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GENERAL STUDIES

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ECONOMIC GROWTH AND DEVELOPMENT

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Economics: An Introduction

Definition

Economics as a word comes from the Greek : oikos means 'family, household, or estate', and nomos stands for 'custom, law' etc. Thus, "household management" or management of scarce resources is the essential meaning of economics. Economic logic is applied to any problem that involves choice under scarcity.

Take for example, land. It is a scarce resource. India has 15% of global population but only 2.4% of the global land. Thus there is huge pressure on land. It is needed for agriculture (food and non-food); manufacturing; residential purposes and so on. There should be rational and judicious use of land for which economics can help to make public policy. The challenges associated with land use are being grappled with presently , for instance in the Land Acquisition and Rehabilitation and Resettlement Act 2013 where the land claims of farmers, industry and other sections are addressed.

Apportion - share out

Similarly, water is scarce and is becoming even more so. There are demands for agricultural, industrial, domestic and other uses. How to apportion the existing amount of water among all these users is a public policy challenge being considered by the **Draft National Water Policy (NWP, 2012). Similar is the purpose of the food security law and land acquisition law.**

Broadly, economics is a social science that studies human activity aimed at satisfying needs and wants.It encompasses production, distribution, trade and consumption of goods and services

Initially, economics focused on "wealth" and later "welfare". That is, initially, it did not deter economists from advocating maximum production regardless of who benefited from it and how much misery it produced. Later, by the late 19th century, there was hue and cry about children being made to overwork and receive paltry payment for their work, to give one example. Then welfare became the focus of the descipline.

As a policy science, economics is always confronted with trade offs as scarcity of resources is the basis of the discipline. Trade offs involve making choices in policy making wherein there is a compromise on one goal to achieve another goal. It is a way of balancing among desirable goals. Presently, the policy of Reserve Bank of India aims at moderating inflation that it is the overriding objective of its monetary policy, even as some growth is eroded in the process. Thus, a bit of growth is traded off for price stability. Similarly, government wants to give subsidies to the poor and weak. It may mean more borrowings and thus some fiscal excess but poverty is addressed and thus political stability. Thus, fiscal prudence may be traded off to some extent in pursuit of welfare. The current state of public finance is an accurate description of this dilemma with fiscal deficit targeted at 4.8% of GDP(2013-14). In the land acquisition law, compensation for the land owners is increased to balance the interests of the industrialists and the farmers and others. Investment may moderate in the process, but social justice gets addressed.

The focus on tradeoffs arises from the scarce resources that make it necessary to choose between competing alternatives. Choosing one benefit implies forgoing another alternative to a greater or lesser extent. Thus, there is an opportunity cost to the available resources and there is a continuous process of weighing alternatives and balancing them (opportunity cost is the cost of foregoing an opportunity while choosing another).

Adam Smith, generally regarded as the Father of Economics, author of An Inquiry into the Nature and Causes of the Wealth of Nations (generally known as The Wealth of Nations) defines economics as "The science of wealth." Smith also offered another definition, "The Science relating to the laws of production, distribution and exchange."

Relegate - place in a lower rank or position

Definitions in terms of wealth emphasize production and consumption, and do not deal with the economic activities of those not significantly involved in these two processes ,for example, children and old people. The belief is that non-productive activity is a cost on society. It meant that man was relegated to the secondary position and wealth was placed above life. In democratic times, it is not acceptable. There was a demand to balance wealth creation with focus on social and human welfare. Thus arose the shift in the focus to welfare economics- study of man and of human welfare, not of money and goods alone. Economics since then involved study of social action connected with the attainment of human well being.

Beyond, wealth, welfare and trade offs, there has been an intense search in the discipline for right foci- sustainable development, green economy, well being, national happiness and so on.

Economics is usually divided into two main branches:

Microeconomics, which examines the economic behavior of individual actors such as consumers, businesses, households etc to understand how decisions are made in the face of scarcity and what effects they have on larger economy.

Macroeconomics, on the other hand, studies the economy as a whole and its features like national income, employment , poverty, balance of payments and inflation.

The two are linked closely as the behavoir or a firm or consumer or household depends upon the state of the national and global economy and vice versa.

'Mesoeconomics' studies the intermediate level of economic organization in between the micro and the macro economics like institutional arrangements etc. Meso is relative. Study of a sector of economics like auto, infrastructure may be considered mesoeconomics while the study of each unit may fall under micro.

DIVISION OF ECONOMICS	FOCUS
Microeconomics	Production/output in individual industries and businesses and consumer and behavior, How much steel, How much office space, How many cars, Consumer behaviour
Macroeconomics	National production/output, Gross domestic product, employment, Poverty, Inflation, BOP

There are broadly the following approaches in the mainstream economics, the basis of all the streams being the same the same: resources are scarce while wants are unlimited(often mentioned as the economic problem)

- Keynesian macroeconomics based on the theories of twentieth-century British economist John Maynard Keynes. It says that the state can stimulate economic growth and restore stability in the economy through expansionary policies. For example through massive programme of spending on infrastructure when the demand is low and growth rate is falling. In the recessionary phase that the economies of the western world in particular and rest of the world in general are going through due to 2008 financial crisis, the relevance of Keynes is growing. The intervention by State is only when the economic cycle turns down and growth slows down or is negative. In normal times, it is the market that drives growth through the force of supply and demand though the respective roles of State and market are coming under critical scrutiny post-Lehman. Indian government stepped up expenditure with fiscal and monetary stimuli in the 2008-10 period to withstand the recessionary winds from the west. With growth spurting, the gradual and calibrated exit from the stimulus was begun in the 2010-11 Union Budget. The theories of Keynesian economics were first presented in The General Theory of Employment, Interest and Money(1936).
- **Political economy** was the original term used for studying production, buying and selling, and their relations with law, custom, and government, as well as with the distribution of national income and wealth. *Political economy* originated in moral philosophy. It was developed in the 18th century as the study of the economies of states, or *polities*, hence the term *political* economy. Today, *political economy* may refer to examining how political forces affect the choice of economic policies, especially as to distributional conflicts and political institutions. *Political economy* most commonly refers to interdisciplinary studies drawing upon economics, law, and political science in explaining how political institutions, the political environment, and the economic system—capitalist, socialist, or mixed—influence each other.
- Neoliberalism refers to advocacy of policies such as individual liberty, free markets, and free trade. Neoliberalism "proposes that human well-being can best be advanced by liberating individual entrepreneurial freedoms and skills within an institutional framework characterized by strong private property rights, free markets and free trade".With the communist model of economic management through state ownership of economy failing by the mid-1980s and industrial democracies registering a history victory over it with their free market model, market forces returned as the winning format for economic success. It is the return of the liberalism of the Adam Smith era and is refered to as neo-liberalsim in its present form since mid-1980s. India's economic reforms are largely centred around it. The expression of neoliberalism is used by some as leaving too much role to the market forces and can be detrimental to genuine human and sustainable growth.

Don't use this term

- In distinction to the above, there is the school of socialist economics based on public (State) ownership of means of production to achieve greater equality and give the workers greater control of the means of production. It comes in many forms- Nehruvian socialism where there is public and private sector coexisting and complementing called mixed economy. It may also establish fully centrally planned economy which is also called command economy- economy is at the command of the State. Private ownership of assets is not allowed. For example, erstwhile USSR,

Industrial democracy - Democracy having free markets

Cuba etc. The latter (no private property, total economy being owned by the state etc) is known as communist model.

- Development economics is a branch of economics which deals with not only promoting economic growth and structural change but also improving the well being of the population as a whole through focus on health and education and workplace conditions, whether through public or private channels. Its thrust is mainly on low i come countries. The most prominent contemporary development economists are Nobel laureates Amartya Sen and Joseph Stiglitz.

Structural change of an economy refers to a long-term and broad based change of the fundamental structure, rather than microscale or short-term change. For example, a subsistence economy is transformed into commercial economy or a regulated mixed economy is liberalized. An insulated and protectionist economy becomes open and globalized. India has been structurally reorienting its economy since the early 1990s under which there is more room for markets; privatization of the public sector; greater flow of foreign investment and foreign goods etc.

Green economics focuses on and supports the harmonious interaction between humans and nature and attempts to reconcile the two. It is refered by many names like sustainable development, green economy (Rio Plus 20, 2012)

Economic growth

Economic growth is the change- increase or decrease, in the value of goods and services produced by an economy. If it is positive, it means an increase in the output andthe income of a country. It is generally shown as the increase in percentage terms of real gross domestic product(GDP adjusted to inflation) or real GDP.

Measuring Growth

Measures of national income and output are used in economics to estimate the value of goods and services produced in an economy. Common measures are Gross National Product (GNP) and Gross Domestic Product (GDP).

National income accounting

National income accounting refers to a set of rules and techniques that are used to measure the output of a country. It is used almost synonymously with GDP.

GDP is defined as the total market value of all final goods and services produced within the country in a given period of time- usually a calendar year or financial year or a fraction like quarter.

GDP can be real or nominal. Nominal GDP refers to the current year production of final goods and services valued at current year prices. Real GDP refers to the current year production of goods and service valued at base year prices. Base year prices are constant prices.

In estimating GDP, only final marketable goods and services are considered. When it is compared to the base year figure, the real growth levels are seen.

To explain further, gains from resale are excluded but the services provided by the agents are counted. That is, when a used car or house is sold, no new goods are being produced. But the

eg:- By resaling house nothing is generated except agent is providing his service. So only gains to an agent is added

fault to someone

real estate or the auto agent makes some money though commission which adds to the service economy. Similarly, transfer payments (pensions, scholarships etc) are excluded as there is income received but no good or service produced in return.

However, not all goods and services from productive activities enter into market transactions. Hence, imputations are made for these non-marketed but productive activities : for example, imputed rental for owner-occupied housing.

The value of intermediate goods is a part of the final goods and services and so are not counted separately as it amounts to double counting and exaggerates the value of the output.

Market Price and Factor Cost

Market price refers to the actual transacted price and it includes indirect taxes- custom duty, excise duty, sales tax , service tax etc.

Factor cost refers to the actual cost of the various factors of production and it includes government grants and subsidies but it excludes indirect taxes.

10kg seed = 100 FC
subsidy = 100 - 90 = 10Rs
∴ Market price = 90
∴ FC = 100
GDP at FC = 100 or
GDP at MP = 90
GDP at FC = GDP at MP + subsidy
∴ GDP FC = 90 + 10 = 100

(100 is part of FC, MP + subsidy = FC)

Relationship between market price and factor cost

GNP at factor cost = GNP at market price – indirect taxes + subsidies
GDP at factor cost = GDP at market price – indirect taxes + subsidies

Factor costs

Factor costs are the actual production costs at which goods and services are produced by the firms and industries in an economy. They are really the costs of all the factors of production such as land, labor , capital, energy, raw materials like steel etc that are used to produce a given quantity of output in an economy. They are also called factor gate costs (farm gate, firm gate and factory gate) since all the costs that are incurred to produce a given quantity of goods and services take place behind the factory gate ie within the walls of the firms, plants etc in an economy.

Transfer Payments

Transfer payment refers to payments made by government to individuals for which there no economic activity is produced in return by these individuals. Examples of transfer are scholarship, pension.

Estimating GDP/GNP

Three approaches

There are three different ways of calculating GDP. The expenditure approach adds consumption, investment, government expenditure and net exports (exports minus imports). On the other hand, the income approach adds what factors earn: wages, profits, rents etc. Output approach adds the market value of final goods and services .The three methods must yield the same results because the total expenditures on goods and services (GNE) must by definition be equal to the value of the goods and services produced (GNP) which must be equal to the total income paid to the factors that produced these goods and services.

In reality, there will be minor differences in the results obtained from the various methods due to changes in inventory levels. This is because goods in inventory have been produced (and therefore included in GDP), but not yet sold. Similar timing issues can also cause a slight discrepancy between the value of goods produced (GDP) and the payments to the

factors that produced the goods, particularly if inputs are purchased on credit.Inventory is a detailed list of all the items in stock

Final goods are goods that are ultimately consumed rather than used in the production of another good. For example, a car sold to a consumer is a final good; the components such as tyres sold to the car manufacturer are not; they are intermediate goods used to make the final goods. The same tyres, if sold to a consumer, would be a final goods. Only final goods are included when measuring national income. If intermediate goods were included too, this would lead to double counting; for example, the value of tyres would be counted once when they are sold to the car manufacturer, and again when the car is sold to the consumer.

Only newly produced goods are counted. Transactions in existing goods, such as second-hand cars, are not included, as these do not involve the production of new goods.(mentioned earlier)

GDP considers only marketed goods. If a cleaner is hired, his pay is included in GDP. If one does the work himself, it does not add to the GDP. Thus, much of the work done by women at home- taking care of the children, aged; chores etc which is called `care economy' is outside the GDP. Even what the elder sibling teaches the younger one is outside the scope of national accounts.

Gross means depreciation (wear and tear of machinery in their use) of capital stock is not subtracted. If depreciation is subtracted, it becomes net domestic product.

Calculating the real GDP growth -inflation adjusted GDP growth-allows us to determine if production increased or decreased, regardless of changes in the inflation and purchasing power of the currency.

Output expressed as GDP at factor cost at constant prices makes more genuine sense as inflation/deflation is factored out and the distortions of subsidies and indirect taxes are also deducted. Thus, quantitative levels of production changes are expressed.

The data from the current prices is adjusted to the constant prices by using deflators- it helps take out the contribution of inflation to the value of the output. Errors can occur in the process of deflating the figure based on which deflator is used. GDP data for the first quarter of 2010-11 was miscalculated because the price deflator was wrongly used. For GDP by output and expenditure figures, two different deflators were used and the shrinkage went wrong. For one figure, CPI was used as deflator and for the other GDP figure, WPI was used.

