responsibility for it.

③ Regulator of
- → Money Market
- → Forex Market
- → Govt Securities Market → SEBI – regulates securities other than Govt's sec.

④ Banker to the Banks
- Loans to Banks
- Deposits from Banks.

⑤ Banker to Government — SG + UG.

⑥ Regulates Payments & settlements system → Including payments of net banking, cheques etc... All modes of payment.

⑦ Plays Development Role in Economy.

⑧. Research & Statistics → RBI – Database on Indian Economy

1. MONETARY POLICY REGULATOR:

Regulation of Money Supply & Credit.

Objectives
- 1). Price Stability [Keep Inflation under Control]
- 2). Adequate Credit Supply to Productive Eco. Sectors.
  - ↳ Linked to GDP Growth – Development role.

Twin objectives are contradictory and tests the art of RBI in regulating Price stability w/o affecting GDP growth
Balance — Optimum credit supply & Inflation control —

INSTRUMENTS OF MONETARY POLICY

I. Quantitative Insts. of. MP:

1]. CRR (Cash Reserve Ratio)

Reserves of a Bank
- → Required Reserves – cash Balances which Banks are reqd. statutorily to keep with RBI; No interest on this
- → Excess reserves – Voluntary reserves with Banks and not with RBI

$$CRR = \frac{\text{Reqd. Reserves}}{NDTL} \times 100$$

$\boxed{\text{At present CRR} = 4\%}$

Higher CRR ⟶ Higher RDR ⟶ Less capacity with Banks to give loans to public
↓
LOWER MONEY SUPPLY

Higher CRR ⟹ CONTRACTIONARY MONETARY POLICY

Similarly: Lower CRR ⟹ EXPANSIONARY MP

Note: If RBI needs to affect Money supply within few days (2-3 days), then only they will touch CRR.

2] SLR (Statutory Liquidity Ratio)

Proportion of NDTL that Banks are required to keep Statutorily in the form of some specified Liquid Assets.

- Govt. Securities – Major part
- Excess Reserves [Vault cash/cash in hand]
- Current account deposits with other Banks
- Gold

— Not as strict as CRR – but Liberal choice with Banks

— SLR is over & above CRR.

Higher SLR ⟶ Higher RDR ⟶ Less loan to Public ⟶ Lower Money supply

Higher SLR ⟶ CONTRACTIONARY MP

Higher SLR ⟶ More loans to Govt. (Govt. Securities) ⟶ Welfare Expenditure ⟶ Increase in MS (though not equal to the lowered MS)

→ Hence, CRR is a more effective/sharp MP as it is strict & no choice to banks.

→ But, Govt is happy with SLR as they get

→ Minimum guaranteed loans

SLR is gradually declining

At present SLR = 19.5%
19% of it – Govt-Sec.

Note: Banks may also keep more Govt. securities than required. For ex. 25% of NDTL can be Govt-Sec. – Esp. during Finan. Crisis

3]. Bank Rate

4]. Repo Rate

At present

BR	6.75%
RR	6.5%

↑ BR or ↑ RR → More excess reserves with Bank [To meet short-term liquidity requirements. If ↓ BR/RR, I can take loan from RBI anytime but when loans are costly, I keep more cash.]

↓

Lower Money supply ← less loans to Public ← Higher RDR

Still, this is not as effectives as CRR as this has freedom as banks can't be forced to take up less/more loans — it will only discourage banks to take loan.

Even then RBI changes only BR/RR or SLR frequently as it deliberately wants to give freedom to banks. RBI will use CRR only as a last resort in crucial situation.

Between Bank Rate & RR, why RBI changes RR only often?

Bcos — Reverse Repo market:

Surplus fund with Bank → Buy Govt-Sec. from RBI in Rev. Repo Mkt → Same Govt. Sec. can be used to take loan under Repo Market

Banks don't need extra Govt. sec to take loans from Repo market ⟸ How is this Beneficial?

In case of BR, Banks would need extra Commercial Bills which would reduce their loan giving capability to public.

RBI gives dual window to Banks in case of RR — which enables Govt. sec to be circulated btwn Banks & RBI.

L.A.F (Liquidity Adjustment Facility)

→ Combined operation of Repo rate + Reverse Repo rate

MSF (Marginal Standing Facility)

MSF Interest Rate = 6.75%

Similarity: Banks can take loans from RBI

Difference: MSF – Overnight loans taken by Banks from RBI
- Higher interest rate as it is emergency loan
- Banks are allowed to use SLR Govt-Sec. as well to get MSF Loans – Happy for Banks as otherwise they would need extra Sec.

SLR: Good return + Safest Investment + Facility to take MSF loan

Note – In LAF, banks can buy security from Reverse Repo market.
- LAF also acts as a Balance – as Banks can purchase G-sec. during excess money & also take loans with same securities during scarce money.

5]. OPEN MARKET OPERATIONS (OMO):-

i) RBI buys Govt Securities from Banks
↓
Increases Liquidity with Banks
↓
More capacity to give loans
↓
High MS → $\boxed{\text{EXPANSIONARY MP}}$

ii) RBI Sells Govt-Securities to Banks
↓
Reduced Liquidity with Banks
↓
Less capacity to give loans
↓
Less MS → $\boxed{\text{CONTRACTIONARY MP}}$

During DEVALUATION → RBI Sells Govt Securities to Banks
+ INFLATION CONTROL
Open Market Operation (ii)

Quantitative Easing (QE):

→ Most Famous in: Developed Countries - esp. US, JAPAN.

* In this, the central bank purchases large no. of long term securities (Govt-Sec + other sec) from Banks & Public.

→ It is a large scale operation — Massive increase in Money supply — Larger Scale than (i) OMO.

? Why not in India? - It will be Suicide for India - ↑ Inflation already

× We don't need QE as MPs are enough.

✓ But, devt countries need QE as they find it difficult to increase money supply using conventional MPs.

? Why Conventional MP Instruments not useful in Developed Countries?

Because their Interest Rates are very low; Ex: 0.5% in Japan
(Can't affect much for further reduction) → Liquidity Trap
→ No expectation of Further fall

After 2008: US went for QE which also included printing of more dollars; Also JAPAN did it - Helicopter Money

⇓

Some of these $ came to India too as Foreign Investment

But then QE reduction happened (Tapered Tantrum)

↑

(due to ↑ Inflation beyond a point) Affected Foreign Investment in India

II. Qualitative Instruments of MP :

1]. Margin Requirements on Loans

Minimum proportion of loan that borrower has to arrange itself

Ex: 100% - Loan requirement (say, for Automobile)

40% - Own ; 60% - Bank will give as loan.

✓ RBI can differentiate among borrowers in this type — By ↑ Marg. Req. on Loans

Through this RBI can discourage credit for certain type of borrowers (ex: Luxury cars or Not so productive Credits).

2]. Differential Interest Rates on Loans

Lower Interest rates on Agriculture Loans (Interest Subvention scheme)

PSL - Priority Sector lending.

3]. Moral Suasion

Policy directive passed to banks from RBI through Public Forum.

It is not mandatory but just a moral obligation.

It is a type of finetuning of MP when other instruments may not be effectively working.

MONETARY POLICY TRANSMISSION

Asks — Whether changes in MP are passed on to Public by Banks/not.

✓ Contractionary policies are transmitted very well - no problem here.

× Expansionary MP are however not so well transmitted.

⇓

Challenge of MP Transmission

Some methods to ensure transmission are:

BPLR (Benchmark Prime Lending Rate)

Introduced in 2003 by RBI.

Lowest Interest rates at which banks can give loans to Borrowers (i.e) Below which Interest can't be reduced.

Why this BPLR? Banks tend to give Loans @ very ↓ Interest to favoured borrowers & @ high rate to other public - To regulate this.

BPLR is decided by Banks (not RBI) on the basis of Cost of Funds.

↑

Not specified; left as subjective category - hence banks misused this - Banks unnecessarily altered BPLR.

Base Rate

Introduced in 2010. by RBI

Minimum interest rate at which banks give loans to preferred Borrowers.

It is Determined by Banks → on basis of Cost of Funds, which have maturity upto 1 yr, to banks

Around 2015-16, despite ↓ in repo rate by RBI, Banks didn't decrease the Base rate as repo rate is not considered but only cost of funds.

So RBI brought new concept.

MCLR (Marginal Cost of Funds based Lending Rate)

Marginal cost of Funds ⇒ include very short term change in cost of funds (i.e) changes in Repo Rate.

By this way, RBI has made it mandatory to change MCLR in case of change in Repo Rate.

↓ Repo rate ⟶ ↓ MCLR ⟶ ↓ Avg. interest rates ⟶ Better monetary policy transmission.

It has made repo rate an important factor in Monetary policy.

Recently RBI is eyeing to align Base rate & MCLR to reduce discrepencies in interest rates.

INDIAN BANKING SECTOR

History:

Yellow Book on Money & Banking.

I. 1969 to 1991:

Before 1969, Banks used to be controlled by Big Industrial houses & banks were catering to them only & not common public (unpreviledged section)

So 1969 – NATIONALISATION OF BANKS – 14 banks

By 1980 – 14+6 – 20 Banks Nationalised.

Nationalisation ⇒ Govt. taking over control to ensure social responsibility.

Post 1969: Problems for Banks

i) LEAD BANK SCHEME [Only till 1991] → BRANCH EXPANSION

Every nationalised bank should act as lead bank in that particular district — To take responsibility for developmental activities.

So there was more Branch Expansion of Banks.

problem: Branch expansion → ↑ cost of Banks → profitability impacted

ii) Priority Sector lending [PSL]

Atleast 40% of total loans/credits must go to priority sector.

priority sector ⇒ Agriculture, small businesses, rural Indus, etc

18% of total credit reserved for Agriculture.

PSL was of lower Interest Rate

problems: PSL led to ▷ lower profit for Banks;

↓ ▷ Higher NPA in PSL (High default in loans)

why? More problem with banks as they didn't know to manage PSL as they had lack of experience (It was not only becos of farmers not paying back)

Post 1991:

PSL – Existed before 1969 & even after 1991

→ Even now there are lot of similarities – 40%, 18%..

→ Difference is: PSL has expanded to

✓ Education ✓ Housing ✓ Exports in addition to Agri + Small Bus

→ Atleast 8% to small & Marginal farmers.

In PSL context, Private sector & public sector both have to obey.

For Foreign Banks – 32% in PSL.

– no need necessarily to Agriculture

iii) HIGHER CRR & SLR

At its peak: SLR $\rightarrow$ 38.5% of NDTL

CRR $\rightarrow$ 25% of NDTL

63.5%

It was a mess for Banks. $\rightarrow$ If 100 Rs comes, 63.5 Rs will have to be kept aside.

So, this too reduced the profit of Banks.

Why CRR & SLR high? To meet the high Fiscal deficit of Govt.
[SLR is largely govt. securities;
CRR is used by RBI to give loan to govt.]

So, there was a need for Massive Reforms.

Howv, Banks didn't have role in BOP crisis, yet reforms of 1991 benefitted banks too.

NARASIMHAN COMMITTEE, 1991

→ Most important committee on Banking in India.

→ Based on these Recommendations only 1991 reforms happened.

→ However, few of recommendations were not implemented
- ↳ Abolition of Priority Sector lending / limit it only to poor farmers. ⇒ But PSL continued & even expanded
- ↳ Restructuring of Banks – possibility of mergers & acquisitions in Banking sector + Specialised Banks for different types of functions.
  - ✓ 2/3 banks big enough to compete Internationally
  - ✓ some National banks
  - ✓ some specialised only in Deposits [Recently, we now have Payment Banks]

Some most important accepted Recommendations / Reforms:

i] On Directed Investment → lower SLR & CRR.

By 1997, SLR → came down to 25%. (from 38.5%)
By 2001, CRR → came down to 5%. (from 25%)

This gave more space & freedom to banks to give profitable loans.

This is a type of LIBERALISATION reform.

ii] Interest Rate Deregulation → shld be Market determined.

[Before 1991, it was controlled by Govt]

Banks can now look at demand & supply of loans & take decision based on Market.

This is a type of LIBERALISATION reform.

Main market det. Interest rates were for < Loans / Long-term deposits

In recent times, < Short-term Deposits / Savings deposits } came under market det. Interest rate

iii] Private Sector Banks were allowed in India

It is a type of PRIVATISATION reform

It doesn't mean public sector getting privatised but just giving space for other players in economy.

1ST PRIVATE BANK in 1994 ⇒ ICICI - now 2nd largest in India.

Ex: HDFC, AXIS

IV] Foreign Banks were also allowed in India

It is a type of GLOBALISATION measure/reform

Ex: HSBC, ⇒ It can be called FDI in Banking

They still have scope of development though.

V] Banks allowed to raise funds from International Capital Market.

It is a type of GLOBALISATION reform.

Banks from share market } @ International economy.
Bond market }

VI] Capital Adequacy Reforms

To handle risks better.

Called as BASEL I Norms [International norms in same matter reforms]

VII] Solving NPA problem in Banks.

CAPITAL ADEQUACY

- Simplified Balance sheet of Bank

LIABILITIES	ASSETS
1. Capital	1. Deposits with RBI
2. Reserves (excess)	2. Deposits with other Banks.
3. <u>Deposits</u>	3. <u>Loans & Advances</u>.
4. Borrowing by Banks	4. Investments (Govt. security, foreign Govt. securities, shares of companies etc.)
5. Other liabilities	5. Fixed Assets (Land, Building, etc.)
	6. Other Assets..

CAPITAL

- Money from selling shares
  Debentures, Bonds, etc.

Why Capital & Reserves under liabilities?

Actively they are not earning profits / regular returns

They are yet kept → To handle risks.

Opportunity cost — the more capital & reserves left, less capacity to give loans. But they are req. in adequate amount to handle risks.

Capital & Reserves classified into [Based on quality].

i) Tier I / Core Capital

ii) Tier II / Supplementary Capital

Quality: Readily available to Bank.