GDP and GNP

Factors of Production

The two are related. The difference is that GNP includes net foreign income- what foreigners produce in the country is subtracted from what Indians produce aborad or vice versa. That is meant by net foreign income. GNP adds net foreign income compared to GDP. GDP shows how much is produced within the boundaries of the country by both the citizens and the foreigners. GDP focuses on where the output is produced rather than who produced it- it is a geographical concept. GDP measures all domestic production, disregarding the producing entities' nationalities.

In contrast, GNP is a measure of the value of the output produced by the "nationals" of a country- both within the geographical boundaries and outside. That is , all the output that the Indian citizens produce in a given year – both within India and all other countries makes up

the GNP of India. For example, there are Indian and foreign firms operating in India. Together what they produce within the Indian geography is the GDP of India. The profits of foreign firms earned within India are included in India's GDP , but not in India's GNP.

In other words, income is counted as part of GNP according to who owns the factors of production rather than where the production takes place. For example, in the case of a German-owned car factory operating in the US, the profits from the factory would be counted as part of German GNP rather than US GNP because the capital used in production (the factory, machinery, etc.) is German owned. The wages of the American workers would be part of US GDP, while the wages of any German workers on the site would be part of German GNP.

GDP is essentially about where production takes place. GNP is about who produces. If it is an open economy with great levels of foreign investment (FDI) and lesser levels of outbound FDI, its GDP is likely to be larger than GNP.

If it is an open economy but more of its nationals tend to move economic activity abroad or earn more from investing abroad compared with non-nationals doing business and earning incomes within its borders, its GNP will be larger than GDP.

If it is a closed economy where nobody leaves its shores, nobody invests abroad, nobody comes in and nobody invests in the country, its GDP will be equal to GNP.

Japan used to belong in the last category. Until the mid-1990s, the difference between Japan's GDP and GNP amounted to less than one percentage point of GDP. With only limited numbers of people doing business abroad, the GDP and GNP were essentially the same thing.

Presently, Japan's GNP tends to be around 2 percentage points larger than its GDP. Japanese economy is globalised with Japanese investment in China, USA, Europe etc. In stark contrast to the Japanese case, there are other nations where the difference between GDP and GNP is not only large, but inverted as well. That is to say, GDP is larger than GNP. Ireland is a case in point. That country's GDP has tended over recent years to eclipse its GNP by as much as 20 percent.

This is typical of a very small and very open economy. When such a country manages to attract a lot of foreign direct investment, domestic economic activity expands quite quickly. But the earnings from all that economic activity, if they are sent home by the companies in question, may not leave the country richer at all.

Analysts tend to say that GDP is a better measure than GNP, and that now seems to have been accepted by all the major industrial countries. The reason is that GDP is domestic production where employment is created; inflation is modeated; tax revenues are more and so on. GNP also has its advantages and India is a big beneficiary of it- remittances from aborad; acquisition of foreign companies; invest abroad to tap on foreign opportunities etc. But the consensus is that former is of greater value than the latter.

There are other related concepts too.

Gross National Product and Net National Product

We have seen GDP and GNP above.

Net National Product

In the production process a country uses machines and equipment. When there is depreciation, we have to repair or replace the machinery. The expenses incurred for this are called the depreciation expenditure. Net National Product is calculated by deducting depreciation expense from gross national product.

NNP = GNP - Depreciation

National Income is calculated by deducting indirect taxes from Net National Product and adding subsidies. National Income (NI) is the NNP at factor cost.

NI = NNP - Indirect Taxes + Subsidies

Per Capita Income is per capita GDP: GDP divided by mid year population of the corresponding year. Similarly, per capita GNP can also be calculated.

The growth of GDP at constant price shows an annual real growth.

The real GDP per capita of an economy is often used as an indicator of the average standard of living of individuals in that country, and economic growth is therefore often seen as indicating an increase in the average standard of living.

Base year

For examining the performance of the economy in real terms through the measurement of Gross Domestic Product (GDP), national income, consumption expenditure, capital formation etc., estimates are prepared at the prices of selected year known as base year. Base year is a specific year from which the economic growth is measured .It is allocated the value of 100 in an index. The estimates at the prevailing prices of the current year are termed as "at current prices", while those prepared at base year prices are termed "at constant prices". The comparison of the two estimates gives the measure of real growth. It means the production of the current year is valued at base year prices so that the real growth is worked out by deducting the impact of inflation or deflation. That is, the increase in the value of the GDP due to inflation is excluded and the 'real increase' is found out.

The base year of the national accounts is changed periodically to take into account the structural changes which take place in the economy and to depict a true picture of the economic growth.

The first official estimates of national income were prepared by the Central Statistical Office (CSO) with base year 1948-49 for the estimates at constant prices. These estimates were published in the publication, "Estimates of National Income" in 1956. With the gradual improvement in the availability of basic data over the years, a comprehensive review of methodology for national accounts statistics has constantly been undertaken with a view to updating the database and shifting the base year to a more recent year. As a result, base years of the National Accounts Statistics series have been shifted from 1948-49 to 2004-05 which is the new series of national accounts being followed from 2010.

Normally, when the base year of national accounts statistics is changed, there is some change in the levels of GDP estimates. This happens due to widening the coverage.

A base year has to be a normal year without large fluctuations in production, trade and prices of commodities in general. Reliable price data should be available for it. It should be as recent as possible. The National Statistical Commission wants that the base year should be revised every five years.

GDP deflator

GDP Deflator is a comprehensive measure of inflation, implicitly derived from national accounts data as a ratio of GDP at current prices to constant prices. It encompasses the entire spectrum of domestic economic activities including services, it is available on a quarterly basis with a lag of two months since 1996. Given the delay involved in obtaining the GDP deflator, national income aggregates extensively use WPI for deflating nominal price estimates to derive real price estimates.

Unlike some price indexes, the GDP deflator is not based on a fixed basket of goods and services. It covers the whole economy.

National Account statistics

The Central Statistical Office (CSO) in the Ministry of Statistics and Programme Implementation (MoSP&I) is responsible for the compilation of NAS. At the State level, State Directorates of Economics and Statistics (DESs) have the responsibility of compiling there State Domestic Product and other aggregates.

The statistics that are released by the CSO and the State DESs relate to various macro-economic aggregates of the Indian economy. The aggregates compiled and released (at current and constant prices) at annual periodicity by the CSO include gross and net domestic product by economic activity, consumption, saving, capital formation and capital stock, public sector transactions and dis-aggregated statements, as well as the consolidated accounts of the nation namely like Gross Domestic Product. The CSO also releases the quarterly GDP estimates.

The CSO revises the base year of the NAS series periodically. The CSO releases the current series of NAS with 2004-05 as Base Year. The first estimates for a reference year are released by the CSO, about two months before the close of the year, in the form of Advance Estimates (AE) of National Income. These estimates present at both current and constant prices and at factor cost, the Gross National Product (GNP), Net National Product (NNP), Gross Domestic Product (GDP), Net Domestic Product (NDP), and Per Capita Income. These estimates are subsequently revised and released as updates of advance estimates. Quick Estimates of NAS and the Revised Estimates of the earlier years are released by the CSO utilising the available data of various sectors provided by the statistical system, in the month of January or February of the following year (with a 10-month lag). Along with the Quick Estimates for the previous financial year, estimates for the earlier years are also revised using the detailed data supplied by various source agencies and final figures released.

The need to measure economic growth

The following aims can be attributed to the study of economic growth

- when growth is quantified , we can understand whether it is adequate or not for the given goals of the economy
- we can understand its potential and accordingly set targets
- we can adjust growth rates for their sustainability
- we can prevent inflation or deflation to some extent if we see the performance of the economy in quantitative terms
- we can balance the contributions of the three sectors of the economy and steer the direction of growth towards national goals- away from agriculture to manufacturing as in the case of India in recent years
- target appropriate levels of employment creation and poverty alleviation
- forecast tax revenues for governmental objectives
- corporates can plan their business investments

Problems in calculating National Income

The measurement of national income encounters many problems. The problem of double-counting has already been noted. Though there are some corrective measures, it is difficult to eliminate double-counting altogether. And there are many such problems and the following are some of them.

Black Money

Illegal activities like smuggling and unreported incomes due to tax evasion and corruption are outside the GDP estimates. Thus, parallel economy poses a serious hurdle to accurate GDP estimates. GDP does not take into account the 'parallel economy' as the transactions of black money are not registered.

Non-Monetization

In most of the rural economy, considerable portion of transactions occurs informally and they are called as non-monetized economy- the barter economy. The presence of such non-monetary economy in developing countries keeps the GDP estimates at lower level than the actual.

Household Services

The national income accounts do not include the 'care economy'- domestic work and housekeeping. Most of such valuable work rendered by our women at home does not enter our national accounting.

Social Services

It ignores voluntary and charitable work as it is unpaid.

Environmental Cost

National income estimation does not account for the environmental costs incurred in the production of goods. For example, the land and water degradation accompanying the Green revolution in India. Similarly, the climate change that is caused by the use of fossil fuels. However, in recent years, green GDP is being calculated where the environmental costs are deducted from the GDP value and the Green GDP is arrived at.

Intangible

Vague & abstract

Business cycles

Alternating periods of expansion and decline in economic activity is called business cycle. That is,the ups and downs of the economy. There are four stages in the business cycle: expansion, growth, slowdown and recession. Recession may not follow every time. When recession takes place, it may not be of the same intensity every time. For example, the 2008 global financial meltdown is the deepest since the WW2 and is called the Great Recession. If recession deepens, it is called depression and occurred only once in the last century in 1930's. All economies experience economic cycles. Explaining and preventing these fluctuations is one of the main focuses of macroeconomics.

Recession may end with the corrective measures taken by the government and the market. One such measure is stimulus. If it does not end and relapses for any reason, due to external or internal shocks, it is called double dip recession.In 2012, UK is in double dip recession. When recession worsens, with de-growth becoming stubborn and deeper and more and more people lose jobs, it is called depression- statistical markers may differ. Greece in 2012 is in depression with 50% of the young people out of work.

Economic Growth: Its benefits and side effects

The first benefit of economic growth is wealth creation. It helps create jobs and increase incomes. It ensures an increase in the standard of living, even if it is not evenly distributed. Government has more tax revenues: fiscal dividend. Economic growth boosts tax revenues and provides the government with extra money to finance spending projects. For example, the flagship programmes of the government like the NREGA are a direct result of the tax buoyancy of growth the country experienced since 2003 till 2011. It sets up the positive spiral:rising demand encourages investment in new capital machinery which helps accelerate economic growth and t create more employment.

Economic growth can also have a self-defeating effect: violate the principles of fairness and equity thus setting off social conflicts. Environmental costs are another risk.

Reliability of GDP as a measure of progress

Economic growth is generally taken as the measure of advancement in the standard of living of the country. Countries with higher GDP often score highly on measures of welfare, such as life expectancy. However, there are limitations to the usefulness of GDP as a measure of welfare:

- GDP does not value intangibles like leisure, quality of life etc. Quality of life is determined by many other things than economic goods.
- the impact of economic activity on the environment may be harmful-pollution, climate change, unsustainable growth, ecological refugees, life style diseases etc
- It only gives average figures that hide stratification. Economic inequality is not revealed by GDP figures
- Condition of poor is not indicated For example, Indian economy grew at 8.4% in 2010-2011 but the food inflation was over 14% causing immesirization of the lower classes
- Gender disparities are not indicated
- It does not matter how the increase in wealth takes place- whether by civilian demand or war
- GDP does not measure the sustainability of growth. A country may achieve a temporarily high GDP by over-exploiting natural resources

The major advantages to using GDP per capita as an indicator of standard of living are that it is measured frequently, widely and consistently. Frequently in that most countries provide information on GDP on a quarterly basis, which allows a user to spot trends more quickly. Widely in that some measure of GDP is available for practically every country in the world, which allows crude comparisons between the standard of living in different countries. And consistently in that the technical definitions used within GDP are relatively consistent between countries, and so there can be confidence that the same thing is being measured in each country.

The major disadvantage of using GDP as an indicator of standard of living is that it is not, strictly speaking, a measure of standard of living.. For instance, in an extreme example, a country which exported 100 per cent of its production would still have a high GDP, but a very poor standard of living.

The argument in favour of using GDP is not that it is a good indicator of standard of living, but rather that (all other things being equal) standard of living tends to increase when GDP per capita increases. This makes GDP a proxy for standard of living, rather than a direct measure of it.

Because of the limitations in the GDP concept, other measures of welfare such as the Human Development Index (HDI), Index of Sustainable Economic Welfare (ISEW), Genuine Progress Indicator (GPI) and Sustainable National Income (SNI), Gross National Happiness(GNH), Green GDP, natural resource accounting have been suggested.

They are proposed in an attempt to give a more complete picture of the level of well-being and the position with reference to natural resource depletion, but there is no consensus as to which is a better measure than GDP. Some of the above defy quantification. GDP still remains by far the most often-used measure.

Alternatives to GDP

Some economists have attempted to create a replacements for GDP which attempt to address many of the above criticisms regarding GDP. Other nations such as Bhutan have advocated gross national happiness as a standard of living, claiming itself as the world's happiest nation.(Read ahead for Recent advances in the concept)

HDI

The UN Human Development Index (HDI) is a standard means of measuring well-being. The index was developed in 1990 by the Pakistani economist Mahbub ul Haq, and has been used since 1993 by the United Nations Development Programme in its annual report.

The HDI measures the average achievements in a country in three basic dimensions of human development:

- A long and healthy life, as measured by life expectancy at birth.
- Knowledge, as measured by the adult literacy rate (with two-thirds weight) and the combined primary, secondary, and tertiary gross enrolment ratio (with one-third weight).
- A decent standard of living, as measured by gross domestic product (GDP) per capita at purchasing power parity (PPP) in US Dollars.

Each year, UN member states are listed and ranked according to these measures.
India ranks at 134 among 187 countries in terms of the human development index (HDI) in 2011. It is placed in the "medium" category.India's ranking in 2010 was 119 out of 169 countries.

The HDI goes beyond a nation's gross domestic product (GDP) to measure the general well-being of people under a host of parameters, such as poverty levels, literacy and gender-related issues.

The 2010 Human Development Report came up for the first time with an Inequality-adjusted Human Development Index (IHDI), which factors in inequalities in the three basic dimensions of human development (income, life expectancy, and education).

HPI

An alternative measure, focusing on the amount of poverty in a country, is the Human Poverty Index.The Human Poverty Index is an indication of the standard of living in a country, developed by the United Nations.
Indicators used are:

- Life span
- functional literacy skills
- Long-term unemployment
- Relative poverty (poverty with reference to the average per capita income)

GPI

The Genuine Progress Indicator (GPI) is a concept in green economics and welfare economics that has been suggested as a replacement metric for gross domestic product (GDP) to measure economic growth. Unlike GDP it is claimed by its advocates to more reliably distinguish uneconomic growth - harmful economic growth under which inequalities pile up and environmental damage is huge.

A GPI is an attempt to measure whether or not a country's growth, increased production of goods, and expanding services have actually resulted in the improvement of the welfare (or well-being) of the people in the country.

GNH

Gross National Happiness (GNH) is an attempt to define quality of life in more holistic and psychological terms than Gross National Product.

The term was coined by Bhutan's former King Jigme Singye Wangchuck in 1972 to indicate his commitment to building an economy that would serve Bhutan's unique culture based on Buddhist spiritual values. While conventional development models stress economic growth as the ultimate objective, the concept of GNH is based on the premise that true development takes place when material and spiritual development occur side by side to complement and reinforce each other. The four dimensions of GNH are the promotion of equitable and sustainable socio-economic development, preservation and promotion of cultural values, conservation of the natural environment, and establishment of good governance.

Natural Resources Accounting and Green GDP

Natural resources are essential for production and consumption, maintenance of life-support systems, as well as having intrinsic value in existence for intergenerational and other reasons.

It can be argued that natural capital should be treated in a similar manner to man-made capital in accounting terms, so that the ability to generate income in the future is sustained by using the stock of natural capital judiciously. By failing to account for reductions in the stock of natural resources, standard measures of national income do not represent economic growth genuinely. Soil, water and biodiversity are the three basic natural resources.

National Biodiversity Action Plan published by Government of India, Ministry of Environment and Forests in 2008 highlights as an action point the valuation of goods and services provided by biodiversity. More specifically, the Action Plan states: to assign appropriate market value to the goods and services provided by various ecosystems and strive to incorporate these costs into national accounting.

In the Nagoya (Japan) meet in 2010 on biodiversity protection, India declared that it will adopt natural resource accounting. The 2010 UN biodiversity summit decided to respect the link between economic policy, natural capital and human wellbeing. There should be global partnership is to mainstream natural resources accounting into economic planning. India, Colombia and Mexico accepted it. This will plug deficiencies in traditional accounting systems. As mentioned above, India's national biodiversity action plan has already incorporated some of these concepts.

Green GDP

Green Gross Domestic Product (Green GDP) is an index of economic growth with the environmental consequences of that growth factored in. From the final value of goods and services produced, the cost of ecological degradation is deducted to arrive at Green GDP.
In 2004, Wen Jiabao, the Chinese premier, announced that the green GDP index would replace the Chinese GDP index. But the effort was dropped in 2007 as green GDP figures shrank the size of the GDP to unimpressive levels.

India and green accounting

India aims to factor the use of natural resources in its economic growth estimates by 2015 -to make "green accounting" part of government policy on economic growth.

The green GDP estimates account for the consumption of natural resources as well. This would help find out how much of a natural resource is being consumed in the course of economic growth, how much being degraded and how much being replenished.

In the calculation of Green GDP, there are methodological concerns about how to monetize the loss of biodiversity; how to measure the economic impacts of climate change due to green house gas emissions etc.

Sarkozy's Alternative metric

The Commission on the measurement of economic performance and social progress was set up in 2008 on French government's initiative.

Increasing concerns have been raised since a long time about the adequacy of current measures of economic performance, in particular those based on GDP figures. Moreover, there are broader concerns about the relevance of these figures as measures of social well-being, as well as measures of economic, environmental, and social sustainability.

Reflecting these concerns, President Sarkozy decided to establish this Commission, to look at the entire range of issues. Its aim is to identify the limits of GDP as an indicator of economic performance and social progress, to consider additional information required for the production of a more relevant picture etc. The Commission is chaired by Professor Joseph E. Stiglitz. Amartya Sen and Bina Agarwal are also associated with it. The commission gave its report in 2009.

The Stiglitz report recommends that economic indicators should stress well-being instead of production, and for non-market activities, such as domestic and charity work, to be taken into account. Indexes should integrate complex realities, such as crime, the environment and the efficiency of the health system, as well as income inequality. The report brings examples, such as traffic jams, to show that more production doesn't necessarily correspond with greater well-being.

Stiglitz explains: The big question concerns whether GDP provides a good measure of living standards. In many cases, GDP statistics seem to suggest that the economy is doing far better than most citizens' own perceptions. Moreover, the focus on GDP creates conflicts: political leaders are told to maximise it, but citizens also demand that attention be paid to enhancing security, reducing air, water, and noise pollution, and so forth – all of which might lower GDP growth. The fact that GDP may be a poor measure of well-being, or even of market activity, has, of course, long been recognized.

More recent developments
Details, discussion and dictation in the class

Moral economy

"Moral economy" is a name given in economics, sociology and anthropology to the interplay between cultural mores and economic activity. It describes the various ways in which custom and social pressure coerce economic actors in a society to conform to traditional norms even at the expense of profit. It is also an economy in which the stake holders like workers expect respect and dignity along with salary and working conditions- the latter not being all, the former being quite important as well. If moral economy breaks down, industrial unrest may result.

Laissez-faire
A market economy is an economic system in which goods and services are traded, with the price being determined by demand and supply.

Laissez-faire is a French phrase meaning "let do, let go, let pass." Its proponents make arguments against government interference with economy and trade. It is synonymous with free market economics .It is generally understood to be a doctrine opposing economic interventionism by the state beyond the extent which is perceived to be necessary to maintain peace and property rights.

Supporters of a market economy generally hold that the pursuit of self-interest is actually in the best interest of society. Adam Smith says:

"By pursuing his own interest [an individual] frequently promotes that of the society more effectually than when he really intends to promote it." (Wealth of Nations)

Adam Smith calls it the invisible hand- the force that combines the individual self interest into a collective social interest. However, as we have seen in the melt down of the western economies since 2008 and as Nobel laureate Joseph Stiglitz commented, invisible hand may not exist. That is why it is invisible!
There are a variety of critics of market as an organizing principle of an economy. These critics range from those who reject markets entirely, in favor of a planned economy, such as that advocated by communism to those who wish to see them regulated to various degrees. One prominent practical objection is the environmental pollution generated. Another is the claim that through the creation of monopolies, markets sow the seeds of their own destruction. Still another, since 2008, is the excessive speculation and financialization of the market and its crash.

Social market
Some proponents of market economies believe that government should intervene to prevent market failure while preserving the general character of a market economy.

It seeks an alternative economic system other than socialism and laissez-faire economy, combining private enterprise with measures of the state to establish fair competition, low inflation, low levels of unemployment, good working conditions, and social welfare.

Market economy and poverty
Free market economists argue that the only way to solve poverty is by creating new wealth. According to them, planned economies and welfare will not solve poverty problems but only make them worse. Low levels of government regulation and interference, free trade, and tax reform are the way to achieve growth. Open economy, competition and innovation generate growth and employment.

Advocates of the third way -social market solutions to poverty- believe that there is a legitimate role the government can play in fighting poverty. They believe this can be achieved through the creation of social safety nets such as social security and workers compensation.

Most modern industrialized nations today are not typically representative of Laissez-faire principles, as they usually involve significant amounts of government intervention in the economy. This intervention includes minimum wages to increase the standard of living, anti-monopoly regulation to prevent monopolies, progressive income taxes, welfare programs to provide a safety net for those without the capacity to find work ,disability assistance, subsidy programs for businesses and agricultural products to stabilize prices - protect jobs within a country, government ownership of some industry, regulation of market competition to ensure fair standards and practices to protect the consumer and worker, and economic trade barriers in the form of protective tariffs - quotas on imports - or internal regulation favoring domestic industry.

Market and Government failure
The inability of an unregulated market to achieve allocative efficiency is known as market failure. The main types of market failure are: monopoly, steep inequality, pollution etc. The western economic recession since 2008 is the result of market failure where excessive speculation and borrowings have disoriented the economies with huge human and economic cost.

Exemplary – Be or give a typical example of

Government failure is the public sector analogy to market failure and occurs when government does not efficiently allocate goods and/or resources consumers. Just as with market failures, there are many different kinds of government failures. Inefficient use of resources, wastage and retarded economic growth due to government monopolies and regulation are the results of government failure. Often, the performance of the public sector in India is cited to exemplify government failure. The sickness of Air India resulting from its mismanagement is an example of government failure.

Structural composition of the economy

The three-sector hypothesis is an economic theory which divides economies into three sectors of activity: extraction of raw materials (primary), manufacturing (secondary), and services (tertiary).

According to the theory, the main focus of an economy's activity shifts from the primary, through the secondary and finally to the tertiary sector. The increase in quality of life, social security, growth of education and culture and avoidance of unemployment with reduction of poverty are the effects of such transition.

Countries with a low per capita income are in an early state of development; the main part of their national income is achieved through production in the primary sector. Countries in a more advanced state of development, with a medium national income, generate their income mostly in the secondary sector. In highly developed countries with a high income, the tertiary sector dominates the total output of the economy.

The primary sector of the economy involves changing natural resources into primary products. Most products from this sector are considered raw materials for other industries. Major businesses in this sector include agriculture, fishing, forestry and all mining and quarrying industries.

Primary sector is a larger sector in developing countries; for instance, animal husbandry is more common in Africa than in Japan.

The secondary sector of the economy includes those economic sectors that create a finished, usable product: manufacturing and construction.

This sector generally takes the output of the primary sector and manufactures finished goods or where they are suitable for use by other businesses, for export, or sale to domestic consumers. This sector is often divided into light industry and heavy industry.

Light industry is usually less capital intensive than heavy industry, and is more consumer-oriented than business-oriented (i.e., most light industry products are produced for end users rather than as intermediates for use by other industries).Examples of light industries include the manufacture of clothes, shoes, furniture and household items (e.g. consumer electronics). Heavy industry means: traditional production **industries** in the auto, steel, rubber, petroleum, and similar areas, requiring high capitalization and producing large quantities. Some more examples are heavy machinery, big factories, chemical plants, production of construction equipment such as cranes and bulldozers.

The tertiary sector of economy (also known as the service sector) is defined by exclusion of the two other sectors. Services are defined in conventional economic literature as "intangible

or invisible goods". The tertiary sector of economy involves the provision of services to businesses as well as final consumers. Services may involve the transport, distribution and sale of goods from producer to a consumer as may happen in wholesaling and retailing, or may involve the provision of a service, such as or entertainment. The service sector consists of the "soft" parts of the economy such as insurance, government, tourism, banking, retail, education, and social services. Examples of service may include retail, insurance, and government.

The quaternary sector of the economy is an extension of the three-sector hypothesis. It principally concerns the intellectual services: information generation, information sharing, consultation and research and development. It is sometimes incorporated into the tertiary sector but many argue that intellectual services are distinct enough to warrant a separate sector. The quaternary sector can be seen as the sector in which companies invest in order to ensure further expansion. Research will be directed into cutting costs, tapping into markets, producing innovative ideas, new production methods and methods of manufacture, amongst others. To many industries, such as the pharmaceutical industry, the sector is the most valuable because it creates future branded products which the company will profit from. This sector evolves in well developed countries and requires a highly educated workforce.

The quinary sector of the economy is the sector suggested by some economists as comprising health, education, culture, police, fire service, and other government industries not intended to make a profit. The quinary sector also includes domestic activities such as those performed by stay-at-home parents or homemakers. These activities are not measured by monetary amounts but make a considerable contribution to the economy.

Some terms

A developing country is a country that has not reached the Western-style standards of democratic governments, free market economies, industrialization, social programs, and human rights guarantees for their citizens.

Countries with more advanced economies than other developing nations, but which have not yet fully demonstrated the signs of a developed country, are grouped under the term newly industrialized countries.

Development entails a modern infrastructure (both physical and institutional), and a move away from low value added sectors such as agriculture and natural resource extraction. Developed countries, in comparison, usually have economic systems based on economic growth in the secondary, tertiary and quaternary sectors and high standards of living.
The category of newly industrialized country (NIC) is a socioeconomic classification applied to several countries around the world.

NICs are countries whose economies have not yet reached first world status but have, in a macroeconomic sense, outpaced their developing counterparts. Another characterization of NICs is that of nations who were till a decade or so back had regulated economies but are open now and are undergoing rapid economic growth. Incipient or ongoing industrialization is an important indicator of a NIC. In many NICs, social upheaval can occur as primarily rural, agricultural populations migrate to the cities, where the growth of manufacturing concerns and factories can draw many thousands of laborers.

NICs usually share some other common features, including:

- A switch from agricultural to industrial economies, especially in the manufacturing sector.
- An increasingly open-market economy, allowing free trade with other nations in the world.
- Emerging MNCs
- Strong capital investment from foreign countries.

A **high-income economy** is defined by the World Bank as a country with a per capita income of US$12,476 or more in 2011. While the term "high income" may be used interchangeably with "First World" and "developed country," the technical definitions of these terms differ. The term "first world" commonly refers to those prosperous market economies like the west, Japan etc.