TIER I / core capital

→ The best quality capital

→ Within this, Common Equity Capital / Share capital is the best quality.

↳ Shares sold to public. Hence, money readily available

→ DISCLOSED RESERVES also belong to Tier I.

Ex: cash - readily available in Bank.

TIER II / Supplementary Capital

→ REVALUATION RESERVES - The value / extra reserve the bank can get if the assets (Land, Building, etc.) are revalued at today's price in market

→ It is good but not readily available like Tier I.

Capital Adequacy Reforms

BASEL I Norms, 1988

* BASEL → In Switzerland - a city.
→ HQ of BIS [Bureau of International settlement]

✓ Meeting of Central Banks (for financial stability of Global economy)

✓ Earlier they were very famous for talking of capital adequacy.

→ Minimum Capital Requirements for handling Credit risk.

Credit risk ⇒ Is possibility of loss if loans are defaulted

BASEL II Norms, 2004

i] Minimal Capital Requirements

3 Risks:

a) CREDIT RISK

b) MARKET RISK

possibility of loss due to change in market value of Assets and liabilities.

Ex:1 Recently, lower market interest rates in India is a market risk ⇒ FPI in bonds moving out → ↓ Bond prices → ↓ Bank profits

Ex:2 Rupee depreciation

It makes Repayment costlier in international economy

[Deposit by NRI @ 1$ = 60 Rs ; Maturity-interest @ 1$ = 70 Rs]

c) OPERATIONAL RISK

possibility of loss due to faulty system, people & External factors.

Ex: possibility of fraud in case of unsafe internet Banking.

RWA [Risk Weighted Assets]

→ Loans adjusted for the 3 RISKS.

✓ Not every loan is risky

▸ Govt. loans are risk-free; Household, corporate loans are riskier.

Loans
Rs.100 Cr

- 30 Cr (Govt) → 0% risk
- 50 Cr (Companies) → × 20% (anticipated risk)
- 20 Cr (Households) → × 30% hypothetical however

RWAs will always be less than their assets/Loans as risks pull them down.

CAR or CRAR [Capital to Risk weighted Asset Ratio]

$$\text{CAR/CRAR} = \frac{(\text{Tier I} + \text{Tier II})\ \text{capital}}{\text{RWA (Risk weighted Asset)}}$$

It tells, how much good quality capital the bank has to avoid risk associated with assets/loans.

Generally, higher CAR is preferable.
But, if it is very high, it will impact profitability of Banks. How?

Under BASEL Norms ⟹ CRAR must be atleast 8%
RBI ⟹ keeps it at 9% [9% (Tier I + Tier II) of RWA].

Most times, Indian banks have followed it.
However, we have scope & potential to increase it.

ii] SUPERVISORY REVIEW

Banks should have adequate Risk-management system which is to be regularly supervised by country's central Bank.
Now, Risk management department is imp. part of Banking.

iii] MARKET DISCIPLINE

Transparency norms (i.e) Disclosure requirement of Balance sheet of Banks to public.

The detailed Balance sheets are even published by banks from time to time.

BASEL III Norms, 2010

- Similarity with BASEL II,
  - (i), (ii) & (iii) with slight changes.
- Max. difference is with:
  - Min. Capital Requirements

→ It came immediately after 2008 crisis. The norms have become more strict.

2008 → Sub-prime Crisis in US

↳ It was clearly a banking crisis

The banks in US had given lot of <u>sub-prime loans</u>

↑ loans given to less credit worthy / Risky borrowers.

& these loans were defaulted in a huge way leading to Banking crisis → National crisis → International crisis

↳ It basically started with Banks of most developed countries.

9.6

i] STRICTER MIN. CAPITAL REQUIREMENTS :

⇒ Common Equity Tier I Capital → Atleast 4.5% of RWA out [Earlier only 2%] of total 8% CAR.

Why this? Before 2008, more capital was in Tier II & was not readily available.

⇒ However, official CAR was kept same @ 8%.

— No compromise on stability of Banks clear cut —

ii] CAPITAL CONSERVATION BUFFER [CCB]

CCB
- [Banks own resources] ∘ dividend payments
- ∘ Bonuses.

Its quality is same as TIER I.

It must be atleast 2.5% of RWA.

So, unofficially CAR = 8% + 2.5% = 10.5%

— Hence capital assets increased —

iii] COUNTER CYCLICAL CAPITAL BUFFER.

If economy is in upswing (good times) → Banks must Create Buffer

when in Downswing (bad time) → Banks can Consume Buffer

This is country specific.

If it had been there before 2005, we wouldn't have had NPA crisis now.

During 2005–2008: Good time in Indian economy & Banks gave more & more riskier loans

IV] LEVERAGE RATIO

$$LR = \frac{\text{TIER I Capital}}{\text{Total Assets (Loan)}}$$

It will complement CAR to look into capital adequacy.

Min LR = 3%

LR always less than CAR.

V] LIQUIDITY RISK

4th risk in addition to ①, ② & ③ risks.

Banks face diff. liquidities from time to time. Low liquidity is loss to banks. So need:

$$\text{Liquidity coverage Ratio [LCR]} = \frac{\text{Stock of High quality Liquid Assets}}{\text{Total Net cash Outflow in 30 days (approx. Expected)}}$$

High quality Liquid assets
- cash over & above CRR
- Govt. securities over & above SLR
- Foreign govt. securities

Ideally, it must be LCR = 100%.

But it is difficult in reality.

INDIAN SCENARIO

India must start following Basel III from 2019.
Is India prepared?

YES ⇒ CAR, LR are OK

NO ⇒ LCR is difficult; CCB is also difficult
so, now RBI has told atleast to have it 60%.

Our NPA is increasing, quality of assets ↓ - Poor loans.
But req. of having more CAR, Tier-I Eq. capital, in this scenario is difficult.

BASEL-III Norms

Changes compared to BASEL-II

i] More strict requirements related to the Common Equity TIER-I capital, which means Banks have to keep more of Best quality capital to handle risks related to the loans.

ii] In addition to 8% of CAR, banks need to maintain CCB created from their own resources like:
- By limiting payed out dividends
- Employee Bonus payments etc..

It should be atleast 2.5% of RWA

iii] There should be a CCCB [Counter Cyclical Capital Buffer] optional for the country where the banks should create additional Buffer during economic upswing & consume buffer during economic downswing

iv) LEVERAGE RATIO

A min. percent of total assets (3%) must be maintained as TIER-I capital.

v) LIQUIDITY MANAGEMENT

Basel III identifies liquidity risk as possibility of loss due to lack of cash with bank to meet the needs of depositors and borrowers.

For this, a 100% LCR should be maintained.

LCR requires bank to maintain enough high quality liquid assets to deal with the cash outflows over the next 30 days.

NPA (NON-PERFORMING ASSETS)

— Loans where Interest payments are 90 Days past Due. —

✓ It is the 1st step to becoming default.

✓ If it is not Non-performing, it is called Standard Assets

Interest and principal amounts being repaid ↵

→ Once loan is in NPA ~~is on~~ for 12 months, Sub-standard Assets

→ If loan is in sub-standard for 12 mnts, Doubtful Assets

→ If Doubtfull too persists, then Loss Assets [2 yrs of NPA]

↳ Very low probability of recovering.

→ when banks accept it couldn't recover, Write-off loans.

Generally, public sector banks are prone to declare easily Write-off loans as govt. only is going to pay (i.e) we, taxpayers. Private sector is more cautious & will try its best to recover the loan.

NPA

Lack of Ability to Repay

(i.e) Failed purpose of loan.
For recent NPA crisis, this reason is citied largely.
Most loans were given during 2005-2008
Good time of Indian economy made Banks & ppl reckless.
Then, 2008 slowed down the economy & hence inability.

Lack of Willingness

(i.e) Ability is there but they don't repay due to slow legal process.

Solutions for NPA Problem

Provisioning for NPAs

Accounting for estimated loss from NPAs.

Provisioning $\Rightarrow$ ↑ in liabilities $\Rightarrow$ ↓ in profits

conceptually, $\underbrace{\text{provisioning}}_{\text{done only by banks with NPA.}} \approx \underbrace{\text{capital adequacy}}_{\text{must be done by every bank irrespective of NPA = min. CRR.}}$

But diff is,

Post 1991

NARASIMHAN COMMITTEE Sol (1) Legal Reforms)

Most NPAs is due to lack of willingness

why? Weak legal mechanism.

SOLN a) Debt Recovery Tribunals

↓

To bring down the time of Judicial process.

b) SARFAESI ACT, 2002

[Securitisation & Reconstruction of Financial assets & Enforcement of Security Interest]

↳ Banks were empowered to take control over the security (collateral) of the loan w/o involving Courts. (Earlier court was involved) with a 60 days prior notice.

Sol ② a) Asset Reconstruction Companies (ARCs) :-

→ Type of NBFCs ; Privately owned

→ Buy NPA from banks at a discount (lower price)

Options of ARCs

- Recover NPAs (Get all claims on security)
- Control over the management of defaulting company.
  ↳ Through this they can again try to recover the NPAs
- Convert the NPAs into Financial securities & sell it to investors. ≃ mutual fund units (pool savings & convert into securities)
  ↳ But this has not worked very well as it is a high risk security as its base is bad loan.

Even overall ARC concept has not worked well in India

If banks sell NPAs ⟹ It improves their Balance sheet (as they don't need provisioning)
⇓
Also, Banks then can give more loans

Logically, ARC is a good solution. But;

Limitations of ARC :-

⇒ Conflict btwn Banks & ARCs on discounted price of NPA.
  ↳ Banks complained to RBI of exploitation by ARCs.
  ↳ So RBI ⟶ more transparent pricing. But, yet
  ↳ less & less (bad loans) NPAs are purchased by ARCs.

⇒ ARCs may not manage defaulting companies.
  ↳ Bcos companies may be of variety of sectors.

Sol ⓐ b) Bad Banks (BB):

≈ to ARCs. But,

Difference is ⇒ Bad banks will be funded & controlled by the govt. & not private companies

⇓

So, they will try to solve NPA problem of PSBs. (PSB NPA > Private NPA)

Why BB may not work?

→ ARC has not been successful.

→ Govt. doesn't have enough experience in recovery of NPAs. So it will be worse than ARCs.

[Due to lot of criticisms, BB has not come up yet.

⇒ BB may be successful if there is lack of willingness problem & not capability problem.

Company won't pay, so no Atleast save Banks ← loss for them

→ But in India, mostly it is lack of Ability problem.

How? Most NPAs in India → loans given during 2005-2008, when Indian economy was at one of its best →

Higher economic growth → Over optimism → Banks, Borrowing companies → Reckless lending

Post 2008: Slowdown

↓

Lack of ability to repay (Borrowing companies didn't gain profit as expected)

Solution to NPAs will be successful only if we are able to tell which problem is significant

Lack of Willingness	Lack of Ability
Here, priority is:	Here, priority is to be:
* Saving the banks.	* To make company more able to become able to pay back.

Why NPA is a serious problem?

Not only because of defaulting loans but also that it hurts the future loan giving capacity of Banks.

TWIN BALANCE SHEET PROBLEM

1] It is the poor Balance sheet of borrower/ borr. companies
[losses primarily due to slowdown → ↓ Demand]
↓
[Increasing the NPAs]

2] And poor balance sheet of Banks due to NPAs.

So, increase/ improve the Balance sheet of borrower so that they are better able to pay back
↓
In turn, this will improve balance sheet of Bank, likely.

Sol 3 : ~~Reconstruction~~ Restructuring of Loans

Concession on Loan repayments to borrowing companies.

- ↳ Longer repayment period
- ↳ Lower Interest rate

How Borr. companies will benefit? This will likely improve their balance sheet / ability of bank.

$\boxed{\text{STRESSED ASSETS} = \text{NPAs} + \text{Restructured Loans}}$

How Banks will benefit? Banks don't need provisioning of restructured loans for some time. So their Balance sheet improves.

~~why name~~ stressed assets?

Restructured loans are technically, though not NPAs but, still defaulted ones. There is only a hope that it may be repaid

TYPES OF RESTRUCTURING OF LOANS

① CDR (Corporate Debt Restructuring):

Simplest. Either via ↑ repayment period or ↓ Interest rate.

② SDR (Strategic Debt Restructuring)

③ S4A (Scheme for Sustainable Structuring of Stressed Assets)

Similarity of ② & ③

NPAs Converted into
- → Debt — Concessions given to borrowers (≃ CDR)
- → Equity — Group of banks get significant share holding in borrowing company

Some Management control ⟶ likely to recover NPAs.

Difference btwn ② & ③:

↳ Started with SDR ⟶ 51% shareholding is like a punishment to borrower under cover of helping them.

↳ This was criticised, so came S4A ⟶ < 51% shareholding only.

Major Limitations of Restructuring of Loans:

⇒ May be misused by Banks to hide their NPAs.
- ↳ Hiding is just postponing & doesn't solve the problem.
- ↳ R. Rajan felt the need for genuine restructuring.
- ↳ NPAs shouldn't be covered for sometime but need a sustainable solution.

⇒ May be misused by Borrowing companies.
- ↳ May pose as having lack of ability even when they are willing defaulters.

⇒ Group of Banks may not be able to manage the company.

Sol:4 IBC [Insolvency & Bankruptcy Code]

Note: It is a broader reform. Here we look at it as a reform only w.r.t. NPA problem.

1st Gen Reforms:

✓ LPG → was about : Liberal Entry of Firms.

X Not taken care of : Liberal exit of Firms, as all companies won't be successful/Efficient

2nd Gen Reforms:

✓ Exit of Inefficient Firms

IBC is primarily about this.

Economically same, Diff is legal:

- Insolvency → Company broken down/disaggregated. Beginning — Liquidation starts — ongoing process.
- Bankruptcy → Final stamp of court approving or declaring the Insolvency.

How is it a solution for NPA problem?

2016 → Parliament legislated it.

2017 → Implementation.

JUNE, 2017 ⇒ RBI instruction — Banks should go for having a Resolution plan for 12 largest (non-perf-Assets) NPAs (i.e) 12 companies

Why these 12? These 12 account for 25% of total NPAs.

Resolution Plan (RP)

Whenever a company is having ↑ NPA a/c

⇓

It can be referred to NCLT (National Company Law Tribunal)

⇓

Banks + NCLT will have to come up with RP.

↳ Insolvency professionals → Try to retain the asset value of the company

(i.e) return the remaining +ves of company ≃ Marketing

Try to sell the company to other company in <u>same sector</u>.

✓ Employees won't loose job, only owner will change

✓ Assets of company retained; <u>Banks also get a part of loan</u> which the <u>new owner has to pay</u>. as soln. to NPA
(Amount is determined by bidding)

June, 2017 ⇒ RBI time period : 9 months for RP

If RP fails → then company will be liquidated
[declared Insolvent → Bankrupt]

But, this is not preferred as liquidation is a pain for employees & also for overall economy as it sends wrong signals about economic performance.

Successful RP :

TATA steel acquiring 72.65% shares of BHUSHAN steel.

& settling the loans of Bhushan steel with 37% Haircut.

Haircut → that part of loan not repaid.

→ Only successful RP in Indian Economy

But, No other company has come forward after this.

Limitations of IBC (in terms of soln. to NPA)

⇒ Some sectors are more lucrative [(i.e) steel] to Buyers compared to others. [(i.e) Infrastructure]

Why so? Infra. → Long term, more investment..

⇒ Banks fear higher Haircuts in future.

⇒ stricter rules from RBI.

↳ limitation from overall resolution process & not IBC perse

→ FEB, 2018: RBI → all restructuring schemes are abolished.

→ For NPAs > Rs. 2,000 crores, Banks must bring RP within 180 days (from March, 1) else be ready for HIGHER PROVISIONING

- 50% of loans
- 100% of loans [Liquidation cases]

Likely to reduce Bank's profits. Very rigid - 180 days.

Why RBI did this?

→ RBI wanted to arrest the loopholes of restructuring cover.

→ RBI also felt, unless in case of emergency, Banks won't act. Hence this was to speedup the restructuring process.

→ RBI wanted to ~~set~~ implement IBC & not just sit & watch.

What has happened to all this now, after 180 days deadline?

Nothing much. But Govt. has come inbetween.

SUNIL MEHTA COMMITTEE

Recommendations of it were accepted by Govt for a:

PROJECT SASHAKT

i) For NPAs > Rs. 500 Cr, ARCs/AMCs will be setup to resolve NPAs before taking NPAs to NCLT.

ii) For NPAs = Rs. 50 to 500 Cr, Bank-led Approach.
(i.e) Lead Bank will bring RP within 6 months

iii) For NPAs < Rs 50 Cr, Individual Bank can resolve it within 3 months.

→ With Project Sashakt, an extra layer has come up between Banks & NCLT — ARC/AMC. But neither the committee / Govt has given any blueprint for ARC/AMC.

→ Critics say ARC inbtwn is DILUTING THE IBC. (Govt. does this for helping PSBs)

Reforms In PSBs [Public Sector Banks]

— P.J. Nayak Committee, 2014 —

Why only for PSBs? More NPAs here.

Indradhanush Reforms

1. **Appointments**: Separation of Top positions of Chairperson & MD/CEO. → It is implemented now.
   ≃ political person   ≃ Banking professional.

2. **Set up BBB** [Banks Board Bureau] ⇒ for top appointments
   Earlier Fin. Ministry will directly appoint them.
   BBB → must have all members from Banking sector & no govt. representative.
   But actual BBB in working → chairperson + 6 Members
   dilutes the intended BBB.   Senior bureaucrats   3 officials → Bureaucrats   3 Experts → Atleast 2 from Banks

3. **Capitalization**: Govt. will ↑ Capital of PSBs by Rs. 70,000 Cr in 4 years
   (so that they don't fail in CAR norms)
   Limitation:
   → Amount not enough
   → Very Idea itself is debated. Nayak committee didnot recomend this as it is only a temporary solution.
   It told — Either Merge (or) Privatise

4] <u>DE-STRESSING</u> : Reducing NPAs of PSBs < Restructuring / RP.

5] <u>EMPOWERMENT</u> : ↓ Govt. Intervention in PSB functioning.
Generally, Govt. schemes's burden will be on PSBs.
So, it is a sensible reform but doesnot seem to be implemented.

6] <u>ACCOUNTABILITY</u> : Govt. will rank PSBs on basis of KPI (key Performance Indicators) & give Incentives for better performing banks (like, ↑ Bonus for Bank employees)
→ This is a very good reform. It will increase the:
↑COMPETITION ⟶ ↑ EFFICIENCY ⟶ ↑ PROFITS

Privatisation & Competition link
→ In economic theory, no absolute guarantee that privatisation will bring in competition. So, the debate must be to bring in competition in some way not only in private sector but also in PSBs.
Esp. In Indian scenario PSBs are very important to reach common people.
→ Also, private sector also has some problems.
→ Focus must be to ENCOURAGE COMPETITION IN PSBs.
↳ If implemented properly KPI will be Game changer.

7) GOVERNANCE REFORMS: Improve → Systems, → Processes, → Skill development

↓

DIGITAL BANKING

⇒ Indradhanush, overall, is ≃ to reducing the OPERATIONAL RISK of Basel norms.

MERGERS & ACQUISITIONS in PSB

Mergers – similar sized banks

Acquisitions – weaker bank acquired by stronger bank

Economies of Scale - Benefits:

✓ Large scale production → lower avg. cost → ↑ Productivity, ↑ Profit.

✓ +ve term.

Banking ✓ M&A means ↓ no. of. branches → ↑ in efficiency & Profit

· Similar Banks – M&A – → Balance sheet, → Work culture, → Management, → Client base

Examples:

① 1995 – PNB + NBI (New Bank of India)

> PNB was big, more profitable whereas NBI was poor.

> Hope was: Poor performance of NBI would be changed by PNB

> But, it was a failure, Backfired.

> Few yrs later, PNB profits came down.

> Why? Lesser the similarities, ↑ the chances of failure.

> Then for a decade no M&A.

② 2007-08 → SBI + 7 Associate Banks

> started then, but culminated only recently

> Not much of problems.

> No. of branches are coming down
↓
cost coming down → Overall perf. is slightly better now

> Has similar work culture + Management.

> Client base was different. But it was said SBI will get diff groups of clients from many places (earlier princely states)

> Too early to give a verdict on it, have to wait & watch.

③ Bank of Baroda + Dena Bank + Vijaya Bank

- Most experts are not for this.
- BOB & DB → Gujarat ; VB → Karnataka
- DB & VB → loss making ; Balance sheet ↓
- so, not much similarities & hopes are not high w.r.t. Benefits of economies of scale.

Challenges w.r.t. M & A:

Lesser no. of Banks / Branches

→ Good for reducing Cost. But,
Challenges in FINANCIAL INCLUSION

→ Possibility of JOB LOSS. So far just shifted but in long run, unsustainable (↑ Tech; ↓ Branches;)

Phrase generally used:

'Few Banks are Too BIG To FAIL'

When there are few banks, Govt. can't afford to loose them & they got to save it in case of crisis. So, the banks may take unduly adv. & become reckless.

So, this is BAD as we saw in Ex: 2008 Lehman Brothers

India: SBI ; ICICI ; HDFC

Few good / big Banks imp. for Govt.

For Conclusion, take a middle path

FINANCIAL INCLUSION

Def: Ensuring Access of Basic Banking services to relatively poor population or in remote areas etc.

1969 – Nationalisation of Banks was for this.

PSL (Priority Sector Lending) also a tool for this.

What is expected out of schemes for Financial Inclusion?

i) Low cost → For affordability of many people.

ii) KYC (Know Your Customer) Norms → Must be easier.

II BUSINESS CORRESPONDENT SCHEME (or) BANK MITRA SCHEME, 2005

→ Business correspondent can be

- ✓ Individuals (or)
- ✓ Institutions – SHGs, NGOs...

→ They both provide Banking services by visiting remote areas. Say Deposits or withdrawal.

- ✓ Cost effective – substituting branches
- ✓ Easier KYC norms.

So, Theoretically very good. But, limitations later

Limitations:

a) General lack of professionalism among the Business correspondents. [× skill devt × Experience]

b) Lower remuneration to business correspondents which also is reason for lack of professionalism. Even when they took commissions, it was not decent.

c) Lack of credit – More people were more in need of loan rather than deposit & withdrawal.

d) Lack of infrastructure – Electricity; Internet.

– Good scheme. But need Better implementation & workability. ✓ cost eff. ✓ simplicity –

$\boxed{2}$ PMJDY [Pradhan Mantri Jan Dhan Yojana], 2014

- To open more bank accounts,
- (as no of bank a/c is a criteria for FI in Global level)

Data: ≃ 80% of adult population now has bank a/c
≃ 55% before this scheme.

Success of scheme:

✓ INCENTIVES:

a) Zero balance a/c

b) Easier KYC norms (only 1 KYC was enough)

c) Mobile banking, Rupay debit cards - free of cost.

d) Life cover ⟶ Rs. 30,000 } w/o any premium.
Accident cover ⟶ upto Rs. 1,00,000 }

✓ Govt. pressurised PSBs to open more JD a/c.

Limitations:

a) Not cost effective for Banks.
→ Lower revenue - due to lower deposits
→ Higher Expenditure - to maintain large no. of a/c

b) Many of these a/c are Duplicate accounts

Duplicate accounts → A/c opened by a person already having an account.

> Thus, they are not for financial inclusion.
> So, in that 80%, many a/c are double-countings
> Estimate: 1/3rd may be duplicate a/cs

c) Dormant accounts

- In normal case, banks will charge for inactivity.
- But here, can't charge.
- Estimate: ≃ 40% dormant a/cs
- But now this % is going down due to DBT.

But, DBT was expected to work even better but couldn't.

d) Lack of Credit

_ Banks are not ready to give loan to zero-balance a/c

3 PAYMENT BANKS, 2015

By RBI. Started in 2015 & still in process.

On advice of NACHIKET MOR COMMITTEE under RBI.

Features:

(i) Can accept deposits upto Rs. 1 lakh + Debit cards

(ii) Can't give loans ; can't issue Credit Cards.

Why limit on deposits?

To prevent misuse of easier KYC norms (even PAN was not needed)

Cap came up after demonetisation as it was misused to deposit black money.

If no loans, then how profit?

They are coming from already est. sector

Ex: 1st payment Bank : AIRTEL PB

They must also have reach in rural areas.

Ex: PAYTM PB ; FINO PB ; INDIAN POST PB (Highest reach of all) ; ADITYA BIRLA PB.

(iii) keep atleast 75% of their NDTL in Govt. Securities ($\simeq$ SLR)

— For making money safely.

(iv) Less emphasis on opening Branches & ATMs

- Focus on Mobile banking.
- This will keep their cost lower.

(v) Beneficial to Migrant labourers – in terms of remitting money to families.

- even PMJDY didn't take this into concern as they needed atleast 1 KYC of that place.
- PB ask only e-KYC even belonging to other place.

How money will reach families?

PBs tie up with shops in small towns & villages.

Thus, shops acting as Bank branches.

Problem:

AIRTEL told KYC used for airtel sim can be used to PB also.

This led to opening of bank a/cs w/o ppl's consent/knowledge

what RBI did?

e-KYC must be verified by a 3rd party (other bank, etc)

DOUBLE EDGED SWORD (KYC)
- Easier – misused
- Tough – Difficult for inclusion.

Earlier, Airtel was given 7.25% (high), but now lower.

CHALLENGES TO FINANCIAL INCLUSION

i) Lack of Credit.

ii) Lack of Infrastructure → Electricity, → Internet

↳ even more ⊗ in case of Payment Banks.

iii) Lack of Financial Literacy.

↳ Awareness – Ex: Ppl asked 1 lakh after PMJDY ☺

↳ Capabilities – Operating easiness.

↳ If this is lagging, frauds may increase as preventions are not taken (digital operations).

TOPIC- 4

EMPLOYMENT & UNEMPLOYMENT

6-7 qns in Mains from E&U+P+A+ WTO topics.

Employment

Def: Engaged in an Economic activity
contributes to GDP.

Full Employment (Ideal)

Def: All those who are willing & able to work.

→ Get work for specified time period (as long as he is willing)
→ Get wages according to their skills

Under Employment (Real)

Lack of Full employment. (i.e) when either of the 2 conditions are not satisfied. But atleast 1st condition must be met.

Unemployment (Extreme)

Out of those who are willing to work ppl don't get work.
Due to lack of Job creation (rather than skill lag)

Assessment:

- Ideally, Govt. should move towards Full employment.
- Atleast Govt. shouldnot let rise of unemployment.
- Regular increase in unemployment is inexcusable.

TYPES OF UNEMPLOYMENT (Asked in prelims also)

① Frictional / Functional Unemployment

— Unemployment between 2 jobs —

→ Generally, it is voluntary; temporary.

→ So, relatively harmless.

→ Rather, it is good for economy.

How? A person leaves job for a Better Job

Ex: Leaving job for UPSC prep. Wages Skills Job satisfaction

↳ Generally, there will be skill development during this time leading to better wages later. This will likely increase productivity

↳ It also means Jobs are getting created. (indirect)

→ However, very high frictional unemployment is not good. Either, Employee is not good or Employer is not able to provide good jobs.

② Structural Unemployment

— Mismatch between available & required skills —

Root cause: Structural changes in economy.

Ex: Technological change (in IT, Banks,..)

> Privatisation - Pub-sector jobs ↓; Pvt-sector jobs did not rise

Few but highly skilled employees are preferred.

> Globalisation (esp. Import Dependent)

- lack of domestic production

> Change in Education structure also.