According to the United Nations, for example, some high income countries may also be developing countries. The GCC (Persian Gulf States) countries, for example, are classified as developing high income countries. Thus, a high income country may be classified as either developed or developing. GCC countries for example are rich but not developed. They have pockets of export economy based on oil and gas and the rest of the economy is under developed.

The term developed country, or advanced country, is used to categorize countries that have achieved a high level of industrialization in which the tertiary and quaternary sectors of industry dominate. Countries not fitting this definition may be referred to as developing countries.

This level of economic development usually translates into a high income per capita and a high Human Development Index (HDI) rating. Countries with high gross domestic product (GDP) per capita often fit the above description of a developed economy. However, anomalies exist when determining "developed" status by the factor GDP per capita alone.
Second world was the communist countries with command economies but they do not exist today.

Third world was made up of the developing countries.
Least Developed Countries (LDCs or Fourth World countries) are countries which according to the United Nations exhibit the lowest indicators of socioeconomic development, with the lowest Human Development Index ratings of all countries in the world. A country is classified as a Least Developed Country if it meets three criteria based on:

- low-income (three-year average per capita income of less than US $905, which must exceed $1,086 to leave the list(2013-14)
- human resource weakness (based on indicators of nutrition, health, education and adult literacy) and
- economic vulnerability (based on instability of agricultural production, instability of exports of goods and services and the percentage of population displaced by natural disasters)
-

The classification currently applies to 48 countries.

Vital Statistics

The per capita income of Indians for the first time crossed the Rs 50,000-mark in 2010-11, although using current prices as the barometer. The per capita income at current prices during 2012-13 is estimated to be Rs 68,747 as compared to Rs 61,564 during 2011-12, showing a rise of 11.7 per cent, according to the CSO.

The huge figure is seen to be illusionary as economists prefer to use factor cost at constant prices to weed out the impact of inflation. It is not a great milestone to celebrate. It may be the other way as inflation actually hurt the poor and the low income groups rather than cushioning them as the higher figure shows.

Growth and the value of output

National income of India in terms of Gross Domestic Product (GDP) is composed of contributions made by three sectors namely, primary sector, secondary sector and tertiary sector. The primary sector consists of agriculture, forestry, fishing, mining and quarrying. Secondary sector includes manufacturing, construction and electricity, gas and water supply, while the tertiary sector comprises of trade, transport etc, finance & real estate, community and personnel services.

In terms of growth of the economy, sharp fall in Indian currency against the US dollar and slower economic growth have caused India's GDP for Fiscal Year 2012-13 to shrink in US $ terms to $1.84 trillion from $1.87 trillion a year earlier.

The Indian economy grew at its slowest pace in four years at 4.4% in the first quarter (Q1, or April-June) of the current fiscal year 2013-14, compared with 4.8% during the preceding quarter (January-March) of the last fiscal.

Seen from another, less reliable, yardstick of gross domestic product (GDP) at market prices, India actually grew at 2.4%.

While agriculture grew 2.7% in the first quarter, mining and manufacturing contracted 2.8% and 1.2%, respectively. Electricity grew 3.7% and construction 2.8% during the quarter.

In services, only community, social and personal services—representing government expenditure—grew faster in the first quarter at 9.4%, compared with 8.9% during the same quarter a year ago.

Trade and hotels grew at a meagre 3.9%, while financing, insurance and business services grew at a robust 8.9% in the fiscal first quarter.

The Central Statistics Office (CSO) data shows GDP growth at market price was only 2.4% against GDP growth at factor cost of 4.4% for the first quarter. GDP at market price is calculated by adding indirect taxes to GDP at factor cost while subtracting subsidies, as discussed above.

The lower GDP at market price compared to GDP at factor cost is because the subsidy component is growing extremely fast and the government is borrowing to fund subsidy.

SOCIO-ECONOMIC PLANNING

Planned economy is one in which the state owns(partly or wholly) and directs the economy. While such a role is assumed by the State in almost every economy, in planned economies, it is pronounced: for example in communist and socialist countries- former USSR and China till the 1970's. In such a case a planned economy is refered to as command economy or centrally planned economy or command and control economy. In command economies, state does the following

- Control all major sectors of the economy
- Legislate on their use and about the distribution of income
- State decides on what should be produced and how much ; sold at what price
- Private property is not allowed

In a market economy, it is the opposite- state has a minimal role in the management of the economy- production, consumption and distribution decisions are predominantly left to the market. State plays certain role in redistribution. State is called the laissez faire state here. It is a French phrase literally meaning "Let do."

Indicative plan(see ahead) is one where there is a mixed economy with State and market playing significant roles to achieve targets for growth that they together set. It is operated under a planned economy but not command economy.

The difference between planned economy and command economy is that in the former there may be mixed economy and while in the latter Government owns and regulates economy to near monopolistic limit.

Command economies were set up in China and USSR, mainly for rapid economic growth and social and economic justice but have been dismantled in the last two decades as they do not create wealth sustainably and are not conducive for innovation and efficiency. Cuba and North Korea are still command economies.

History of Economic Planning in India: The beginnings

India being devastated economically after more than 2 centuries of colonial exploitation resulting in chronic poverty, eradication of poverty was the driving force for the formulation of various models of growth before Independence.

In 1944 leading businessmen and industrialists (including Sir Purshotamdas Thakurdas, JRD Tata, GD Birla and others) put forward " *A Plan of Economic Development for India*" - popularly known as the 'Bombay Plan'.It saw India's future progress based on further expansion of the textile and consumer industries already flourishing in cities like Bombay and Ahmedabad. It saw an important role the State in post-Independent India: to provide infrastructure, invest in basic industries like steel, and protect Indian industry from foreign competition.

Visionary engineer Sir Mokshagundam Visvesvarayya. pointed to the success of Japan and insisted that 'industries and trade do not grow of themselves, but have to be willed, planned and systematically developed' – in his book titled "*Planned Economy for India*"(1934) Expert economists and businessmen were to do the planning. The goal was poverty eradication through growth,

appalling – very bad

The Indian National Congress established a National Planning Committee under the chairmanship of Jawaharlal Nehru. It (1938) stated the objective of planning for development "was to ensure an adequate standard of living for the masses, in other words, to get rid of the appalling poverty of the people". It advocated heavy industries that were essential both to build other industries, and for Indian self-defence; heavy industries had to be in public ownership, for both redistributive and security purposes; redistribution of land away from the big landlords would eliminate rural poverty.

During the 1940's, the Indian Federation of Labour published its People's Plan by MN Roy that stressed on employment and wage goods. SN Agarwala, follower of Mahatma Gandhi published Gandhian Plan that emphasized on decentralization; agricultural development; employment; cottage industries etc.

Planning Goals

After Independence in 1947, India launched the five year plans for rapid growth. Planning has the following long term goals

- Growth
- Modernization
- self-reliance and
- social justice

Economic growth is the increase in value of the goods and services produced by an economy. It is conventionally measured as the percent rate of increase in real gross domestic product, or real GDP- real means adjusted to inflation. Growth measures quantitative increase in goods and services.

Economic development refers to growth that includes redistributive aspects and social justice. GDP shows growth and not welfare and human development aspects like education, access to basic amenities, environmental quality, freedom, or social justice. Economic growth is necessary for development but not sufficient.

Growth is expected to spread to all sections and regions; raise resources for the Government to spend on socio-economic priorities etc. It takes a long time for growth to trickle down to all people and regions. Therefore, State plans for an expeditious process of inclusive growth. Modernization is improvement in technology. It is driven by innovation and investment in R and D. Education is the foundation of modernization. The more modernized the economy, the greater the value created by it.

Self-reliance means relying on the resources of the country and not depending on other countries and the MNCs for investment and growth. India embarked on the goal partly due to the colonial experience and partly due to the goal of orienting growth to development and poverty eradication. Nehru-Mahalanobis model of growth that closed Indian economy and relied on basic industries is the main plank for self-reliance.

The term self-reliance should not be confused with self-sufficiency – the former means depending on resources of the country and avoid dependence on external flows; the latter means that the country has all the resources it needs. No country can be self-sufficient.
Social justice means inclusive and equitable growth where inequalities are not steep and benefits of growth reach all- rural-urban, man-woman; caste divide and inter-regional divides are reduced.

While the above four are the long term goals of the planning process, each five year plan has specific objectives and priorities.

Planning Commission

The Planning Commission was constituted in March, 1950 by a Resolution of the Government of India, and works under the overall guidance of the National Development Council. The Planning Commission consults the Central Ministries and the State Governments while formulating Five Year Plans and Annual Plans and also oversees their implementation. The Commission also functions as an advisory body at the apex level.

The 1950 resolution setting up the Planning Commission outlined its functions as to:

- Make an assessment of the material, capital and human resources of the country, including technical personnel, and investigate the possibilities of augmenting such of these resources as are found to be deficient in relation to the nation's requirement;
- Formulate a Plan for the most effective and balanced utilisation of country's resources;
- On a determination of priorities, define the stages in which the Plan should be carried out and propose the allocation of resources for the due completion of each stage;
- Indicate the factors which are tending to retard economic development, and determine the conditions which, in view of the current social and political situation, should be established for the successful execution of the Plan;
- Determine the nature of the machinery which will be necessary for securing the successful implementation of each stage of the Plan in all its aspects;
- Appraise from time to time the progress achieved in the execution of each stage of the Plan and recommend the adjustments of policy and measures that such appraisal may show to be necessary; and
- Make such interim or ancillary recommendations as appear to it to be appropriate either for facilitating the discharge of the duties assigned to it, or on a consideration of prevailing economic conditions, current policies, measures and development programmes or on an examination of such specific problems as may be referred to it for advice by Central or State Governments.

The Prime Minister is the ex officio Chairman of the Planning Commission. Deputy Chairperson enjoys the rank of a cabinet minister. A member of the Planning Commission enjoys the rank of a Minister of State in the Union Government. *Cabinet Ministers* with certain important portfolios act as part-time *members.*

The Deputy Chairman and the full time Members of the Planning Commission function as a composite body in the matter of detailed plan formulation. They provide advice and guidance to the subject Divisions of the Commission in the various exercises undertaken for the formulation of Approach to the Five Year Plans, and Annual Plans. Their expert guidance is also available to the subject Divisions for monitoring and evaluating the Plan programmes, projects and schemes.

The Planning Commission functions through several technical/subject Divisions. Each Division is headed by a Senior Officer designated as Pr. Adviser/Adviser/Addl. Adviser/Jt. Secretary/Jt. Adviser.

The various Divisions in the Commission fall under two broad categories:

- General Divisions which are concerned with aspects of the entire economy; and
- Subject Divisions which are concerned with specified fields of development.

The General Divisions functioning in the Planning Commission are:

- Development Policy Division,
- Financial Resources Division,
- International Economics Division,
- Labour, Employment and Manpower Division,
- Perspective Planning Division,
- Plan Coordination Division,
- Project Appraisal and Management Division,
- Socio-Economic Research Unit,
- State Plan Division, including Multi Level Planning, Border Area Development Programme, Hill Area Development and North Eastern Region (NER), and
- Statistics and Surveys Division,
- Monitoring Cell.

The Subject Divisions are:

- Agriculture Division,
- Backward Classes Division,
- Communication & Information Division,
- Education Division,
- Environment and Forests Division,
- Health & Family Welfare Division,
- Housing, Urban Development & Water Supply Division,
- Industry & Minerals Division,
- Irrigation & Command Area Development Division,
- Power & Energy Division (including Rural Energy, Non-Conventional Energy Sources and Energy Policy Cell)
- Rural Development Division,
- Science & Technology Division,
- Social Welfare & Nutrition Division,
- Transport Division,
- Village & Small Industries Division, and
- Western Ghats Secretariat.

The Programme Evaluation Organisation undertakes evaluation studies to assess the impact of selected Plan Programmes/ Schemes in order to provide useful feedback to planners and implementing agencies.

The Commission is a corner-stone of our federal structure, a think-tank ; helps to balance the priorities and expenditures of the Ministries of the Union Government ; throws up ideas on policies for structural and perspective changes ; and is a reservoir of research."

Relevance of Planning

There has been a national debate about the relevance of planning in the era of liberalization where the state controls and regulations are dismantled to a great extent and market forces are given larger role. The investment of the government for the five year plans is also on decline. The trend began in the 7th plan and strengthens into the Eleventh Plan.

It is true that the quantitative aspects of planning in terms of control over economy are being selectively phased out and the nature of planning process is undergoing a qualitative change. Planning is important for the following reasons in the era of liberalization

- In a federal democracy like ours, the principal task of planning is to evolve a shared vision among not only the federal units but also among other economic agents so that the efforts of all the actors become convergent towards the national priorities. the role of planning is to develop a common policy stance for center and states. Also, the task of federal policy coordination is central to Indian Planning. For example, the need to invite foreign investment in infrastructure areas like power need center – state coordination as the necessary legislation and administrative changes involve both.
- While the growth process can be made the responsibility of the corporate sector to a greater degree, its direction and distribution are to be steered by planned public intervention so that regional imbalances are reduced and socio economic inequities are set right. For example, directing the growth of the large industry into the backward areas and technology intensive areas to realize national goals.
- The nature of instruments available to planners in the implementation has changed. Quantitative controls have yielded place to qualitative ones .The planning process has to focus on the need for planning for policy.
- Planning at the grass roots level that is participatory is very crucial for improving the delivery systems and proper use of the resources. The role of the government is thus to facilitate participatory planning.
- Environmental priorities are a major concern of planning
- Planning is necessary for the sectors like energy, communication, transport and so on as private sector needs to be guided into the national plan.
- In the era of globalization where corporates are not expected to plan beyond the growth of a particular unit, the role of safeguarding national interest is that of planning by the State. For example , being subjected to various discriminative trade practices by EU, USA and so on, the Indian farmers, manufacturers and exporters have to fight sophisticated battles in the WTO for which the legal services and information and building up bargaining power are best provided by the State.