* Natural Rate of Unemployment = Frictional + Structural unemployment
  - It is unavoidable & natural
  - We can't restrict Tech growth & Fric. is voluntary

(3) Cyclical Unemployment

- Due to ECONOMIC DOWNSWING – (Be it slowdown or recession)

Earlier referred during Basal norms counter-cyclical

Why? During economic downswing:

- Firms make lower profits → Need to cut costs → Retrench / Fire some employees

Ex: Post 2008 crisis

(4) Seasonal Unemployment

- Due to seasonal nature of production –

→ Esp. in Agriculture

→ MGNREGA completely for this one type.

→ Very big problem in India

(5) Disguised Unemployment

→ Marginal productivity of workers is zero :-

(i-e) last worker's productivity

→ These workers are SURPLUS WORKERS

(i-e) even when removed, productivity is not affected

[Employment is not just working but necessarily contributing to Production]

→ Here, Formal wages are not paid.

↳ As mostly they are Family members.

$$\text{Average Remuneration} = \frac{\text{Total production value}}{\text{No. of family members}}$$

as No. of family members ↑, Production value ↓

↓ Standard of Living ← ↓ Avg. remuneration

→ Grounds for Poverty.

MEASUREMENT OF EMPLOYMENT & UNEMPLOYMENT

Labour force → Part of population which is Willing & able to work. (i.e) Those who are seeking jobs.

- They may be Employed or Unemployed. (Both)
- strictly speaking, no-age group must be put due to ~~the~~ child labour & ↑ life expectancy ; But we can say major labour force is btw ≈15 & 64 yrs of age.

INDICATORS

① LFPR

$$\text{Labour force Participation Rate} = \frac{\text{Labour force}}{\text{Total population}} \times 100$$

② WPR

$$\text{Worker population Ratio} = \frac{\text{No. of Employed person}}{\text{Total population}} \times 100$$

as WORKER → means Employed.

③ See

$$\text{Proportioned Unemployed} = \frac{\text{No. of unemployed person}}{\text{Total population}} \times 100.$$

④ UR

$$\text{Unemployment Rate} = \frac{\text{No. of. Unemployed person}}{\text{Labour force}} \times 100.$$

→ Better indicator

How to measure Labour force?

No. of. Job applications.

(i.e) A student who has never applied for a job is not part of labour force.

⇒ It is very difficult to measure in the Agriculture sector.

SURVEY – 3 Methods used by NSSO in measuring emp. & unemp.

NSSO – National Sample Survey Office : HH Survey (MoSPI) 5 yrly Survey (last) None since 2011-12.

① Usual status

Reference period : 1 year

Activity status : ≥ 30 days (employed)

② Current Weekly Status – CWS

Reference period : 7 days

Activity status : ≥ 1 hour (employed)

Why so liberal?

~~This is only sample survey & not~~ census.

These methods are more relevant for Informal sector as situation is worse than formal sector.

→ Both these surveys will only give details as of Employed or Unemployed – Binary variable – misguiding

Problem: Degree is missing [1hr also emp; 100 hrs also]

CHRONIC UNEMPLOYMENT

→ Higher unemployment rate even by usual status survey

- Chronic → Persistent; Regular phenomena
- Usual status → Decent period; Liberal days. even then if rate is ↑, very bad.

SEASONAL UNEMPLOYMENT

→ Higher unemployment rate by CWS.

CWS – Done – not in busy period — won't suspend
not in very lean period – Migrated to cities.

↓

During intermediate period.

③ Current Daily Status – CDS

Reference period: 7 days

On a particular day; if work is :

- Below 1 hr → Zero person day to employment
- 1 – 4 hrs → ½ person day to employment
- > 4 hrs → 1 person day to employment

Ex: $\underbrace{0 \quad 1 \quad 1/2 \quad 0 \quad 1/2 \quad 1 \quad 0}$

Sum it up – 3 person day to employment

⟹ It tells about DEGREE of Employment rather than just calling someone employed or unemployed.

⟹ Max. is 7. Hence 7 – 3 = 4 PDs to unemployment in this example.

* Unemployment rate will be highest in the CDS method.

OCCUPATIONAL STRUCTURE

- Distribution of employment/jobs among different Economic Sectors:

> AGRICULTURE
> INDUSTRY
> SERVICE

Note: They are similar to
- primary
- secondary
- Tertiary

But not same.

Stage: 1 - shift

When a country is growing with higher GDP for the 1st time, Jobs move from Agri ⟶ Industry, because generally higher economic growth is mainly beginning of ↑ Industrial growth.

Stage: 2 - shift

Industrial growth can't continue w/o service growth. Hence then, shift will be from Industry ⟶ Service

Ex: Marketing, Transp, Insurance, Banking, ...

There comes a point where services growth will overpower Industry, & more jobs in services.

INDIAN SCENARIO: (Unique - Exceptions)

i) No significant shift of jobs from agriculture
ii) Some jobs which did move away from agriculture: went into services, bypassing Industry. - ☆
☆ - only exception among big economies to have this shift, a puzzle for many

	Share in Employment		Share in GDP (Real)	
Agriculture	≃ 50%	complete lack of correlation	≃ 14–15%	Disguised unemployment
Industry	≃ 15–16%	Some what correlated	≃ 21%	
Service	≃ 34–35%	not so well correlated	≃ 64–65%	

Strict Macroeconomic theory will tell that there should be correlation b/w share in Employment & Share in GDP. So that there must be ability to pay for jobs. But India is an exception in this aspect too.

No NSSO survey after 2011-12 so data may vary from source-source

<u>Disguised unemployment</u> – Despite being counted as employed, no contribution to GDP.

So <u>indirect measure</u> of it is via this correlation gap.

(sub-sector)
Construction → 9–10% of Empl. share
Construction → 7–8% of GDP share

may be part of → Industry / Services

Here, we are putting it under services as ESI does so.

<u>Secondary</u>
Industry + Construction.

⊗ TRENDS IN INDIAN EMPLOYMENT & UNEMPLOYMENT

Focus on understanding
Don't mug numbers.

	Period	Employment Growth rate
Pre reforms	1983-94	2.7% p.a
Post reforms	1994-2000	1.07% p.a
	2000-2004	2.62% p.a
	2004-09	0.4% p.a

— Jobless Growth (1990s)
Despite ↑GDP growth, Employment growth is lower.

Jobless growth back.

Structural changes post 1991 – ↑capital intensive industries, tech ↑, privatisation – might have been one of the factors of Jobless growth but not the major player, as after 2000 – the empl^mt growth rate ↑ed.

Indian employment is largely in unorganised sector, all these structural changes were in organised sector, so only this didn't play much in Indian emply^mt.

Main reason for Jobless growth & then surge post 2000:

1994-2000 → Not much govt. exp. on job creation as it was in 1983-94. Why? BOP crisis, IMF conditionalities (contractionary policy). Hence jobless growth.

2000-2004 → Govt-exp on job creation is again up. Hence the surge of emp. growth rate in this period.

So, there is Correlation b/w Govt exp. on job creation and employment growth rate during $\boxed{1980-2005}$

Year	Unemployment rate	Period	Emply^{Mt} Growth rate
1993-94	6%	1983-94	
1999-2000	7.3%	1994-2000	
2004-2005	8.3%	2000-2004	
2009-10	6.6%	2004-2009.	

Why ↑ in unemp^t rate despite ↑ in empl. growth rate during 2004-2005?

Increase in LFPR { Labour force Growth Rate > Jobs growth rate } → Higher unemploy^t. rate

Despite growth of job creation, Labour force number is also crucial in unemployment rate.

Why ↑ in Labour Force?

The answer is not simply population growth rate as we had it before also. But, answer is:

* Demographic Dividend → Higher share of Younger (≃ 15-35 yrs) working age group population.

'Dividend' → +ve term → POTENTIAL for Higher eco. growth.

Though not Guarantee as there are certain conditions

CONDITIONS (to utilise demographic dividend +vely)

1. Education.
2. Skill Development.
3. Health.
4. Creation of Productive jobs.

a) ~~Either~~ the dividend achieves 1, 2, 3 & becomes productive.

b) Productive jobs are created in economy.

When these 2 happen simultaneously, greater economic growth.

Successful examples of Demographic dividend:

* JAPAN * S. KOREA * TAIWAN * CHINA & other east Asian economies.

East Asian Miracle → Unparalleled economic growth due to demographic dividend

Indian uniqueness → Longest ever demographic dividend [2000–2030], so more scope.

But, we've crossed half way but not much for conditions.

→ Education – Yes improvement, but quality ×

→ Skill devt. – Yes, but need more

→ Health – Not much. infact poor than neighbours.

→ Creation of Prod. jobs – Lack from 2005.

If within 10 yrs, we are not utilising this then post demographic dividend there comes a period of <u>BACKFIRE</u>: Now JAPAN is going through it. (i.e) ↑↑ in DEPENDENT Population, ↓↓ in WORKING population.

	Emplmt gr. rate		Unemp.t rate
2000–04	2.62% pa	2004–05	8.3%
2004–09	0.4% pa	2009–10	6.6%

Hear Neo-Liberal IMF/WB

INDIA	US
Mostly unorganised	Mostly organised

Hence market dependence is not much suitable to India. Govt's role is imp. here.

why despite ↓↓ in employment growth rate, unemp is also down?

Decrease in LFPR.

why? No NSSO (5 yrly HH survey) after 2011-12.

Till 2015-16 → We have limited Annual Survey on employment → by LABOUR BUREAU.

Post 2016 → No survey. Only EPF audit.

[2005 – 2015]

II <u>Lower Empl. Gr. rate</u>:

but GDP growth is there (Below 1% pa)

<u>JOBLESS GROWTH.</u>

Why? ↓ in LFPR
- → RURAL
  - Male → Stagnant
  - Female → Most significant decline
- → URBAN
  - Male → Some Increase
  - Female → Decline

1st school of Thinking : Don't worry abt Jobless Growth.

Most economists say that decline in female LFPR is not bad in Indian case. why?

Reasons behind ↓ in Female LFPR :

i) Education : Higher enrolment rates since 2004-05

- More rise in rural than in urban (% increase)
- More rise in female than in male.

Since they are students now, not a part of labour force.

ii) Change in HH Income — Female LFPR

Inverse relationship

As HH income increases beyond benchmark, the female LFPR decreases (voluntary or forced is another debate).

So since 2004-05 : Rural HH income have increased definitely

why? MGNREGA, 2006

Decent Agricultural growth.

iii) Mechanisation of Agriculture

↑ Capital Intensive ↑ Tech

So ↓ in human employment
- Male — Stagnant
- Female — sig. decline

Mechanisation replaces more of women oriented jobs,

Men ; Women

↓ More skilled jobs. ; ↓ Low skilled jobs

Gendered div. of labour in Agriculture

(i), (ii), (iii) majorly show reasons for decline in rural female but not in urban female.

This is what worries the other economists & Sociologists.

2nd School of Thought: Jobless growth is a problem. (from social angle)

Sociologists → ↓ in urban female LFPR due to unfavourable SOCIO-CULTURAL factors.

[2005-15]

2 Change in Occupational Structure:

(i) Decrease in emplyt in Agriculture → Higher share already so obviously ↓ is bound → Mechanisation of agriculture

— Not surprise; not bad

(ii) Decrease in Employment in Industry → lowest share already → ↑ potential for creating productive jobs

— Surprise; Unfortunate

Already low share, again ↓ is very bad.

↑ potential but not bein utilised – very -ve feature.

(iii) Increase in employment in Service — atleast 1 sector is giving jobs.

But

Not necessarily very good – why? →

Post-2008

More job-loss in organised sector

– Not much cyclical unemp. as in other countries –

But, unorganised empl. was not much affected.

Ask: Women – HH work – not part of GDP

Indian Service Sector

Traditional

→ ↓ Tech. intensive

→ ↓ Remuneration

- Comparitively less share on GDP
  - > Transport
  - > Construction
  - > Postal
  - > Social Services.
- ↑ Employment share here

Modern

→ ↑ Tech. intensive

→ ↑ Remuneration.

- Higher share on GDP
  - > IT, IT related services (BPO..)
  - > Communications (Telecom...)
  - > Financial services.
- ↓ Employment share here.

---

i) Poor quality of employment

Lower wages. Why?

ii) Poor emp growth rate

Poor correlation b/w GDP share and employment share.

* Another dimension of JOBLESS GROWTH

⇒ POOR QUALITY Of Jobs created ⇐

(Traditional service)

So.....

JOBLESS GROWTH is the real problem & not much optimistic.

* Latest feature of Jobless growth

More jobs than industry.

But since last 5 yrs we are seeing ↓ in Jobs in Modern services.

Why? AUTOMATION

The only potential for productive jobs so far also now eaten by Tech.

"So, the next best potential for creating productive jobs is INDUSTRY."

But... some modern services still have scope:

- Education
- Health
- E-commerce

Mostly under Govt. but no genuine effort to create jobs.

ORGANISED & UNORGANISED SECTORS

Generally it is referred:
Organised → Formal
Unorganised → Informal
But there are some diff. in technicalities.

Note: Whenever a sector or sub-sector is contributing to GDP, it is commonly expected to give decent wages atleast better than dull sectors.

ORGANISED ENTERPRISE

Legal {
> 10 or more hired worker (with Electricity as an Input)
> 20 or more hired workers (w/o Electricity " " ")
}
> Registered Tax Payers – Recently considered organised even if 10 or less workers.

> Better quality of employment
✓ Higher wages ✓ Social Security benefits
✓ Job security (more permanance relatively)

UNORGANISED.

NSSO (2009-10) → 85% jobs from unorganised.
Hence, overall quality of jobs is poor. (POV from hired workers)

Construction
→ By hired workers definition → Organised & even by tax payment
→ By quality of employment → Unorganised (↓ wages; No soc. security; no job security)

(2004-05) NCEUS / Prof. ARJUN SENGUPTA COMMITTEE

NCEUS – National Commission on Enterprises in Unorganised Sector.