Thus, planning continues to be relevant and ever more so for the following reasons

- Federal cooperation and coordination
- Equitable growth
- Environment friendly development
- Defending national interest in the age of globalization
- Inter-sectoral balance in growth

Changing Role of Planning Commission

From a highly centralized planning system, the Indian economy is gradually moving onwards indicative planning where hard planning is no longer undertaken. The role of the Planning Commission accordingly changes. The Commission concerns itself with the building of a

long term strategic vision of the future and decide on priorities of nation. It works out sectoral targets and provides promotional stimulus to the economy to grow in the desired direction. Planning Commission plays an integrative role in evolving a national plan in critical areas of human and economic development. In the social sector, Planning Commission helps in schemes which require coordination and synergy like rural health, drinking water, rural energy needs, literacy and environment protection.

When planning in a vast federal country like India involves multiplicity of agencies, a high powered body like the PC can help in evolution of an integrated approach for better results at much lower costs.

In our transitional economy, Planning Commission attempts to play a systems change role and provide consultancy within the Government for developing better systems. It has to ensure smooth management of the change and help in creating a culture of high productivity and efficiency in the Government

In order to spread the gains of experience more widely, Planning Commission also plays an information dissemination role.

With the emergence of severe constraints on available budgetary resources, the resource allocation system between the States and Ministries of the Central Government is under strain. This requires the Planning Commission to play a mediatory and facilitating role, keeping in view the best interest of all concerned.

From Planning Commission to Systems Reforms Commission

There has been a significant change in the role of the PC since its inception in 1950. Initially for about 4 decades, due to centralized planning, resources were those of the Central government and the priorities and monitoring were also the works of the Central Government. It effectively meant the PC. Planning Commission had veto over every aspect – related to growth and socio-economic development- of the functioning of the Union Ministries and the State Governments: The manner of raising and utilising resources; specific allocations to particular schemes and programmes; location of enterprises; expansion and reduction of capacities; application of technologies; sources of supplies; modalities of implementation; priorities, phasing, pricing, targets and time-frames; nature of the instrumentalities; qualifications and strength of personnel of organisations; staff emoluments etc.

Since 1991, India adopted the indicative planning model , away from the kind of centralised planning on the Soviet model envisaged by Jawaharlal Nehru. Now Ministries and Departments, as well as the corporate entities in the private sector, enjoy a lot of functional, financial and operational autonomy.

States have more autonomy and corporates contribute more than half to planning resources. Thus, centre's role is on decline in quantitative and qualitative terms and thus that of the PC. In the era of liberalisation, the economic players should properly be left to decide for themselves what they consider to be the appropriate courses of action on the various issues coming up before them, whether they relate to policies, schemes or investments.
The government intends to convert the Planning Commission into a think-tank to generate original ideas in the very broad domain of economic policy for the government to then act on. It will also be the government agency responsible for acting as an interface with other

independent think-tanks and NGOs. The PM would like the commission to engage more directly with the "polity", with various ministries in the Central and state governments, and be able to persuade them to implement certain ideas or "plans" generated by the government's own think tank. That isn't radically different from its existing role — the Planning Commission has few direct powers of execution in any case and must rely on the power of persuasion to sell its ideas to the Centre and states.

Interestingly enough, the new role sought for the Planning Commission seems to be very similar to the role played by the National Advisory Council, which also generates ideas within, coordinates with NGOs and civil society and then tries to "persuade" the government to act. NAC's focus so far has been social sectors whereas a systems reforms commission can take on a broader gambit of issues, including public finances, infrastructure and so on.
The government's move to revamp and gradually transform the Planning Commission into a System Reforms Commission is a major step that can make the institution more relevant to a market economy. The idea is to metamorphose the plan panel from a reactive agency into a strategic thinking group, which maps out risks and opportunities by focusing on issues
The shrinking role of the government in mobilising and controlling investments has pushed the Planning Commission to focus more on issues related to enforcing fiscal discipline in the central and state governments, including in the various ministries, departments and public sector enterprises.

According to Arun Maira, PC member, the Planning Commission will gradually transform itself into a Systems Reforms Commission for resolving the systemic problems of the 21st Century over the next two-three years as desired by Prime Minister Manmohan Singh. It will restructure itself to serve three essential functions: build a larger network around its members with think tanks and opinion makers, produce thought papers at a faster pace and communicate more lucidly with polity.

National Development Council
The National Development Council is not a Constitutional body nor a statutory body (not set up by an Act of the Parliament). Union Cabinet set up the NDC in 1952 with the following functions

- To prescribe guidelines for the formulation of the national plan.
- To consider the national plans formulated by the Planning Commission.
- To assess the resources for the plan and recommend a strategy for mobilizing the resources.
- To consider important questions of socio-economic policy affecting development of the nation.
- To review the progress of the five year plan mid-course and suggest measures for achieving the original targets.

NDC is headed by the Prime Minister of India and comprising of all Union Cabinet Ministers, Chief Ministers of all the States and Administrators of Union Territories and Members of the Planning Commission .PC members are ex-officio members of the NDC.. Ministers of State with independent charge are also invited to the deliberations of the Council.

The National Development Council (NDC) has a special role in our federal polity.
It is the apex body for decision making and deliberations on development matters.

PC is apese advisory body

It has the explicit mandate to study and approve the Approach Plan to the Five year Plans and the Five Year Plan documents. The mid-term reviews of the Five year Plans are considered by the NDC. In fact, without the NDC approving, the Five Year Plan does not come into effect.

57th meeting of NDC was held in December 2012 to approve the 12th FYP.

The CMP of the UPA Government (2004) says that NDC will be activated. It will meet at least three times in a year and in different state capitals . It will be developed as an effective instrument of cooperative federalism.

Mixed economy

India is a mixed economy combining features of both capitalist market economies and socialist command economies. Thus, there is a regulated private sector (the regulations have decreased since liberalisation) and a public sector controlled almost entirely by the government. The public sector generally covers areas which are deemed too important; or not profitable enough for the private sector. Thus such services as railways and postal system are carried out by the government.

Since independence, various phases have seen nationalisation of such areas as banking, thus bringing them into the public sector, on one hand, and privatisation of some of the Public Sector Undertakings during the liberalisation period on the other

Financial resources for the Five year Plans

The resources for the Plan come from

- Central budget
- State budgets
- PSEs
- Domestic private sector and
- FDI

A Note on Gross Budgetary Support

Resources of the Centre consist of both budgetary resources including external assistance routed through the budget and the Internal & Extra Budgetary Resources (IEBR) of Central Public Sector Enterprises (CPSEs). The quantum of budgetary resources of the Centre which is available for providing overall budgetary support to the plan is divided into two parts viz. budgetary support for Central Plan (including U.Ts without Legislature) and Central Assistance for States' Plans (including U.Ts with Legislature). A part of the budgetary resources allocated as budgetary support for the Central Plan is used for providing necessary support to CPSEs.

GBS is the amount from the central Budget that goes to fund the plan investments during the plan period.

History of Planning

First Plan (1951- 56)(W/o NDC)

The First Plan stressed more on agriculture, in view of large scale import of foodgrains and inflationary pressures on the economy. Other areas of emphasis were power and transport. The annual average growth rate during the First Plan was estimated as 3.61% as against a

target of 2.1%. Renowned economist **KN Raj**, who died in 2010 was one of the main architects of India's **first five-year plan**.

Second Plan (1956-61)

With agricultural targets of previous plan achieved, major stress was on the establishment of heavy industries. Rate of investment was targeted to increase from 7% to 11%. The Plan achieved a more than targeted growth rate of 4.32%. This Plan envisaged to give a big push to the economy so that it enters the take off stage. It was based on Nehru-Mahalanobis model- self-reliance and basic-industry driven growth.

Third Plan (1961-66)

It tried to balance industry and agriculture. The aim of Third Plan was to establish a self sustaining economy. For the first time, India resorted to borrowing from IMF. Rupee was also devalued for the first time in 1966. India's conflict with Pakistan and repeated droughts also contributed in the failure of this Plan.

Annual Plans

As the Third Plan experienced difficulties on the external front (war with China in 1962 and Pakistan in 1965); and the economic troubles mounted on the domestic front- inflation, floods, forex crisis- the Fourth Plan could not be started from 1966. There were three annual plans till 1969. This period is called plan holiday- that is when five year plans are not implemented. The Annual Plans were: 1966-67, 1967-68 and 1968-69.

Fourth Plan (1969-74)

The main objective of this Plan was growth with stability. The Plan laid special emphasis on improving the condition of the under-privileged and weaker sections through provision of education and employment. Reducing the fluctuations in agricultural production was also a point of emphasis of this Plan. The Plan aimed at a target growth of 5.7% and the achievement against this was 3.21%.

Fifth Plan (1974-79)*

The main objective of the Plan was Growth for Social Justice. The targeted growth rate was 4.4% and we achieved 4.8%. It was cut short by the Janata Party that came to power in 1977.

Sixth Plan (1980-1985)*

Removal of poverty was the foremost objective of Sixth Plan. Another area of emphasis was infrastructure, which was to be strengthened for development of both industry and agriculture. The achieved growth rate of 5.7% was more than the targeted one.

Direct attack on poverty was the main stress of the Plan.

Seventh Plan (1985-90)*

This Plan stressed on rapid growth in food-grains production and increase in employment opportunities. The growth rate of 5.81% achieved in this Plan was more than the targeted one. The plan saw the beginnings of liberalization of Indian economy.

The 8th Plan could not start in 1990 due to economic crisis and political instability. There were two annual plans- plan holiday.

Eighth Plan (1992-1997)

This Plan was formulated keeping in view the process of economic reforms and restructuring of the economy. The main emphasis of this Plan were

- to stabilize the adverse balance of payment scenario sustainably
- improvement in trade and current account deficit
- Human development as main focus of planning.

It was indicative plan for the first time. The Plan was formulated in a way so as to manage the transition from a centrally planned economy to market led economy. The targeted annual average rate of growth of the economy during Eighth Plan was 5.6%. Against this, we achieved an average annual growth of 6.5%.

The Plan was based on Rao-Manmohan Singh model of liberalization.

Ninth Five Year Plan (1997-2002)

The salient features of the Ninth Five Year Plan are a target annual average growth rate of 6.5 per cent for the economy as a whole, and a growth rate of 3.9 per cent for agriculture sector, among others. The key strategies envisaged to realise this target rest on attaining a high investment rate of 28.2 per cent of GDP at market prices. The domestic saving rate, which determines the sustainable level of investment, is targeted at 26.1 per cent of the GDP. Care has been taken to ensure achievement of a sustainable growth path in terms of external indebtedness as well as fiscal stability. Rate of growth achieved was 5.4%

Tenth Plan

Tenth Plan (2002–2007) The main objectives of the tenth Five Year Plan of India were:

- Attain 8% GDP growth per year.
- Reduction of poverty rate by 5 percentage points by 2007.
- Providing gainful and high-quality employment at least to the addition to the labor force.
- Reduction in gender gaps in literacy and wage rates by at least 50% by 2007.

Eleventh Plan (2007-12)

'Towards Faster and More Inclusive Growth' is the central theme of the plan that seeks to lower poverty by 10%, generate 70 million new jobs, and reduce unemployment to less than 5% Rs 36.44 trillion Eleventh Five-Year Plan promises to accelerate economic growth and make it more inclusive. The chief thrust of the plan, that will run from 2007-08 to 2011-12, will be agriculture, education and infrastructure -- all areas that remain a concern in a rapidly growing economy.

As many as 27 detailed national targets have been set in the plan, ranging from enhancing incomes and reducing poverty, to education, literacy, health, infant mortality, maternal mortality and child development.

Achievements

GDP growth in the Eleventh Plan 2007–08 to 2011–12 was 7.9 per cent compared with 7.6 per cent in the Tenth Plan (2002–03 to 2006–07) and only 5.7 per cent in the Ninth Plan (1997–98 to 2001–02). The growth rate of 7.9 per cent in the Eleventh Plan period is one of the highest of any country in that period which saw two global crises.

Agricultural GDP growth accelerated in the Eleventh Plan, to an average rate of 3.7 per cent, compared with 2.4 per cent in the Tenth Plan, and 2.5 per cent in the Ninth Plan.

Rural real wages increased 6.8 per cent per year in the Eleventh Plan.
Net enrolment rate at the primary level rose to a near universal 98.3 per cent in 2009–10. Dropout rate (classes I–VIII) also showed improvements.

11th Five Year Plan (2007-2012) in detail

The eleventh plan has the following objectives:

1. **Income & Poverty**
   - Accelerate GDP growth from 8% to 10% and then maintain at 10% in the 12th Plan in order to double per capita income by 2016-17
   - *Rs.36,44,000 lakh crores ($910 billion) is the investment*
   - gross budgetary support (GBS) is Rs 14,21,711 crore, double of the last plan
   - Increase agricultural growth rate to 4% per year to ensure broad-based development
   - Create 70 million new work opportunities.
   - Reduce educated unemployment to below 5%.
   - Raise real wage rate of unskilled workers by 20 percent.
   - Reduce poverty by 10 percentage points
   - industrial and services sector growth to 9-11 per cent
   - investment rate to be at 36.7 per cent
2. **Education**
   - Reduce dropout rates of children from elementary school from 52.2% in 2003-04 to 20% by 2011-12
   - Develop minimum standards of educational attainment in elementary school, and by regular testing monitor effectiveness of education to ensure quality
   - Increase literacy rate for persons of age 7 years or more to 85%
   - Lower gender gap in literacy to 10 percentage points
3. **Health**
   - Reduce infant mortality rate to 28 and maternal mortality ratio to 1 per 1000 live births
   - Reduce Total Fertility Rate to 2.1
   - Provide clean drinking water for all by 2009 and ensure that there are no slip-backs
   - Reduce malnutrition among children of age group 0-3 to half its present level
   - Reduce anaemia among women and girls by 50% by the end of the plan
4. **Women and Children**
   - Raise the sex ratio for age group 0-6 to 935 by 2011-12 and to 950 by 2016-17
   - Ensure that at least 33 percent of the direct and indirect beneficiaries of all government schemes are women and girl children
   - Ensure that all children enjoy a safe childhood, without any compulsion to work

NDC - 1952 (by union cabinet)

5. **Infrastructure**
   - Ensure electricity connection to all villages and BPL households by 2009 and round-the-clock power.
   - Ensure all-weather road connection to all habitation with population 1000 and above (500 in hilly and tribal areas) by 2009, and ensure coverage of all significant habitation by 2015
   - Connect every village by telephone by November 2007 and provide broadband connectivity to all villages by 2012
   - Provide homestead sites to all by 2012 and step up the pace of house construction for rural poor to cover all the poor by 2016-17
6. **Environment**
   - Increase forest and tree cover by 5 percentage points.
   - Attain WHO standards of air quality in all major cities by 2011-12.
   - Treat all urban waste water by 2011-12 to clean river waters.
   - Increase energy efficiency by 20 percentage points by 2016-17.

12th FYP

12th Five-Year Plan (2012-17) aims to achieve annual average economic growth rate of 8 per cent, down from from 9 per cent envisaged earlier, in view of fragile global recovery.

During the 11th Plan (2007-12), India has recorded an average economic growth rate of 7.9 per cent. This, however, is lower than the 9 per cent targetted in 11th Plan.

12th Plan seeks to achieve 4 per cent agriculture sector growth during 2012-17. The growth target for manufacturing sector has been pegged at 10 per cent.

The total plan size has been estimated at Rs.47.7 lakh crore, 135 per cent more that for the 11th Plan (2007-12).

As regards to poverty alleviation, the Commission aims to bring down the poverty ratio by 10 per cent. At present, 30 per cent of the population is below poverty line.

Growth Performance in the Five Year Plans (per cent per annum)

	Target	Actual
1. First Plan (1951-56)	2.1	3.61
2. Second Plan (1956-61)	4.5	4.32
3. Third Plan (1961-66)	5.6	2.38
4. Fourth Plan (1969-74)	5.7	3.21
5. Fifth Plan (1974-79)	4.4	4.80
6. Sixth Plan (1980-85)	5.2	5.69
7. Seventh Plan (1985-90)	5.0	5.81
8. Eighth Plan (1992-97)	5.6	6.7
9. Ninth Plan (1997-2002)	6.5	5.35
10.Tenth Plan(2002-2007)	8%	7.8%
11. Eleventh Plan(2007-12)	9%	7.9%
12.Twelfth FYP	8%	5% in 2012-13

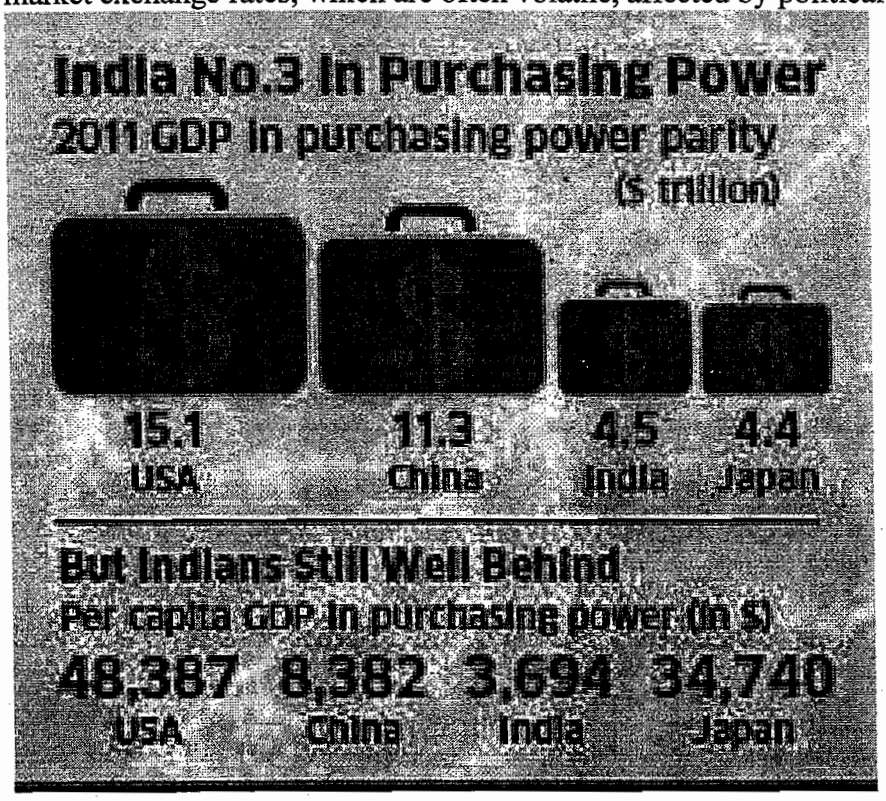
Achievements of Planning

In the last about 60 years since India became a Republic, the National Income has increased many times. Today, India is the third largest economy in Asia with about $1.84 trillion GDP after China and Japan; is the 9th largest economy in the world.

India overtook Japan to become the world's third-largest economy in purchasing power terms. Data released by the International Monetary Fund (IMF) shows that India's gross domestic product in purchasing power parity (PPP) terms stood at $4.46 trillion in 2011, marginally higher than Japan's $4.44 trillion, making it the third-biggest economy after the United States and China.

The PPP system allows GDP comparisons to be made by asking how much money would be needed to purchase the same goods and services in two countries and using that to calculate an implicit foreign exchange rate.

Under this method, a dollar should be able to buy the same amount of goods anywhere in the world and exchange rates should adjust accordingly. It nullifies distortions that come with market exchange rates, which are often volatile, affected by political and financial factors.



eg:- Big mac cost 4$ in USA & 100Rs in India
∴ 1 $ will can buy me $\frac{1}{4}$th of Big mac in India.

The Economist magazine's proprietary Big Mac Index, which takes the price of a McDonald burger across 120 countries to calculate the 'real' price of their currencies, is another crude way to measure PPP. India was included in the index recently. It showed that the Indian rupee was undervalued by 62% against the US dollar in 2012.

The PPP comparison is more useful while comparing the standards of living between countries. While the per capita GDP in PPP terms shows that India still has some distance to go to reach Japanese levels, "the difference is less than the comparison of per capita GDP in nominal dollar terms would indicate".

In the face of global recession, India remains the second fastest growing major economy after China.

Data released by the Planning Commission in July, 2013, suggested that poverty in India had declined from 37.2 percent in 2004-05 to 21.9 percent by 2011-12.

From 2004-05 to 2011-12 poverty fell by 2.24% annually as against 0.74% in the preceding 6 years. In absolute numbers the number of poor fell by 138 million during these seven years, an Indian and even a world record. Similar achievements by China are celebrated by the world.

Social indicators improved e though there is a long way to go- IMR, MMR, literacy, disease eradication etc. The industrial infrastructure is relatively strong – cement, steel ,fertilizers, chemicals, etc Agricultural growth is also gaining momentum with food grains production at 258 mt in 2012.

Forex reserves are $282 b (November 2013) which is a dramatic turnaround from 1991 when we had a billion dollars.

More than 2 lakh MW of power capacity is installed by 2013.
India has emerged as a back office of the world and its prowess in software is growing.
India ranks 11th worldwide in factory output (2013)
India ranks 10th worldwide in services' output.

There has been considerable expansion of higher education. At the time of Independence there were 20 universities and 591 colleges, while today, there are almost 500 universities and 21,000 colleges. Literacy levels are 75%(2010).

The failures of planning are equally clear

- Poverty still plagues about 250 million (Tendulkar)
- Inflation on CPI and food inflation are rising relentlessly hurting the poor- CPI is in double digits(above 10%) in September 2013.
- Unemployment is high
- Regional imbalances are intensifying
- Malnutrition haunts about half the children in India.

Indicative planning

With the launch of the economic reforms in 1991, indicative planning was inevitable. It was adopted since 8th five year plan (1992-97). It is characterized by an economy where the private sector is given a substantial role. State would turn its role into a facilitator from that of a controller and regulator.

It was decided that trade and industry would be increasingly freed from government control and that planning in India should become more and more indicative and supportive in nature. In other words, the remodeling of economic growth necessitated recasting the planning model from imperative and directive('hard') to indicative (soft) planning. Since the Government did not contribute the majority of the financial resources, it had to indicate the policy direction to the corporate sector and encourage them to contribute to plan targets. Government should create the right policy climate- predictable, irreversible and transparent-

to help the corporate sector contribute resources for the plan: fiscal, monetary, forex and other dimensions.

Indicative planning is to assist the private sector with information that is essential for its operations regarding priorities and plan targets. Here, the Government and the corporate sector are more or less equal partners and together are responsible for the accomplishment of planning goals. Government, unlike earlier, contributes less than 50% of the financial resources. Government provides the right type of policies and creates the right type of milieu for the private sector-including the foreign sector to contribute to the results.

Indicative planning gives the Government an opportunity to give the private sector encouragement to achieve growth in areas where the country has inherent strengths. It is known to have brought Japan results in shifting towards microelectronics. In France, too indicative planning was in vogue.

Planning Commission would work on building a long-term strategic vision of the future. The concentration would be on anticipating future trends and evolving strategies for competitive international standards. Planning will largely be indicative and the public sector would be gradually withdrawn from areas where no public purpose is served by its presence. The new approach to development will be based on "a re-examination and re-orientation of the role of the government". This point is particularly stressed in the development strategy of the Tenth Five Year Plan (2002-2007)

gaze at/think about

Indicative planning was not contemplated at the beginning of fifties as there was hardly any corporate sector in India and Government shouldered almost the entire responsibility of socio-economic planning.

Rolling Plan

It was adopted in India in 1962, in the aftermath of Chinese attack on India, in the Defence Ministry in India. Professor Gunnar Myrdal (author of famous book' Asian Drama') recommended it for developing countries in his book - Indian Economic Planning in Its Broader Setting.

Dovetail → Fit together easily or conveniently

In this type, every year three new plans are made and implemented- annual plan that includes annual budget ; five year plan that is changed every year in response to the economic demands; and perspective plan for 10 or 15 years into which the other two plans are dovetailed annually. Rolling plan becomes necessary in circumstances that are fluid.

Financial Planning

Here, physical targets are set in line with the available financial resources. Mobilization and setting expenditure pattern of financial resources is the focus in this type of planning.

Physical planning

Here, the output targets are prioritized with inter-sect oral balance. Having set output targets, the finances are raised.

Nehru-Mahalanobis Model of Economic Growth

Indian economy at the time of Independence was characterized by dependence on exports of primary commodities; negligible industrial base; unproductive agriculture etc. 1st FYP

focused on agriculture for food security. But industrialization was urgently needed to modernize the economy and improve its technology.

The turning point in India's planning strategy came with the second five-year (1956-61) plan. The model adopted for the plan is known as the Nehru-Mahalanobis strategy of development as it articulated by Jawahar Lal Nehru's vision and P.C.Mahalanobis was its chief architect. The central idea underlying this strategy is well conveyed by recalling the following statement from the plan document. 'If industrialization is to be rapid enough, the country must aim at developing basic industries and industries which make machines to make the machines needed for further development.'

The Mahalanobis model of growth is based on the predominance of the basic goods (capital goods or investment goods are goods that are used to make further goods; the goods that make up the industrial market like machines, tools, factories, etc). It is based on the premise that it would attract all round investment, ancillarisation, build townships and result in a higher rate of growth of output. That will boost employment generation, poverty alleviation, exports etc. The emphasis was on expanding the productive ability of the system, through forging strong industrial linkages, as rapidly as possible.

Other elements of the model are

- Import substitution. Protective barriers against foreign competition to enable Indian companies to develop domestically produced alternatives for imported goods and to reduce India's reliance on foreign capital.
- A sizeable public sector active in vital areas of the economy including atomic energy and rail transport.
- A vibrant small-scale sector driving consumer goods production for dispersed and equitable growth and producing entrepreneurs.

In terms of the core objective of stepping up the rate of growth of industrial production, the strategy paid off. Rate of growth of overall industrial production picked up . The strategy laid the foundation for a well-diversified industrial structure within a reasonably short period and this was a major achievement. It gave the base for self-reliance.

However, the strategy is criticized for the imbalances between the growth of the heavy industry sector and other spheres like agriculture and consumer goods etc that resulted. It is further criticized as it relied on 'trickle down effect'- benefits of growth will flow to all sections in course of time. This approach to eradication of poverty is slow and incremental. It is believed that frontal attack on poverty is required. Follow the debates about growth and redistribution-Sen-Bhagawati- argument that raged in 2013.

The criticism is one sided as in the given context, the Mahalanobis model was correct for growth and self-reliance.

Merit good → Subsidised (Edu in India)

Rao-Man Mohan Singh Model of Growth

The launching of economic reforms by the government in 1991 is driven by the Rao-Manmohan model - Mr. Narasimha Rao, the PM in 1991 and Finance Minister Dr. Man Mohan Singh. Its essence is contained in the New Industrial Policy 1991 and extends beyond it too. The model has the following contents

- Reorient the role of State in economic management. State should refocus on social and infrastructural development, primarily
- Dismantle, selectively controls and permits in order to permit private sector to invest liberally
- Open up the economy and create competition for PSEs- for better productivity and profitability
- External sector liberalization in order to integrate Indian economy with the global economy to benefit from the resource inflows and competition.

Plummet ↓ Fall steadily or rapidly

Its success is seen in the more than 6.5% average annual rate of growth of economy during the 8th Plan (1992-1997) . Forex reserves accumulated leaving the BOP crisis as history; poverty levels plummetted; and the foreign flows- FDI and FII increased.