'Informal workers' Term given by him:

- ✓ Employed in Informal sector +
- ✓ Employed in Formal sector but nature of employment is Informal.

So, no. of informal workers > Unorganised sector or Informal

	Informal workers
2004-05	91.2% jobs
2009-10	92.4% jobs.

Committee told 85% was underestimate. So, the problem is more severe than it was thought.

No update after 2010, but still the phenomena exists:

'Informalisation of Work Force'

↓

— Poor quality of jobs —

↓

— POVERTY —

Note:

Read: 'UNORGANISED' as unorg. SECTOR

Read: 'INFORMAL' as Informal WORKER

[2017-18] → Good for Job Creation

7mn jobs created-claimed — Payroll Data (EPFO Data)

More EPFO Enrolment.

EPFO doesn't reflect unorganised sector.

Limitations of EPFO Data (in terms of Job creation)

i) Many EPFO a/c inactive

ii) Many a/c are <u>DUPLICATE</u> — already have EPFO a/c, & don't reflect new jobs (but opens another)

iii) ⟹ <u>2016, PM Rozgar Protschan Yojana</u>

To create more formal jobs

Govt. will bear P.F. contribution from employers for 1st 3 years. → Bcs of this more EPFO <u>ENROLMENT</u> & not <u>JOB CREATION</u>.

iv) Post-GST ⟹ More incentive for formalization (Input Tax Credit)

(18 out of 21 already exist).

EPFO says 21 jobs created but only 3 created.

EPO data useful ⟹ Tells abt Formalization of Workforce

Just formalization doesn't guarantee <u>Good quality</u> Jobs

Comes with better Edu, Health, Skill dev, Demo-Dividend. ⟸ when ↑ productivity of worker ⟸ Need ↑ Wages ↵

Qn: what is the reliable data to see enrolment, unemployment, job creation (as NSSO stopped)

REASONS BEHIND INDIAN EMPLOYMENT SITUATION

≃ why Indian Industries couldn't create Jobs? [open ended. Add extra also.

① i) Lack of Industrial Growth   Need - Higher Indus. growth

— Till 1980 - very little Indus. growth (except Mahlanobis strategy - ✓ for a short time)

ii) Post 1980

↳ Discontinuous Industrial growth

- 1983-88 → Consumer durables, automobiles; M. Suz - 1st in Gurugram → BOP problem
- 1993 — 97: Indust. sector reforms; E. Asian crisis, Internal instability (Political)
- 2003-08: ↑ in FDI; 2008 Eco crisis

This discontinuity not enough for job creation as it takes atleast 10 yrs for it - regular growth

↳ Capital Intensive Industrialization

In a labour abundant economy like India, ONLY capital inten. Indus. not enough. We need productive labour Intensive Industries

General notion: Labour intensive indus - inefficient — No.

It depends on the sector - its nature:

Ex: $\underbrace{\text{Textile ; Apparel ; Leather ; Footwear ; Food Proce.}}_{\text{Labour Intensive + Productive (Efficient)}}$

Higher productivity or Jobs ??

→ We need to balance both : Produc. lab. inten. jobs.

→ In case of conflict, choose productivity even if it means sacrificing job creation. Why? What is the use of no. jobs w/o productivity - It will eventually lead to Informalization. In no case unproductive Jobs are of no use.

* i) & ii) are also reasons why no. of jobs jumped from Agri → Services bypassing Industry.

② iii) Lack of Skill Development

High skilled - (Indus, Modern Services) Here

Low skilled - (Agri, Traditional services)

Even with higher Industrial growth, job creation is not guaranteed w/o skill development.

* Hence, again a reason for jump from:

Agri → Trad. services esp. (from 1 poor quality job to another poor quality job)

INSTITUTIONS

ITIs → Skill not matching with required skills

Mismatch b/w Available & Reqd. skills.

Survey of Industrialists revealed this.

They told they would like to create more jobs but the skills are not met. Hence even if jobs ↑, low wages only

Solution: (to ITI problem of mismatch)

✓ More active role of Industries in Skill Development.

⇒ APPRENTICESHIP / INTERNSHIP – learning by Doing.

But, now industrial profit is very low now, so they are less interested in spending time & money on apprenticeship.

✓ So, Role of Govt. is required in terms of FUNDING.

In fact, now this is now starting. But need more.

③ Rigid Labour Laws:

Labour laws → for Welfare of workers
(wages, social security, working conditions, ...)

Rigid → Numerous – 38 labour laws
Rigid → Outdated – even pre-independence ones exist

→ Industrialists claim that they create only less no. of jobs compared to what they could've due to RIGID labour laws.

Industrial Disputes Act, 1947

→ 3 steps to resolve any industrial disputes (worker vs employer)

1. Mutual talks 2. Labour Tribunals 3. Judiciary

> Most disputes not resolved in 1. & 2., but only by 3.

> Most rulings were in favour of Workers.

This created a poor environment for creating jobs.

Caution in hiring workers to avoid cases/disputes.

→ Any industrial unit with 100 or more workers, they must get govt. approval before firing any worker.

Hence, even if I want 110, I will stop at 99 workers to not cross the 100 workers threshold.

Solution: (to jobless growth)

✓ LABOUR REFORMS

Wide: lab. reform.

Less rigid labour laws w/o sacrificing the welfare of the workers; Flexible hiring & firing policies.

Narrow: more like IDA reform.

It is a STATE SUBJECT.

Ex: Rajasthan → very active in lab. Reforms

Increased the IDA threshold from 100 to 300.

Recent proposal:

I] Replace 38 Labour Laws by 4 Codes

1. Code on Industrial Relations
2. Code on Wages
3. Code on Social Security
4. Code on Occupational Safety, Healthy & Working conditions.

Limitations:

→ Many labour reforms are not concerned of worker's welfare but merely simplifying & making flexible to hire & fire. They are more Industry specific.

→ One feature of Code on Wages: Freedom to states to determine different minimum wages

But, it contradicts: Equal Pay for Equal Work – DPSP.

→ Also, strikes by workers may be taken easily illegal.

Migration (Inter-state) → until it is optimum – good & necessary for driving eco. growth

(LR) 13.3

→ It will only mainly benefit the Organised Sector jobs.

Ex: Rajas. change will not benefit industries with < 100 workers
most industries have ≤ 20 workers.

Why Unorganised sector is not changing to organised sector?

④ Lack of Shift from unorganised to Organised Sector

It is basically about increasing the Scale of Production.
So, why not? (↑ capital ; ↑ people)

i) Lack of Credit. [MUDRA, Priority Sector Lending]

↳ Neither of them are picking up. why?

× More NPAs within MUDRA. why? Post-Demonetisation phenomenon – 2016; Unorganised sector is largely cash-driven & hence it ↑ NPAs.

× poor performance of Banks. (↑NPA; ↓ Cap.Ad)

ii) Lack of Infrastructure – Road; Electricity; etc.

iii) Lack of Marketing Opportunities – Ads are costly.

Problem with Ease of Doing Business: [Add more to this from Editorials.]

It is only from perspective of WB (i.e) from western/developed countries perspective.

We need to address the ground realities – say dispersal of credit, etc.

TOPIC-5

POVERTY

— Here, only economic dimension. Add Social & political dimensions & even others also.

ABSOLUTE

Lack of some basic Minimum requirements.

RELATIVE

Income < some proportion of per capita income

(differs from country to country say 60% of per capita)

→ Officially this is not calculated in India / devg. countries. Mostly, only devd. countries do it.

→ But we do measure INCOME INEQUALITY (Rich-poor gap)

↑ in Inc. ineq, also ↑ Per capita Income

– Ironical bcos PCI is also a factor of development.

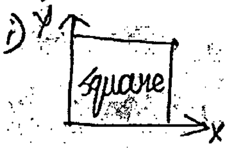
– As such pulls more, more & more ppl will have less income.

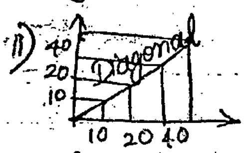
Measures on Income Inequality: (Prelims oriented)

1]. Lorenz Curve

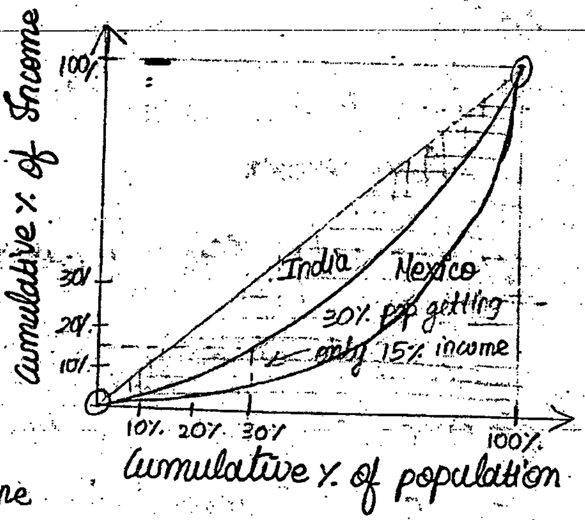
Cumulative % of population
- starting from the poorest.

Geometric property:

i) 

ii) 

Perfect equality line



Why always on right side of diagonal? - bcos we start from poorest.

→ The farther the curve is from Perfect equality line, the more is the income inequality.

→ It will be complex for more no. of countries. So next:

2]. Gini Coefficient

$$GC = \frac{\text{Area b/w Perfect equality line \& Lorenz Curve}}{\text{Area of Half-square in which L-curves lie (fixed)}}$$

Farther the curve from P.E.L, ↑ the area, ↑ GC, ↑ IneIneq.

So, Higher the GC, higher is income inequality.

Range → $\underbrace{0}_{\text{Perfect Equality}}$ to $\underbrace{1}_{\text{Perfect Inequality}}$

Perfect Equality & Perfect Inequality → Unrealistic

General rule ⇒ It should not go beyond 0.5

>0.5:

Latin America; USA

<0.5

East Asia (Japan, S.Korea)
Scandinavia

INDIA : 0.37 (Govt.data)

It is based on consumption expenditure rather than Income. why? Income data is not easily available. why?

- ↓ no.of. IT payers. (Small IT base)
- Most ppl genuinely can't say their income
  Ex: Subsistence farmers don't sell/earn much. So,

CONSUMPTION EXPENDITURE

Closest ~~substitute~~ to Income
More universal than Income (all buy things even if not sell)

INDIA : 0.55 (Independent calculations)

→ Our Inc.inequality is definitely higher than Cons.exp GC

→ No a/c of asset based inequality / Wealth inequality.

How to quantify assets (Gold, land, shares...)?

Land is the most preferred asset.

So, Gini Co-eff :

ON LAND OWNERSHIP : 0.70

→ Just an indication of economic inequality.

→ There are Sociological Dimensions:

- Social Group (caste)
- Gender
- Regional

Read Editorials on this

MEASURES ON ABSOLUTE POVERTY:

1] Poverty Line (PL)

Level of consumption expenditure needed by a HH to fulfill basic minimum requirements for all members over a time period.

Ex: Suppose - 5000 Rs. per HH per month.

Income based poverty line – Relative poverty – in devd. countries

Limitations:

× It is a relatively crude measure of poverty.

APL HHs A (Rs.1010)

PL ——————→ Rs.1000/person/month.

BPL HHs B (Rs.990) C (Rs.500)

Problem: B has better standard of living due to being technically BPL via subsidies, etc. A still suffers. Hence, crude.

2] Head Count Ratio (HCR)

$$HCR = \frac{\text{No. of BPL HHs}}{\text{No. of Total HHs}} \times 100$$

✓ Incidence of poverty → Proportion of poor population.

If method is PL, then HCR can give Incidence.

× Depth of poverty → Rs.100 or Rs 900 in same category

Shortfall from PL: Ex: B-10 ; C-900 ; D-100

II. Poverty Gap (PG)

Average shortfall from P-line over entire population.
(BPL+APL)

PG- It refers to average income needed to take the entire BPL population on the Poverty Line.

- The resource for it will come from APL.

✓ Depth of poverty (addressed the limitation of HCR)

(Even when incidence (or) HCR of poverty is same b/w 2 countries, the greater the PG, the more deep is the poverty)

Poverty Gap Ratio (PGR)

$$PGR = \frac{\text{Poverty Gap}}{\text{Poverty Line}}$$

POVERTY ESTIMATION IN INDIA

Step 1: Definition of P-line

Quantifying Basic Minimum Requirement

Planning Commission defined it through Committees.

1972-73: Dandekar & Rath Committee

Pioneer in Calorie-Based P-line

Nutrition aspect only as Basic min. req.

CALORIE BASED P-LINE

Rural — 2400 kcal/person/day

Urban — 2100 kcal/person/day

From 1972-73, existed till 2004-05 (with little changes)

Step 2: Data Collection → CONSUMPTION EXPENDITURE

By NSSO – 5 yearly surveys

✓ CONSUMPTION BASKET

List of food & Non-food items used in survey

→ 3 METHODS:

1. Uniform Recall Period (URP)

With what reference period the NSSO is collecting data & it is uniform to both food & non-food items.

URP: 30 days.

Food consumption is more regular than non-food, hence ideally it should have a shorter period than non-food.

2. Mixed Recall Period (MRP)

Food → 30 days

Non-Food → 365 days

3. Modified Mixed Recall Period (MMRP) (After Ten. Committee only)

Perishable or costlier foods, bought more regularly in smaller quantities.

Some food items → 7 days ; other food → 30 days

365 days → Non-food items

HMRP gives more reliable data as ppl can recall milk consumption of past week rather than month.

Step 3: Adjustment of Consumption Expenditure for differences in Rural & Urban Inflation

Using PRICE INDEX

Till 2004-05 → Using CPI

Step 4: Comparison b/w P-line definition & Adjusted Consumption expenditure

Suppose, $\underbrace{\text{Rs. }1000/\text{person}/\text{Month}}_{\text{P-line}}$; HH_1 - Rs. 950/P/M } - BPL → Result

HH_2 - Rs. 1090/P/M } - APL

HH_3 - Rs. 1300/P/M

Adjust. Cons. Exp

2004-05: Tendulkar Committee

BG as to why the need for this committee:

POVERTY DEBATE → whether official HCR underestimates actual poverty?