Economic Reforms

Since July 1991, India has been taking up economic reforms to achieve higher rates of economic growth so that socio-economic problems like unemployment, poverty, shortage of essential goods and services, regional economic imbalances and so on can be successfully solved. The force behind the reforms is

- Indian economy reached a level of growth and strength to benefit from an open market economy.
- Private sector in India had come of age and was willing and capable of playing a major role
- Indian economy needed to integrate with the world with all the advantages like capital flows; technology; higher level of exports; state of art stock markets; Indian corporates can raise finances abroad and so on.

The country under the leadership of Dr. Manmohan Singh, Union Finance minister(1991-1996 and Prime Minister since 2004) converted the economic crisis – caused by , domestic cumulative problems of economy, political instability and gulf crisis-into an opportunity to initiate and institutionalise economic reforms to open up the economy. The deep crisis in 1991 could not be solved by superficial solutions. Therefore, structural reforms were taken up.

It was realized that by closing economy to global influences, the country was missing on technology developments and also gains from global trade. India needed exports, FDI and FII for stability on the balance of payments front and higher growth rates for social development. Worldwide, countries were embracing market model of growth, for example China, with proven results. So, India could make the historic shift from centralized planning to market-based model of growth.

Misgivings About Economic Reforms

Initially reforms were feared and resisted as there was scepticism and fear as the experience in Latin American countries in the 1980s was not a success in economic and social terms. The fears related to

- Inflation as there will be little left for domestic consumption as exports would be attractive
- Large scale unemployment due to capital intensity of growth process.
- Worsening of poverty as fiscal concerns will reduce social sector expenditure
- Flood of imports as customs duties will come down.
- food security will suffer as social sector expenditure will be reduced
- Pressures on labour sector due to domestic industry's inability to compete.

Some fears have indeed come true- jobless growth and uncertainty in farming. But by and large, reforms have done well.

Reforms mainly targeted the following areas:

- Dismantling the licence raj so that private sector and government were on a level playing field
- Drive public sector towards sustainable profitability and global play by dereservation; disinvestment; professionalization of management etc
- Fiscal reforms for stabile economic growth.
- Banking sector is deregulated and made to conform to stringent reforms for higher competitive strength and performance globally
- move towards free float of rupee and relaxation of controls on convertibility; aggressive export promotion; FDI and FII inflows etc.

Reforms were prioritized and sequenced in such a way as to make them sustainable and render further reforms feasible. For example, first generation reforms involved essentially non-legislative government initiatives- reduce SLR and CRR for the banking sector. Disinvestment of the PSEs. Deregulation of the rupee gradually and later make exchange rate of the rupee market-driven and so on. The second generation reforms involve legislative reforms and touch a wider section of the society- labour reforms; GST, FDI expansion etc. The former prepares the economy for the latter.

Above all, reforms with human face was the goal , unlike elsewhere in the world like in South America in the 1980's. It yielded results- the social effect of the reforms in India is seen in the flagsips schemes making an impact on health, education, social protection etc. The reforms gained consensus and showed positive results as can be seen below.

- Rates of growth went up
- BOP crisis has been solved in the first few years and today the country has about $ 282 b forex reserves(2013)
- Services sector (tertiary sector) has grown in importance and today contributes almost 57% of GDP(2013) emerging as a global player-India being the global back office.
- Exports have performed well and have recovered handsomely even while the world continues to be trapped in near recession conditions. It accounting for many jobs and quality Indian products
- Resilience of the economy in the face of Great Recession which is still not resolved
- Consumer choice has increased
- Tax-GDP ratio may have shrunk but the tax collections and base increased dramatically

- Nature of external debt has changed and the short term component is less
- Indian companies are listed on Nasdaq and New York Stock Exchange and raised billions of dollars for investment
- FIIs and FDI has picked up.
- Indian corporates have acquired global majors like Jaguar and *Anglo-Dutch steel* maker Corus; Bharati bought Zain's African telecom operations(2010)

While the above facts paint a positive picture of reforms, there are deficiencies as well

- poverty is a challenge and reforms with a human face is the need of the hour
- jobless growth is worrying the policy makers
- regional economic imbalances are intensifying
- While foodgrains production is at 258mtt(2012), there is still pressure on food security
- farmers are feeling directionless under the WTO regime
- Globalization threatens to destabilize agriculture with cheaper imports and questionable provisions related to intellectual property rights impacting negatively on availability of medicines etc.
- Infrastructure so far received inadequate attention except telecom ,roads and ports
- PSU reforms have not made progress and disinvestment and privatization are still to see substantial movement
- Globalization has exposed India to imported inflation due to commodity price rise- CPI has been almost invariably above the double digits since 2008(2013)

Second Generation Reforms

Having begun with the reforms in all the above sectors and seen the economy benefit from them , the second generation reforms were initiated by the end of 1990's. The reason for calling the latter set of reforms SGR is that they followed the initial reforms which laid the foundation for the reform process to deepen. It is a matter of sequencing in line with prioritization; economic preparation; consensus-building and so on. In fact, unless the success in material and human terms of the initial reforms was demonstrated, the next round of 'difficult' reforms would not be possible.

Second generation reforms- labour law flexibility, pension reforms based on employee contribution and the pension funds being deployed in the stock market; value added tax and GST; liberalized FDI including FDI in retail etc- touch on the lives of ordinary people and need successes in other sectors- first generation reforms- to make a convincing case. Otherwise, they may not be allowed by public opinion as we have seen in the case of FDI-MBR debate.

Second generation reforms are difficult as they are directly involved with the daily lives of people like

- User charges need to be rationalized to make these utilities viable but there are bound to be protests
- Man power rationalization in banks and PSUs through VRS faced resistance.
- Labour law flexibility will make TUs agitate.
- Interst rate cut, for example, for small savings will mean less returns for the middle class etc
- Agroreforms may mean small and marginal farmers' resistance

However, unless the SGRs are carried out, investment and growth will suffer with long term adverse consequences for poverty alleviation and employment generation. As the long term benefits of the reforms are bound to show in terms of higher growth rates and more social welfare, consensus needs to be built for successful legislation and implementation of SGRs.

Recession and depression

Recession

The standard definition of a recession is a decline in the Gross Domestic Product (GDP) – contraction in absolute quantity- for two or more consecutive quarters.

Depression

Before the Great Depression of the 1930s any downturn in economic activity was referred to as a depression. The term recession was developed in this period to differentiate periods like the 1930s from smaller economic declines that occurred earlier. This leads to the simple definition of a depression as a recession that lasts longer and has a larger decline in business activity.- more unemployment, deflation, negative growth.

How can we tell the difference between a recession and a depression A depression is any economic downturn where real GDP declines by more than 10 percent. A recession is an economic downturn that is less severe.

There is an old joke among economists: A recession is when your neighbour loses his job. A depression is when you lose your job.

Great Recession 2008-09

The late-2000s recession, more often called the Great Recession, was a severe economic recession that began in the United States in 2007 and ended in mid- 2009, according to the U.S. National Bureau of Economic Research (NBER). However, most people throughout the world consider it to be ongoing, because heightened degrees of unemployment and economic hardship remain a reality even today. The Great Recession has affected the entire world economy, with higher detriment in some countries than others. It is a global recession characterized by various systemic imbalances and was sparked by the outbreak of the financial crisis of 2007–2010.

The financial crisis is linked to reckless lending practices by financial institutions and the growing trend of securitization of real estate mortgages in the United States. The US mortgage-backed securities, which had risks that were hard to assess, were marketed around the world. When these securities lost value and were considered toxic, the financial institutions that bought them either went into heavy losses or went bankrupt fully. These companies being listed on the stock market, equities collapsed in their value as a result. Indian banks had negligible exposure to them.

A more broad based credit boom fed a global speculative bubble in real estate and equities, which served to reinforce the risky lending practices. The precarious financial situation was made more difficult by a sharp increase in oil and food prices. The emergence of Sub-prime loan losses in 2007 began the crisis and exposed other risky loans and over-inflated asset prices. With loan losses mounting and the fall of Lehman Brothers on September 15, 2008, a major panic broke out in the global financial transactions. As share and housing prices declined, many large and well established investment and commercial banks in the United States and Europe suffered huge losses and even faced bankruptcy, resulting in massive public financial assistance.

slump - a sudden fall

A global recession has resulted in a sharp drop in international trade, rising unemployment and slumping commodity prices.

The conditions leading up to the crisis, characterized by an exorbitant rise in asset prices and associated boom in economic demand, are considered a result of the extended period of easily available credit, inadequate regulation and oversight etc.

Some trace the genesis to the Chinese buying US treasuries with their export earnings thus supplying the US cheap money that they could lend recklessly.

The recession has renewed interest in Keynesian economic ideas on how to combat recessionary conditions. Fiscal and monetary policies have been significantly eased to stem the recession and financial risks. Economists advise that the stimulus should be withdrawn as soon as the economies recover enough to "chart a path to sustainable growth". Indian withdrawal from stimulus began in 2010-11 Union Budget and the money policy is becoming tight gradually.

Among the various imbalances in which the U.S. monetary policy contributed by excessive money creation, leading to negative household savings and a huge U.S. trade deficit, dollar volatility and public deficits.

The best authors on the meltdown are Arun Kumar (JNU); Joseph Stiglitz, Paul Krugman and Rangarajan.
Impact on India and related issues and terms are discussed in the class.

12 FYP-related

India@75

It is a path breaking initiative. It envisions how India should be in her 75th year of independence and seeks to bring together all stakeholders including the industry, government, institutions, community groups and individuals to translate the vision into a reality.

Prof (Late) C.K.Prahalad has been the inspiration behind India@75. While commemorating the 60th year of India's independence, in 2007 he articulated the idea of holistic three dimensional development of India to acquire enough economic strength, technological vitality and moral leadership by 75 years of independence. CII adopted his vision in 2008.The concept was adopted by CII to bring together all stakeholders, including the industry, government, institutions, community groups and individuals to translate the vision into reality.

IBIN

Planning Commission jointly with India@75 foundation launched in April 2013 , its unique initiative- India Backbone Implementation Network (IBIN) to remove bottlenecks for improving implementation of policies.

"The IBIN, structurally an organisation, is essentially a process that will promote widespread capabilities in the country to systematically convert confusion to coordination, contention to collaboration, and intentions to implementation," an official statement says.
IBIN aims to seed new techniques into the service delivery system; build a network of partners to create capability to manage effective stakeholder dialogues, resolve dispute and conduct policy impact analysis.

It will also build a knowledge base of tools, techniques and examples to systematically analyse situations or challenges and proactively create solutions.

According to Planning Commission Member Arun Maira: "The IBIN is a fantastic opportunity to resolve issues pertaining to poor implementation and lack of multi-stakeholder consensus by institutionalising capabilities to systematically convert 'confusion to coordination, contention to collaboration, and intentions to implementation' across the country."

Ibin is the model of a process for rapidly improving a nation's capabilities to get things done systematically and democratically as in the Total Quality Movement (TQM) in Japan.
In less than two decades, Japan, that had a reputation for poor quality and low-cost products, became the international benchmark of quality in many industries and several of its public services too.

The essence of the TQM movement was the deployment, at several levels in many organisations: especially the 'shopfloor' levels, but higher levels also, even to top management, of simple techniques for systems thinking, cooperative action and continuous improvement.

These techniques were developed by experts in companies and universities and disseminated in the country through industry and other institutional networks, and through radio, pamphlets, competitions and other means of connecting with the public.

The 'movement' grew as a network: it was not a centrally-managed government programme. There was a principal node in the network: a non-governmental body, the Japanese Union of Scientists and Engineers (Juse), in which many persons from industry and academia, and also government participated to provide a facilitative leadership to the movement.

Within the 12th Plan is the description of a similar transformative process to improve capabilities in the country to get things done. This process, described as the India Backbone Implementation Network, or IBIN, can improve results in many sectors of the economy.
The architecture of IBIN is along similar lines as the TQM movement of Japan. Experience of other countries, such as South Korea and, more recently, Malaysia, which have systematically improved capabilities of coordination and implementation, has also been considered while developing IBIN to fit India's conditions.

The tools and techniques that will be deployed by the IBIN movement will be in some respects similar to TQM, but updated and customised for the objectives of IBIN, with its emphasis on techniques and tools for collaboration, coordination and implementation. They are described in the 12th Plan document now awaiting the approval of the National Development Council.

India has many popular movements uniting citizens against what they do not want: of which corruption is a principal element. The country also needs movements to unite citizens for what they want in their habitats and their lives, and to enable them to work together to create it. The nascent IBIN is a movement for co-creating our worlds.
Like TQM in Japan, it will be formed by a network of many leaders across the country, in the states and in many sectors. Critics say the change IBIN seeks will take a long time, and so it may.

FISCAL SYSTEM

Fiscal policy

Definitions

- That part of government policy which is concerned with raising revenue through taxation and with deciding on the amounts and purposes of government spending.
- The government's policy in regard to taxation and spending programs. The balance between these two areas determines the amount of money the government will withdraw from or feed into the economy, which can counter economic peaks and slumps.
- Government spending policies that influence macroeconomic conditions. These policies affect tax rates and government spending, in an effort to control the economy.
- Government policy for dealing with the budget-especially with taxation and borrowing
- The policy of a government in controlling its own expenditures and taxation, which together make up the budget
- Fiscal policy is the means by which a government adjusts its levels of revenue and spending in order to monitor and influence a nation's economy

Fiscal policy involves use of taxation and government spending to influence economy. In other words, fiscal policy relates to raising and spending money in quantitative and qualitative terms.

As far as fiscal receipts are concerned, taxes, user charges (power, water, transport charges etc); disinvestment proceeds; borrowings from internal and external sources are the main channels. All receipts are not earned and some are borrowed. Receipts and expenditure are divided into revenue and capital accounts. Expenditure is also shown as Plan and Non-plan items.