Why this debate?

Diff in estimates from diff sources

2004-05 → 26% - Indian survey by PC.

WB p-line

2004-05 → \$1/P/Day at PPP

→ 42% of Indian HH is BPL.

NFHS (National Family Health Survey), 2004-05:

46% of children → Malnourishment

Drastically diff from 26% of another survey (P.C)

Hence, to address the lack of correlation, the new committee

Recommendations of TC:

1. Uniform Rural & Urban Consumption basket in poverty estimation. – Temporary solution for outdated cons basket

But, realistically urban basket is more qualitative. so, he recommended: keep urban basket same, but upgrade the rural basket at urban level.

Why? Major problem is outdated consumption basket decided in 1973-74, never changed for 30 yrs.

Permanent solution: Will be time taking, so gave a temp. soln.

– change both baskets, upgrade both.

– Then, need new survey for it → It takes time ≈ 5 yrs

2. Move beyond Calorie based P-Line

Calories + Non-Food Expenditures → EDUCATION, HEALTH } Indicators of Human Capital (even though only minimum)

3. Poverty Estimation should be on MRP – basis only (i.e) only 1 uniform method. why?

✓ Conceptually better

✓ Easier comparison of poverty over time

4. Price Index used in Poverty Estimation

FISHER'S PRICE INDEX (one of the best in statistics)

It can be calculated using data on quantity and Expenditure from SURVEY.

Then why not use FPI for overall Inflation measurement?
Bcos, Inflation data is req. more regularly, so we can't go for survey (time taking). So CPI is better in time than conceptually better FPI.

2011-12: Rangarajan Committee

TC itself said it is only temporary.
Also NSSO survey year 2011-12.

→ TC & RC were on same page on FPI.

New Recommendations:

1. Separate Consumption basket for Urban & Rural Poverty.
   More realistic, not contradictory by evolution.
2. More Comprehensive P-Line Definition than TC.
   - → FOOD → Calories + (Min. Protein & Fat requirement) — ICMR recomm. based
   - → NON-FOOD → + Min. exp. on → House Rent, → Conveyance
3. Poverty estimation must be on MMRP basis.

Politically TC recom^s. were accepted, but RC recom^s. were ignored by NDA govt. in 2014.

Academically RC is much better & acceptable.

Post 2014 – PC abolished & NITI Ayog too didn't take up any poverty estimation measures.

HCR

	TC	RC	
2004-05	37.2%	–	Earlier: 26% by D&RC
$\boxed{\text{2011-12} \quad 22\%}$		29.5%	

↓ Last official poverty estimate so far

→ Significantly, poverty is declining over time by all records.

✓ This is esp. good for Agriculture.

↳ Better agri. growth, generally, ↑ Rural Income → ↓ Poverty

Poverty lines (TC) → @ 2011-12 prices	RC
Rural P-line → Rs. 812/person/Month.	≃ Rs.970/P/M
Urban P-line → Rs. 1000/person/Month.	≃ Rs.1400/P/M.

Has TC ~~addressed~~ settled Poverty debate?

Partially yes: But not completely.

Bcos, P-lines are criticised to be very less by media.

Yes, they are lower.

But, we should not forget the challenges faced by the committees in poverty estimation.

CHALLENGES FACED IN POVERTY ESTIMATION:

1. Subsidies are not accounted for in poverty estimation. Bcoz it is complex.

   If accounted, HCR will reduce as subsidy amount will be added to Cons. exp.

2. Under reporting Consumption Expenditure by HHs.

   If this can be corrected, again HCR will fall. This will reverse the poverty debate.

Ideally, there is scope to increase PL → for which RC is important.

(Yet, depth of poverty is not declining as much as incidence of poverty — challenges are in poverty est. itself, so in PG est. even bigger.)

ALTERNATE MEASURES OF POVERTY

- Poverty: lack of Monetary resources → based on only cons. exp.

But, modern view tells poverty is not just about monetary resources but lack of CAPABILITIES.

AMARTYA SEN

CAPABILITIES:

→ Freedom to perform some functions in society.

Ex: Even with money, if illiterate & unhealthy & unskilled, he/she will still be poor / not free to perform.

Also, lack of basic amenities – clean drinking water, good quality air, sanitation.

Don't measure poverty only on money. Money can be a subset of capability, but not the only thing.

1. SOCIO-ECONOMIC CASTE CENSUS, 2011 (SECC)

7 Indicators for HH survey

a) Nature of houses – shows standard of living
b) Adult Literacy
c) Land Ownership – ⊗ esp in rural case.
d) Caste – HHs → SC/ST, Non-SC/ST – to compare the indicators b/w the 2 categories
e) HHs w/o Adult Member
f) Female headed HHs
g) HHs with differently abled members.

Welfare benefits will be given on SECC data.

LIMITATIONS:

i) Immediate need to upgrade.
Need a regular 5 yearly SECC.

Ask
child in SECC

ii) No health Indicator in SECC.

iii) No objective definition of Poverty.

2. MULTI-DIMENSIONAL POVERTY INDEX - Read the Summary

By: UNDP, & Oxford Poverty & Human development Initiative (OPHI)
(also does HDI as HDR)

→ 3 Indicators

✓ Education (2)
✓ Health (2)
✓ Standard of Living (6) - (water, Elect, Sanitation, Asset)

similar to HDI

HDI	POVERTY
Talks more of achievement	Talk about deprivation,
More health, more HDI	only about basic req.
More Edu, more HDI	

Poverty as per MPI

Deprived of 3 or more Indicators classified as Multidimensionally poor HHs.

INDIA		MPI	TC
	2004-05	>50%	≃37%
	Recent	28-29%	

But actually ≃20% of India would be Poor by Cons.exp.

* Indian poverty is more about lack of Edu, health care, basic amenities than lack of monetary resources.

SOLUTIONS TO POVERTY

Note: Very wide. Add on your own. Scope is huge.

Anything improving Edu/Health/basic amenities will come under solutions to poverty.

1. Directed Anti-Poverty Programs/Empl. Generation Programs:

Since 1980s

→ Directed → Bcos indirect measures didn't work

For ex: Trickle down effect didn't work much.

→ Identify the poor HHs

→ Provide them with employment opportunities.

i) Self Employment programs

ii) Wage Employment programs

SELF EMPLOYMENT PROGRAMS

Provide poor HHs with Income Generating Assets.

Ex: Sewing machines, etc.

Challenges:

→ These assets are costly. So ↑ expenditure.

Fund — Govt. Subsidies + Bank Credit

But banks are not much willing due to ↓ credit worthiness

Recent Changes:

✓ Poor HHs are supposed to arrange themselves in SHGs.

✓ Then they are given Micro-Finance based Credit.

Credit to: (Ideally)

> Poor HHs > SHGs > Lower Interest rates.

Pros:

✓ Cheaper credit

✓ Improves Credit worthiness: through better Ability & willingness to repay loans.

Ability: Loan to one is riskier than loan to a group

Willingness: Group members will pressurize others to pay back

PEER PRESSURE

- Group rewarded - if paid back
- Group penalised - if not
- All Group based & not individual

#In India, microfinance has not worked as well as in:

#<u>BANGLADESH</u> - <u>Best Microfinance in the World</u>#

↓ <u>Repayment rate</u> - >95% : Unparalleled Achievement even > devd. countries.

(Mohammed Yunus)

<u>LIMITATIONS</u>:

i) Loans of SHG from → MF Institutions / → Banks

But, some MFIs have been criticised for ↑ Interest rates even above banks & also accused of giving loan to such also.

Malegam Committee

After this interest rates would come down.

Due to SHG model, nature of income generating assets have also changed.

MICRO ENTERPRISES (≃ Cottage Industries)

SHG will set up ME & come out of poverty.

<u>Schemes</u>:

Many earlier schemes integrated into 1 scheme:

Swarna Jayanti Gram Swarozgar Yojana # [1999-2000]

Rural self employment scheme

Rural poor — SHG — Micro finance — Micro enterprises

One problem in India has been, we've been more focussed on Wage employment programs due to Political factors.

But, Self Employment programs are significant:

* Solution for JOBLESS GROWTH.

How? o Micro finance or ME are Labour intensive

o Most SHGs are Women-based.

(Majority beneficiaries are women) — 90%

— 1st SHG - 1970s SEVA, Gujarat (1974)

— Started as DWCRA - Under Women & children welfare.

Why women? They can remain in House & earn - Comfortable.

EX: Food processing; Crafts

↓

esp: Western & Southern states

WAGE EMPLOYMENT PROGRAMS

Creation of community Assets

Rural Wage Employment program:

Solution to seasonal unemployment (as it is in demand during lean season)

MGNREGS, 2006

Features:

① Launched under NREGAct, 2005 → legal Right to work.

Earlier schemes were welfare schemes, this is right.

Legal guarantee → 100 days of employment to an adult member of every rural household given that these members are willing to do unskilled manual work.

For drought prone areas → it is 150 days

The days is min. / guarantee – more is possible.

Also more than 1 person from any (poor or non-poor) rural HH can work. But the guarantee is only for one.

This is to be told better targetted than self targetted ~~method~~.

(i.e) The very fact that a person comes for unskilled manual work is itself a proof of his very need of work badly.

② If a person doesn't get work within 15 days of application → Unemployment Allowance (SG) ← 1/3rd of wage

CSS (Centrally Sponsored Scheme) → 90% : UG

To make states also accountable.

③ Nature of Work

Must be related to management of Natural resources.

Logic: To link scheme with Agriculture

Why? Indian Agri is lower also due to mismanagement of natural resources.

During absence of Agri work in
lean season

Provide work to sustain livelihood. ← → Manage natural resources which can help agriculture productivity in future.

④ Implementation:

Earlier, schemes were beaureaucratically implemented.
But, this is to be mainly implemented by
GRAM PANCHAYATS.
↳ Best suited to choose an appropriate village specific community work. } Empowering gr. pan - Authority

> District Panchayats
> NGOs
> Govt. department

} Panchayats can take help from them.

⑤ Demand Based Fund Allocation:

Funds will be given to gram panchayats only when they raise demands for it.

Earlier schemes: Top-down approach ; Here: Bottom-Up approach
✓ Better governance

Empowering gram panch - Accountability
How? They'll demand funds only when they've made plans.
Thus Authority & Accountability is balanced by ④ + ⑤.

⑥ Equal minimum wages for → Men
→ Women – Atleast 1/3rd of total jobs to women.

✓ legal

✓ Inflation Indexed (i.e) automatically rise with inflation.

Thus keeping wages higher & ensuring better standard of living.

⑦ SOCIAL AUDITS → Scrutiny of MGNREGS accounts.

Muster rolls : other name for MGNREGS accounts.

- where work?
- what work?
- How many jobs?
- Money given/not?

→ Not just financial aspect but also to social aspects.

Why? To enhance Transparency & check malpractice.

Originally audit tasked to Gram sabha to be submitted to RURAL DEVELOPMENT MINISTRY.

APPRAISAL OF MGNREGS

Criticisms:

1) CORRUPTION in implementation

Fudging of muster rolls

Either
- no guarantee of work or
- no min. wages or
- delayed wages

But, now some states moving to e-muster rolls.
So, decreasing corruption: diff. to fudge ↓.

Data Source

IHDS – India Human Development Survey
– Only source of All India survey of MGNREGS.
By: NCAER (New Delhi) + University of Maryland (US)
→ Free of bias.

ii) POOR TARGETING : 65% of beneficiaries from the scheme belong to non-poor HHs (though not illegal, but ideally there should be more poor HH beneficiaries)

Significant inter-state differences in implementation

Good implementation → TN, Kerala, Ar. Pradesh, Chattisgarh, Rajasthan (unique); All NE states except Ar. Pradesh (strong gram panchayats)

Bad implementation → UP, Bihar, Pun, Har, Maharashtra, Karnataka.

(a) Implementation depending upon POLITICAL WILL & Governance capability & quality.

(b) Awareness among beneficiaries.

TN → Earlier women participation very low.
Then became 1st state to provide creche facilities so that women could participate.

But we can't single out MGNREGS for criticisms, it is due to poor governance. So pol. factors criticise it more rather than of financial factors.

iii) Poor Quality of Assets

Wage to material ratio

Earlier : 60 : 40 @ gram panchayat level.
Now : 60 : 40 @ District panchayat level. → For larger scale infra projects. Ex: Irrigation.

But also, increasing material share can ↑ corruption as middlemen who handle it don't come in social audit.

Problem of new rule:

- May take out some autonomy of gram panchayats.
- Infra is good but this scheme is primarily for wage employment, so scale of infra must not overshadow this objective

iv) Higher Inflation

Higher wages in MGNREGS ⟶ Higher wages in other sectors of economy ⟶ ↓ rural-urban migration

↓

↑ in cost of production

↑ in supply side Inflation

But actually this indicates the success of the scheme. Also, MGNREGS is mainly in lean season, then how can it ↑ inflation throughout the year.

Benefits

i) Poverty Reduction

↑ wages   Better Financial Inclusion

Initially: Cash wages; Then: Post offices via / Bank a/cs
1st by An. Pradesh

ii) Higher Enrolments of children in MGNREGS HHs.

✓ ↑ Wages ⟶ families more capable of spending on Education

✓ ↓ in child labour: Bcos, adult members mainly send child to work due to job & money compulsions.

iii) Women Empowerment

- 1/3rd jobs; Equal min. wages
- 45% of women beneficiaries claimed thus 1st wage employment was under only MGNREGS. Earlier not in job or not paid (disguise unemp)

→ Money to women – productive use like for children than use by men.

NDA → Initially allocated more money to MGNREGS
Aadhar linkage also talked about

But recently → lack of funds.

As per this scheme – Benefits are talked less & criticisms are talked more which should change

SUBSIDIES

Transfer Payments by govt. to Consumers & Producers

Ex: PDS – Consumption subsidy
Fertilizer / MSP – Production subsidy.

Criticisms of subsidy: (By Economic theory)

i) Wastage of Resources.

(i.e) Discounted products are overpurchased.

Ex: Overuse of urea as it is highly subsidised, affects soil fertility – ↓ productivity } chain of wastages.

ii) Increase in Govt. Burden / Fiscal Deficit

iii) More the subsidies → Lesser the public investments (Govt. investments)

↓ Sacrificing long term growth for short term growth.

↓ Needed for long term growth.

Ex: Fertilizer subsidy vs Canal building

Justification of Subsidies:

For poor consumers & Poor producers.

Basic min. requirements primarily: Food grains (PDS)

esp. farmers
- To buy basic inputs to sustain business/agriculture

Food security concern if farmers leave the job.

- Agri. riskier economic activity as it is very dep. on natural resources. so need to (MSP) mitigate risks.

Basis: whom to give?

SUBSIDIES

Indirect → "In-kind" subsidy: Goods provided at lower prices. Ex: PDS

Direct (or) DBT (or) Direct Cash Transfers. → "In cash" subsidy: Goods provided at higher prices & may/may not be market determined. amount deposited in bank a/cs. Ex: LPG subsidy

Basis: How to give?

which is better?

By theory, Direct subsidy is better & govt. has been moving in this direction.

PROBLEMS WITH INDIRECT SUBSIDY:

① Poor Targeting → More room for corruption

How? Subsidised good crosses many intermediaries bfr reaching beneficiaries. Each step has room for corruption. Ex: PDS

say, MP wheat PDS price → Incentive to sell in market for ↑ price.—
20 Rs. 2 Rs.

Black Marketing: Selling PDS grain at higher price in open market. — PDS leakages

How much of grains leak out of PDS.

~~Indirect~~ Direct subsidy → Here too bank employees may be corrupt too.

Indirect subsidy is overly criticised bcos we have a 60 yr history of it. But we should remember, Direct subsidy is just 6 yr. old & we really don't know what it may hold

(2) Higher Govt. burden on indirect subsidy

Administrative cost

Salaries, offices...

Supervision Cost.

To check corruption.

Transportation cost

Storage cost.

— ↓ in direct subsidy

— But, these will remain in direct subsidy as same

(3) Less freedom of choice to beneficiaries than direct subsidy. But that is also only RESTRICTED FREEDOM subject to certain items.

Challenges with Direct Subsidy:

Despite being theoretically better, it has some challenges.

① Lack of <u>Financial Inclusion</u>.

② Lack of <u>Unique Identification</u> of beneficiaries.

w/o this, we may again face problems of poor targeting.
Like Fake beneficiaries. Ex: PDS → lakhs of fake ration cards.
This will come in direct too, that too even more → How?
In indirect - incentive is getting cheap goods & selling in markets;
In direct - incentive is direct cash but with req. of just 1 bank a/c

Aadhar is helping in this ②. Its spread is very impressive.
Yet, challenges are:

a) Possibility of duplication of Aadhar - UIDAI outrightly rejects it, but possible.

b) Even with Aadhar, we need Infra support.

Say for - Biometric authentication: Electricity, fast internet, scanners, missing in many parts esp. rural ← Point of sale devices, etc.

③ Possibility of less cash with beneficiaries &
Direct subsidy not insulated for Inflation.
↳ bcos 1st we buy at higher rate, only then subsidy is received.
↳ Value of direct subsidy in real terms will fall with Inflation.
Ex: Food inflation - very volatile

Conclusion:

1]. Any transition from indirect to direct subsidies should be gradual. → So that we handle situations one by one. Also there may be even more challenges than textual ones.

Real time problems Ex: Pilot project in 2 best districts of An.pradesh for fertilizer subsidy ⇒ Problem of finger print mismatch due to
- old age
- Nature of job (physical strain)

2]. Most crucial subsidies should be converted (if at all) to Direct subsidies only at later stage after transition.

→ So that poor consumers & producers don't suffer more by any failure during transition.

So need differentiation in subsidies.

Ex: LPG goes to more capable HHs ; PDS goes to more poor HHs. (relatively)

UNIVERSAL BASIC INCOME (UBI)

Basic min. income to be given in a near universal manner in bank a/c of beneficiaries unconditionally ↓

Near universal → bcos 100% impossible ; while direct sub is conditional.

(In ESI it was talked about last year (17-18))

BENEFITS :

1). Better targetting → In bank a/cs, so ↓ corruption

Most ppl would be covered, hence no genuine HH will be out, yet not genuine HHs may also get however.

2). Unrestricted Freedom of choice → unconditional (+ve)

3). Act as insurance against risks → say, when breadwinner falls ill, UBI will help + Health insurance kind of

CHALLENGES :

As obviously, Financial Inclusion & Unique Identification.

× Conspicuous Consumption → Unconditional (-ve) (wasteful use of resources)

× less incentive to join job market → less labour supply

→ But ESI says these are theoretical & we don't have much evidence actually.

Pilot Schemes : (In some areas) – No conspicuous consumption seen rather it is spend on Edu. health, etc (But the best HHs were selected in the 1st place)

Proposal → UBI equivalent to Tendulkar P-line.

≃ 800-1000 Rs.

So may not be a serious lack of incentive to work.

X Higher Govt. burden ≃ 4-5% of GDP.

when we are targetting < 5% FD, this is impractical.

ES|

→ In India: Many subsidies go to Middle class HHs → 1% of GDP

→ Food + Fertilizer + Petroleum subsidy → 2% of GDP.

→ Top 10 CSS → 1.4% of GDP.

But should these subsidies be replaced by UBI?

o Not a good idea. Too simplistic. Other subsidies are not only about money but also social factors (ex: MGNREGS)

o Poverty reduction $\xrightarrow[\text{includes}]{\text{also}}$ lack of Edu, Health, Basic amenities.

For these need Bigger investments
Ex: Electricity, water...

So before UBI need 1st Basic universal amenities (say, water, food, etc.)

How to be done?

Proposal to start with selective UBI. 1st to start with women UBI → But, money may not actually go in their hand.

AGRICULTURE

Lowest share in GDP – 1/6th.

Importance of Agriculture:

More durable solution than Subsidy, MGNREGA, etc.

Higher Agri. growth → Higher Rural Income → Lower Poverty (Rural)

Necessary, may not be sufficient

Controlled Rural-Urban Migration

If uncontrolled – urban poor is just shift from rural poor.

Lower Poverty (Urban)

More productive employment

Not all jobs in agri. is disguise unempt. There are also good jobs But youth aren't attracted to good agri. jobs but go for poor urban jobs.

demand side

↑ in demand for Industrial goods

↓

Higher Industrial growth

→ Lower Food Inflation

↓

Controlled ↑ in wages

↓

Low Cost of Production

supply side

→ Provide cheaper Inputs to Agro-based Industries

→ FOOD SECURITY – Basic food to all @ affordable prices.

Produce Enough (or) Import.

Only this is viable for us.

Challenges before Indian Agriculture

① **Lower / Agriculture Productivity** → Lower Agri. growth

(production per unit of area)

Since 1991 → not even 3% p.a. agri growth.

potential - atleast 4% p.a

Benchmarks for any agri. policy

Production is good but productivity is less.

Wheat, Rice, Pulses } worse productivity compared to other countries.

② **Lack of / Equitable Growth** → Benefits to large farmers & not to small & marginal farmers and nothing to landless farmers.

This is one reason why ↑ agri. growth not ↑ rural income

③ challenges from Globalisation → More competition from Agriculture imports. — Then why do we import?

PRE-1991 Indian Agri Sector

1951-65

1951-56: Public investment in Agriculture → Multi purpose river valley projects (Bakranangal, Hirakud, etc.)

Good Beginning

1956-65: Less focus on Agri. due to Mahalanobis strategy → Food crisis in 1960s

↓

Import food grains from US [PL 480]
Public Law 480.

>80% population directly/indirectly depend on agri. Impact is worst.
Also simultaneously with BOP crisis.

Learning: Agri. growth can't wait for any other sector to grow.

Post 1965 TECHNOLOGICAL MODERNISATION Of Agri

↓

Modern Inputs → HYV seeds (wheat, ...), Fertilizers, Pesticides, Irrigation

HYV seeds → Significant increase in ↑ Agri. productivity

⇓

Green Revolution

[Process of ↑ agri. productivity through use of modern inputs]

Irrigation
pre '65: Public investment
Post '65: Private investment (Tube wells etc.)

Green Revolution

1966-80	1980-90
a) Only limited ↑ in productivity	a) Significant ↑ in productivity
b) Limited to few states (Pun, HR, W.UP)	b) Spread of GR to other areas (Central, Western & Southern India)
Why? HYV seeds initially only for wheat. So wheat growing states benefitted. MEXICO	Why? By 1980, HYV seeds for paddy became available. PHILIPPINES
× Regional Inequality.	× Still, NE & E states left out, despite being big rice belts. – Political differences – lacked Pol. will. (But not completely correct though)
Problematic period	* $\boxed{\text{Excellent}}$ for Agri. & Economy
	% increase in 80-90 was never achieved before then nor even after that.

@upsc.risefinity

LAND REFORMS

Syllabus GS-III

Traditional	Modern
Pre-1991	Post-1991
(50s – started 60s, 70s – strong 80s – flattened)	

I. Pre-1991 / Traditional LR

Meaning
Rationale
Implementation

① Abolition of Intermediaries

Pre-Independence

Tenants $\xrightarrow{\text{Land Rev.}}$ Zamindars (Mahalwaris, Jagirdars) $\xrightarrow{\text{Land Rev.}}$ Govt

Why bad?

→ Exploitation of Tenants

B. Govt. was demanding very high land revenue from Zamindars.

→ Lower Agri. productivity

Unless someone is investing in agri. productivity won't ↑. But

B.govt → No interest in investment

Tenants → Couldn't invest due to ↑ Land Revenue

Zamindars → Should've invested as they would've got more revenue.

But why didn't they ? Zamindari rights were temporary - conditional on land Revenue & 40% time rights were auctioned - so they too didn't invest as they were not sure of getting fruits from it.

Post Independence

Tenants $\xrightarrow[\downarrow \text{ Land Revenue}]{\text{Direct +}}$ Govt

Why good?

✓ No more exploitation

✓ Some savings to invest back in Agricult. productivity

⇒ Best Implemented Land Reform in India

—○ Good Political Will with States (As Zamindars were pro British, easy to remove ; Also they were given Monetary Compensation)

At the time of Independence :

$\boxed{\text{TENANTS}}$

<u>Occupancy Tenants</u> → They had ownership rights over land before land Revenue system.

_ But this term is not used now, as they've now become land owners after benefiting from reforms abolishing intermediaries.

<u>Sub-Tenants</u> → Small landholders or landless ones. They've to cultivate in other's land.

This term is now synonymous with 'Tenants'

So, Only the Occupancy Tenants benefitted from the 1st land reforms.

② Tenancy Reforms

a) <u>Security of TENURE</u> (Time period of cultivation) for sub-tenants (i.e) sub-tenants must be given longer period / security & not to be evicted at the will of land owners.

Why good?

✓ Improve the welfare of sub-tenants

✓ More incentives to ↑ productivity to sub-tenants (even now most farmers are sub-tenants)

Despite all inputs to ↑ productivity, if the cultivator is not happy / benefitting from them. So this security is x in addition to better inputs.

b) Regulation of RENT

Rent may be monetary or part of produce (Sharecroppers).
W/o this regulation, security is not beneficial.

⇒ Not as well implemented as 1st reform (x Intermediaries)
—o lack of political will (land owners were politically powerful & they didn't want to share benefits with sub-tenants)

These both were Legal Reforms:
→ Zamindari Abolition Act
→

Yet why diff in implementation? lack of pol.will → Loopholes in law
× Discouraging sub-tenants to get legally registered.

But, in some states, this was best implemented:
* WB ; KERALA → Communist govt.
o MH ; GU ; HP — decently implemented.

WB

In 1970s — comm.party came to power & brought out an Operation Bargadar
- Registration campaign for sub-tenants.
Govt officials went from village-village to register as many of them,

Only example in E & NE India to achieve good agri. growth in 1980s –1990 despite not ~~initially~~ benefitting from GR.

This tenancy reforms will ↑ productivity is not a theory but living example of WB is proof. (Kerala also but it had GR too)

③ Land Ceiling & Redistribution of Surplus land to Sub-tenants (Landless workers): – LEGAL

Rationale → To decrease inequality in land ownership.

To ↑ incentives to ↑ agri. productivity

Implementation ⇒ Poorly implemented than ① & ②.

Even to give security land owners were hesitant, so no way they would give land itself to sub-tenants.

Bhoodan Movement: VOLUNTARY surrender of land.

× But, both Legal & Voluntary failed. Also some land redistributed was also barren.

× Land ownership based gini is very bad even now. – see

④ Consolidation of Land Holding – POST 1970s

Rationale → Small & scattered Agri. plots.

Why? By 1970s, population pressure on Agri was huge due to lack of jobs in industrial sector.

Why bad?

Less efficient Input use. Why? Rigid fencing to secure land

↓

↓ Agri. Productivity.

Meaning → Bringing small & scattered agri. plots in bigger blocks. ✓ More eff. input use ✓ ↑ Agri. productivity.

✓ Economies of Scale ✓ → ↓ cost of production; ↑ productivity.

Implementation: Except few states, not so good.

why? — Is it really necessary?

> Shift in ownership - resisted by farmers due to fear of loosing existing ownership (legally not valid)

What problem - unique to rural economy?

Lack of CONCLUSIVE (legally valid) Ownership Rights

(i.e) More of PRESUMPTIVE TITLE (Societally valid but not legally).

Problem?

Might encourage grabbing of land by influential persons.

> Different blocks → Diff. soil fertility

✓ Good implementation:

PUNJAB; HARYANA; W. UP

Link to GR: Consolidation was precondition to GR. So states which did consolidation earlier benefitted from GR.

But, they too went for consolidation w/o solving the problem of CONCLUSIVE ownership rights. → Small owners & landless complain of loosing land in consolidation.

* This land reform is MORE NEEDED NOW that then. Consolidation

× Bcos, the avg. size of land holding is getting smaller & smaller

× In absence of this reforms, many farmers are giving up Agriculture itself → Problem to food security.

Ceiling & Consolidation may appear contradictory but actually not:

Both talk about 2 extremes:

Ceiling — Very Big → But ceiling is politically impossible.

Consolidation — Very Small. 65% not even 1 ha acre → Focus on this Now. [1 hacre = 2.47 acre]

Both Needed → $\boxed{\text{MIDDLE SIZED LAND PLOTS}}$ Need of the hour.

(5) Co-operative Farming:

Mea: Voluntary pooling of land by farmers & cultivating it together.

Rationale: Economies of scale → ↑ productivity

Diff. from Consolidation:

✓ No shift of ownership req. here → Problem of conclusive ownership overcome.

✓ Not legal but left to farmer's will.

↳ One reason why it didn't work.

So a better reform than Consolidation as per experts.

→ But, farmers need to TRUST each other +

→ Govt. need to play active role.

So, can go for mix of co-op & consolidation to solve problems in Agriculture.

II. Post-1991 / Modern or Market led Land Reforms

Sale & purchase of land ← Devt. of land Markets

Pre-1991 → not much demand for land other than agri. but
Post-1991 → Industrial growth demands more land. So the change.

① Modernisation of land Records:
↓
Scientific survey of land.
↓
Now: Digitization of Land Records
↳ More difficult to be altered & hence can be a solution to lack of conclusive rights.

Main goal: To benefit Industries & Infrastructure & not Agriculture.

For a farmer to sell land, conclusive rights are must.
But it would be good for Agriculture as well — as we could revisit some of our unfinished land Reforms like consolidation.

Ideally → Digitization must be taken up only after FAIR DISTRIBUTION OF LAND.

② Facilitating land leasing:
↓
Compulsory Registration → Land-owners — But they may prevent
→ Lease-holds (Tenants) them too

Why called reform? It will benefit land owners & lease-holds also.
Land owners — ownership rights become conclusive.
Lease holds — security of tenure (Tenancy reforms coming back)

Also, Urbanisation → Many land owners couldn't stay in village most of time making conclusive right problematic even more.

③ Land Acquisition for Public Purpose

$\underbrace{\text{Land Acquisition}}_{\text{Loosing land w/o will of owner}}$ for $\underbrace{\text{Public Purpose}}_{\text{For common welfare}}$

Loosing land w/o will of owner. For common welfare

Ex: NH, Airports, Roads (Infra)
Affordable housing;
Defence.

Why debate?

Those loosing out complain of having less benefits.

LOSERS

a) Land-losers

b) Project affected People

Job Loss | Settlement Loss (More in tribal areas)

Ideal: w/o affecting common welfare, we should try to ensure welfare for both losers too.

* LARR, 2013 [Right to fair Compensation & Transparency in Land Acquisition; Rehabilitation & Resettlement Act]

Issues of debate:

i) Consent Requirement → How much min. consent of project affected ppl is required for project.

2013: 80% for pvt. projects
70% for PPP
Separate act for Govt. project - not this.

5 Sectors * Land Acquisition Amendment Bill, 2015

a) Defence b) Rural Infra c) Affordable Housing d) Industl. Corridors e) Infra where UG owns land

These 5 sectors exempted from Consent requirement - 0%

× Infra developers complained of UPA about 80% consent. 2 extremes: 2 laws

× Industrial corridor → Dedicated Highway b/w 2 metropolitans.

× Infra - UG land → Most debatable

ii) Social Impact Assessment (SIA)

On project affected People | On Environment

2013 Act → SIA mandatory for all land acquisitions.

Criticism: For very small area of land it is not needed; only needed for large area → Justified criticisms

° SIA was to be cleared by a complex Bureaucratic chain. So gives rise to Corruption & Time taken & Costlier.

2015 Bill → 5 Sectors exempted from SIA requirement.

Going to extremity w/o addressing real problem.

iii) Max. of 5% of Irrigated Multi-cropped land can be acquired in a district. Best quality agri. land → Good for Agri.

Why Good provision?

✓ Any agri. land acquisition - permanent loss to agriculture

✓ For acquiring party - it hardly matters if agri land or not.

2015 Bill → They (5 sectors) can be excempted from Agri requirement on Case-by-Case basis.

↳ Main reason why bill is not passing.

→ Anti-agriculture.

iv) Compensation to land losers

2013 Act → Compensation upto 4 times MP (Rural India)
→ Upto 2 times MP (Urban India)

MP → ~~Act~~ registered value of land or land similar to it.

Highly underestimated MP.

The infra developers however get huge profits, y not share a little to these losers 1 time.

2015 Bill → Retained this provision.

v) Employment Guarantee for Project Affected People:

2013 Act → To all P.A.P. (Very difficult)

2015 Bill → To atleast 1 member of affected Farm HH.

Should've included all HHs, as non-farm HH also affected.

Since, bill couldn't pass, CG has given the ball to the SG to do as they wish → CO-OPERATIVE Federalism ☺

Problems with SG doing it:

i) If land acquisition is there across more than one state.

Gujarat: Has done it on lines of 2015 bill. } So will clash.
MH: Not done.

Hence, Land acquisition is the only part of land Reforms kept by constitution in Concurrent List. So, centre can't desert its role completely.

ii) Relatively -ve impact on Agrarian States

The competition b/w states may not be desirable always.

Ex: Due to competition, if Guj (Indust. state) is being copied by M.P (Agri. state) then all loss is for Agriculture.

Food Security & Agriculture Price Policy

"Food Security is about 3 things:
a) Physical access to food grains ↳ Availability
b) Economic access ↳ Affordability
c) Social access ↳ w/o any social discrimination"

– FAO

Agri. price policy is govt's price policy with 2 objectives:
> Remunerative price to farmers – MSP ← ensures physical access; usually > MP
> Affordable price for Consumers – CIP (PDS) ← ensures economic access; usually < MP

Centre Issue Price: Price at which centre sells foodgrains to states
↳ Lower than Market price

Interlinkages:

✓ Both have mostly similar goals.

Food Security Framework

Production (Farmers) → Procured at MSP by FCI (W & R only) → Stored in FCI godowns → Grains sold to states at CIP → PDS outlets → Distributed to consumers at ISSUE PRICES (IP)

Only – MSP – CIP (PDS)

IP = CIP Only centre subsidy
IP < CIP state + centre subsidy

Food Security Subsidy :

Total subsidy given by centre on achieving Food security goal.

$$\underbrace{(MSP - \overset{WP}{\overset{\uparrow}{MP}})}_{\text{subs. to farmers}} + \begin{pmatrix}\text{Transport +} \\ \text{storage +} \\ \text{Handling +} \\ \text{wages etc..} \\ \text{costs}\end{pmatrix} + \underbrace{(\overset{RP}{\overset{\uparrow}{MP}} - CIP)}_{\text{subs. to Consumers}}$$

On simplification : $\underbrace{MSP + \text{other costs}}_{\text{Economic cost of Food grains}} + (-CIP)$

Here we see only on wheat, Rice & pulses

MSP & PROCUREMENT POLICY

> CACP (Commission on Agri Costs & Prices) - calculates MSP

> Based on Cost of Production (A2+FL)

> Only gives recommendation - final say with govt.

Pre-1997 : Actual MSP (Govt.) = Recommended MSP (CACP)

Post-1997 : Actual MSP > Recommended NSP

wheat & Rice

Why? Pressure of politically stronger SGs with coalition culture strengthening

→ Open procurement Policy by FCI : FCI must buy any amount of grains brought by farmers (FCI can deny only when quality is not good otherwise must buy - W & R - only mostly)

–ve impacts of MSP↑

i) Higher Food subsidy burden
   (with 1 Rs. MSP↑, subsidy burden 2 Rs.↑ – due to extra other costs)

ii) Higher Food Inflation
   (Due to ↓ availability of f.grains in open market)

iii) Distorted Cropping Pattern
   (Farmers cultivate geo. unsuitable crops. Ex: R in punjab)

iv) Wastage of Food grains
   (↑MSP + Open procurement + lack of storage capacity with FCI)

v) Lower Agriculture Exports
   (Our prices ↑ than competing countries
   Ex: Rice, sugar, etc.)

PILLARS OF REFORM

MSP – Procurement – Storage

vi)* Poor Targeting – Serious Problem

Benefits of MSP → Few states
→ Large Farmers

Why?

Economic – legally FCI can't deny but it has limited storage & has a target. So going to few states & collecting from large farmers is – economically more efficient – time, cost, etc. – Defeats the very purpose of MSP

Historic – MSP & Proc. Policy is pre-condition to GR bcos only then MP wouldn't crash due to ↑ production due to GR. Hence GR states only primarily got these benefits too as FCI too went to them only.

So, it is time to take MSP benefits to other states also. Though politically tough, reforms are needed for welfare of F & security.

REFORMS IN MSP

① Higher MSP for other crops → Pulses / → Oil Seeds

- ✓ Logical reforms for level playing field for farmers
- ✓ Good for Nutrition security – ↑ production of pulses
- ✓ Potential to reduce import of edible oil – ↑ produc. of oil seeds

② Need for Better & Adequate Procurement* of grains.

(Inadequate procurement → Middlemen exploit farmers
+ ↑MSP) @ price <<< MP – loss for farmers

Worse than no ↑ in MSP

③ Decentralised Procurement

Procurement by states – TN, Chatt, M.P, GR states

- ✓ ↓ transportation costs
- ✓ Better storage
- ✓ Unique: Procurement for NUTRITION security & acc to. food habits of population.

Chatt – 1st state to give pulses in PDS

④ FCI Reforms {Shanta Kumar Committee}

> Procurement reforms – decentralisation fav^d

↳ Future role of FCI must be on states with not much evolved decentralisation – E. UP; BH; ASS; WB – Also, these are the states with potential for 2nd GR

> Storage Related Reforms – Improve storage capacity

↳ Improve efficiency of present storage facilities

Ex: Nature of gunny bags, etc. minor but good

↳ Additional Storage Infra – Pvt. sector or atleast PPP

⑤ Price Deficiency Payments (PDP)

Direct subsidy → (MSP-MP) → Deposited in Bank a/c of farmers

✓ No need for procurement, storage... — ↓ burden

✓ WTO compliant – Direct subsidy is preferred by WTO over MSP.

Challenge:

? If no procurement, then how PDS.
 So PDP is sensible only for crops not req. in PDS.

? For any direct subsidy
 Fin. inclusion; Aadhaar; clear land Records
 (conclusive land ownership)

> MP-pioneer in PDP
> Bhavantar Bhugtan Yojana - 1st PDP scheme
> (for pulses mainly)

OTHER DIRECT INCOME SUPPORT TO FARMERS

① Rythu Bandhu Scheme → Rs. 8000/acre/year – × Not for tenants & landless
 To replace input subsidies gradually
 Very successful scheme - economically & politically

② KALIA Scheme → Benefits all - Small & Marginal farmers, tenants, sharecroppers, landless.

③ PM-KISAN → Rs. 6000/year to small & Marginal farmers

Pre-Requisites
- Financial Inclusion
- Spread of Aadhaar + Infra for biometrics
- Conclusive Land ownership records

⇒ Such policies are better if state specific dep. on scenarios.

PDS

Pre-1997 → Universal PDS (i.e) Higher coverage

Post-1997 → Targeted PDS

BPL HHs | APL HHs

Subsidised Food grains — Lower CIP

Food grains at Economic cost — Higher CIP

Poor quality grains despite FCI procu. g. quality

G. quality grains sold at HP & replaced by poor grains.

Hope was to ↓ subsidy burden.

× But, actually it backfired & Subsidy ↑

why? > Gradual withdrawal of APL HHs from TPDS due to no real subsidy & also poor quality → Higher storage costs → ↑ Subsidy
(Also this is also the time of ↑ MSP)

× Lower average CIP, as APL HHs didn't pay for it.

>2001, Antyodaya Anna Yojana - very cheap grains to poorest of poor
Hence even ↓ CIP

2013, NATIONAL FOOD SECURITY ACT - NFSA

* 1st time legal Right to Food.

→ Even here TPDS, but this is different:

Priority HHs | Antyodaya HHs

$\underbrace{\text{Priority HHs} \quad \text{Antyodaya HHs}}_{\text{Eligible HHs}}$

75% of Rural pop. | 50% of urban pop.

$\underbrace{\text{75\% of Rural pop.} \quad \text{50\% of urban pop.}}_{\text{67\% of total population}}$

67% of total population → Higher coverage ≈ Seems like pre-1997 PDS

→ Very low CIP : Earlier ½ of Economic cost.

Now: Rs. 3 / ~~2~~ / 1 per kg
(Rice / wheat / coarse grain)

Higher coverage argument

Why Justified? ✓

i) May not necessarily ↑ Food Subsidy cost.

Lower storage cost + ↓ wastage of grains due to poor infra

The debate should never be on food subsidy only but also food security.

ii) Less Exclusion Errors* – error of excluding deserving ppl.

> In matters of food security, inclusion error is sometimes ok than exclusion errors excluding really starving people.

> Also, no alternate purpose for food grains than f. security.

iii) Most successful states in PDS → Universal PDS → less leakages

TN
- Only state which never had TPDS
- Right from beginning

Chattisgarh
- 2012 - State Act - Universal PDS
- Before 2013 - NFSA
- In last decade

Lower CIP argument

Why not Justified?

→ ↑ in f. subsidy – Lower CIP for APL HHs also.

→ ↑ in PDS leakages – Due to significant diff b/w MP & CIP.

So we need to have little higher CIP with more coverage