Fiscal policy deals not only with the quantity but the quality of public finance as well. In other words, not merely how much is raised and spent but how has it been raised- is it raised by way of taxes or borrowings; are they excessive or irrational etc. Also, the way the finances so raised are used- wastefully or productively. How much is spent on plan heads and how much populistically targeted etc also is studied.

Fiscal policy can achieve important public policy goals like growth; equity; promotion of small scale industries; encouragement to agriculture; location of industries in rural areas; labour -intensive growth; export promotion; development of sound social and physical infrastructure etc.

Art.112 of the Constitution mandates that expenditure be shown in revenue and other categories.

Non-Plan expenditure is not a Constitutional term but is in use to emphasize on the point that government spends financial resources for consumption (maintenance) as well as asset creation. It includes expenditure on interest payments; defense; subsidies; and public administration.(such as salaries)

A break up of the finances into revenue and capital streams, in general, is as follows:

(keep coming regularly)

- Revenue receipts are recurrent receipts. Revenue account includes the following receipts: taxes and non-tax sources. Taxes are income tax , corporation tax, excise duty, customs duty etc; non tax resources include user charges ;interest receipts; dividends; profits etc

interest on loans

- Revenue account expenditure is essentially the non-plan expenditure that does not create assets, that is, - interest payments, defence; subsidies and public administration. It is synonymous with maintenance and consumption expenditure as also welfare expenditure.

Grant in aid

- Capital account receipts are recoveries of loans and advances made by the Union Government to States, Uts and PSUs; fresh borrowings from inside the country and from abroad;disinvestment proceeds etc. As is clear from above, some of them are debt and some are non-debt.

recovery of loans

- Capital account expenditure is loans made to States, UTs and PSUs; expenditure for asset creation in infrastructure and social areas;loans repaid etc.

Definitions of Deficits

Revenue deficit is the difference between the revenue receipts on tax and non-tax sides and the revenue expenditure. Revenue expenditure is synonymous with consumption and non-development, in general. But in the case of India, the social sector expenditure – flag ship schemes like NREGA is in the revenue expenditure, though as a part of the Plan expenditure (see budget as a glance for further clarity. It is given elsewhere in this Chapter) It is targeted at 3.3% of GDP for 2013-14. FRBMA 2003 says that RD should be zero by the end of 2008-09. The objective is to fund for consumption from government's own resources and not borrowing. In fact, if the FRBM was implemented well, there would have been revenue surplus from 2009-10 onwards that could be used for capital expenditure. But the Great Recession of 2008 made it necessary for the government to borrow more and stimulate the economy thus disrupting the FRBM targets. (More in the classroom)

Fiscal deficit is the difference between what the government earns and its total expenditure. That is, the difference between what is received by the government on revenue account and all the non-debt creating capital receipts like recovered loans and disinvestment proceeds ; and the total expenditure. It amounts to all borrowings of the government in a given period. It is targeted at 5.1% of GDP in 2012-13.

FD= Total expenditure of the Government in a budget minus (Revenue receipts + non-debt creating capital receipts).

Difference must be between Gross FD and Net FD. Net Central Fiscal Deficit is calculated by deducting from the GFD the financial assistance (loans and grants) that the States are given.

Budget deficit considers only the difference between the total budgeted receipts and the expenditure. It was abolished in 1997.

Fiscal Deficit mirrors the health of government finances most accurately unlike the budget deficit concept. BD does not cover all borrowings but only that portion of the borrowings for which government relies on printing money by the RBI → eg. Total receipt = 95; target expenditure = 100 so if out of 5 Rs, 3 borrowed from SLR & 2Rs ~~from~~ by printing, so FBD = 2 Rs

Monetised deficit is the borrowings made from the RBI through printing fresh currency. It is resorted to when the government can not borrow from the market (banks and financial institutions like LIC etc) any longer due to pressure on interest rates or for reasons like fresh money injection into the economy is necessary to push growth up. It means infusion of fresh currency into the market. It corresponds to the budget deficit that is discarded as a concept since 1997. It is discontinued from 2006 as a part of the FRBM 2003.

Primary deficit is the difference between the fiscal deficit and the interest payments. The concept helps in assessing the progress of the government in its fiscal control efforts.

Suppose a govt has borrowed so much in 2012. Now if govt B come to power and deficit is 100 Rs. Out of which interest on borrowing is 70 Rs. So. for govt B primary deficit is 30 Rs.

Deficit Financing

Govt gets money by borrowing also so it will get added to receipt i.e. only BD do not show borrow

Deficit Financing is the phrase used to describe the financing of gap between Government receipts and expenditure. Such gap is called budgetary deficit. It is financed by printing fresh money by the RBI. The gap can be deliberate as the Government wants to spend on welfare and infrastructure for which it has no money and so borrows from the RBI; or due to bad finances of the government; or mainly for consumption and populism.

When the Government has to spend more than what it can raise through tax, non-tax and other sources, it borrows from the market. It can not borrow above a certain amount from the market as it may be inflationary; push up interest rates; increase government's debt burden and thus divert resources from plan to non-plan; burden future generations with unduly high taxation and thus disrupt inter generational parity; and crowd out private investment. Then Reserve Bank of India prints money . In other words, when the resources from taxes, user charges, public sector enterprises, public borrowings, small scale borrowings and others are not enough, RBI prints and gives to the Government. It is called deficit financing.

The money printed by the RBI is called high powered money or reserve money.

The concept of budget deficit was dropped from 1997 budget and as a result deficit financing also was stopped. That is, as a concept both were discontinued as the two were two sides of the same coin- budget deficit is monetized through deficit financing. In fact, FRBM disallows RBI printing money to finance government deficit in normal conditions. But the economic conditions having become adverse since 2008-09, Government is forced to abandon the FRBM rules and is spending well beyond the limits set by the Act. Keynesian stimuli that the government resorted to since 2008 October includes massive borrowing by the Government- from the markets and RBI- to arrest slowdown and stimulate growth.

The beneficial contribution of deficit financing in the early stages of independent India's economic planning and development is manifold. First, in the early 1950s, our domestic savings ratio was less than 9 per cent of GDP, and that constrained the investment and welfare activity of the government.

Second, the capacity to raise non-inflationary sources of financing (taxes, small savings, genuine public borrowings, etc.) was highly limited.

Third, external aid could supplement domestic funding only to a limited extent. It is better to source debt from inside than outside.

Fourthly, foreign direct investment was discouraged as a source of investment and thus scarcity of investment resulted. Therefore, government borrowing became necessary through monetization.

There are two views on the matter. There are some people who regard deficit financing as essential for the purposes of development and welfare; as a healthy means of stimulating economy. There are those who regard any deficit financing as inflationary and a serious threat to the stability of the economy.

On balance it may be said that, if deficit financing is done prudently and the borrowed money is used well, it is healthy. However, if the borrowed money is wasted for consumption, is it against good economics as it can negatively affect money supply and inflation; and also dampen growth.

The viability and desirability of deficit financing, in short, depends on

- Extent of borrowing
- End use of the money borrowed.

WMAs (Ways and Means Advancement)

Prior to 1997, the RBI lent to central government against ad hoc Treasury bills, (since mid-50's) This provision for extending short-term financing was created to bridge temporary mismatches in receipts and payments. However,, the central government slipped into the practice of rolling over this facility, resulting in automatic monetisation of the government's deficit. Automaticity refers to RBI having to print money if the Government's cash balances with the RBI went below a threshold fixed. It had no choice but to create currency and lend to the Government of India. The process of creating 91-day bills and subsequently funding them into non-marketable special securities at a very low interest rate (4.6%) emerged as a principal source of borrowing. It was thought to be irrational for the reasons that the interest rate is not market driven and was very concessional. Nor did the RBI have any voice in deterring the same. Nor was there a limit to how much could be printed in this way.

RBI ~~[illegible]~~ charging only 4.6% to Govt. So it was lucrative since market rate was more.

→ Banks were charging more to lenders.

In the case of state governments, the RBI provides two types of WMAs. Normal WMAs are clean or unsecured advances extended at the bank rate, while special WMAs are extended against the government securities. The latter is exhausted first and then the former may be sought to a limited extent. If the state government borrows over and above the WMA allowed for it by the RBI, it is called overdraft and there is a limit to that too set by the RBI.

Adhoc treasury bills and WMA

Union Government replaced adhoc treasury bills with WMAs in 1997.
WMAs given by RBI to GOI do not require any collateral. Its amount is limited and arrived at the beginning of the fiscal year through consultation between Government and the RBI. There are penal interest rates if the pre-agreed amount is violated. Ways and Means

Advances are made at the Repo Rate. Overdraft is charged penally at two percent above the repo rate

Replacement of the adhoc bills with WMA represents an advance in fiscal discipline and harmonization of the fiscal and monetary policies as the RBI is consulted in Governmental short term borrowing and the 'automaticity' is dropped in the creation of currency by the RBI to fund governmental expenditure.

How much of Fiscal Deficit is right?

Fiscal deficit is bridged by market borrowings and central bank printing fresh currency (monetization), if necessary. To a limited extent, FD is important as the Government's ability to help growth and welfare increases. Government can always return the loans when its revenues improve due to tax buoyancy. However, FD becomes problematic and even destabilizing when it overshoots a rational threshold. Sovereign debt crisis in Europe and the fiscal woes of USA are the result of unsustainably high debt and borrowing. (More in the classroom)

Therefore, moderation of fiscal deficit is important. Large and persistent fiscal deficits are a cause of concern, as they pose several risks.

Fiscal deficits may cause macroeconomic instability by inflating the economy as money supply rises.

Corporate sector is crowded out – they are left with inadequate funds in the markets as the government borrowing requirements increase. Added to that , interest rates will be high as there is pressure on the available money in the market.

If the funding route is through RBI monetization, it means inflation and instability.

Inflation may mean less savings, less investment and eventually it hurts the sustainability of high growth.

Large deficits, even if they do not spill over into macroeconomic instability in the short run, will require higher taxes in the long term to cover the heavy burden of internal debt. It means, as the FRBM Act says , inter generational parity is hurt if debt mounts as future generations will have to pay higher taxes to help the government repay the debt.

Government liabilities- interest payments- increase and there is far less for development.

BOP pressures may mount if inflows drop due to the country being downgraded by rating agencies like Standard and Poor, Moody etc.

Therefore, FDs must be moderated- they are desirable within limits but hurtful beyond the limits.

The above analysis applies to FD in normal times. But in abnormal times like since 2008-09 when the world slipped into recession impacting Indian economy negatively, FD must be allowed to be increased for the fiscal stimuli which are necessary to arrest downturn in the

economy and revive growth. FRBM allows such counter-cyclical expenditure. Even then, deficit should be incurred not for populist expenditure but to stimulate the economy.

The sovereign debt crisis in Eurozone (2010 onwards) and particularly the Greece economy is due to excessive FD. It borrowed and spent excessively. Taxes were not collected efficiently and there was large scale evasion. The stimulus package did not work. Government expenditure did not reduce but revenues fell drastically due to recession and tax leakages. The need for massive borrowing and spending increased. But the government was not able to raise the money at normal rates of interest. It had to pay high rates of interest. That means it was debt-trapped- borrow to pay the debt ~~and~~ at higher and higher rates. The banks and other financial institutions that invested in Greek government bonds panicked. Their share prices fell. Financial system was in danger of instability. Similar crisis was seen in Ireland later and Spain and Portugal too. These countries are acronymally called PIGS. The lesson from Greek crisis is that FD may be incurred only for productive reasons and ensure good returns. Tax collections should be efficient. Accounts of government should be properly maintained and not dressed up.

Reducing FD

FD has to be reduced and the FRBM targets are to be conformed to, under normal conditions. But upto3% of GDP for FD as laid down by FRBM Act is desirable as the Government can borrow and spend for welfare and growth.

The extent of reduction and the manner of reduction matter. More resources should be raised from taxes, user charges, disinvestment etc. Expenditure control should not involve cuts on social sector expenditure as it hurts poor and demographic dividend can not be reaped.

The level of FD should be determined keeping in consideration the following

- whether the debt can be put to productive deployment
- The rate of return on the borrowed funds' use is adequate
- the impact on private sector investment by way of crowding out effect etc

Even more important is not to cut social spending in a move to reduce deficit. In other words, while FD reduction is needed for macroeconomic stability and inter generational parity. Introduction of GST, the DTC amendments, selective disinvestment, broadening of tax base, tax buoyancy etc will yield enough to moderate borrowings.

Global crisis and the FD in India

Global recession impacted India and our growth rate slipped. Tax revenues were hit. There was a massive fall in demand. Corporate sectors postponed investment. Threat to employment was real. Therefore, Government took it upon itself to spend more by borrowing. The result is that fiscal deficit reached an abnormally high level- 6.8% in the year 2009-10. It is because tax revenues went down and expenditure demands were higher. The gap inevitably widened. The fiscal measures taken by the government to counter the negative fall -out of the global slow down on the Indian economy paid off.

Firstly, the Government responded by providing three focused fiscal stimulus packages in the form of tax relief to boost demand and increased expenditure on public projects to create employment and public assets.

Secondly, the RBI took a number of monetary easing and liquidity enhancing measures to facilitate flow of funds from the financial system to meet the needs of productive sectors.

This fiscal accommodation led to an increase in fiscal deficit from 2.7 per cent in 2007-0.8 to 6.2 percent of GDP in 2008-09.
These measures were effective in arresting the fall in growth rate of GDP in 2008-09 and stemmed the fall and achieved a growth of 6.7 per cent. The growth rate further improved to 8.4 % for the next two fiscal years of 2009-10 and 2010-11.

The fiscal stimulus packages

To counter the adverse effects of global recession, government announced the first package in October 2008- tax cuts and additional spending by the government .The package benefited all the sectors – especially textile, housing and real estate sectors. Most significant of the package is the CENVAT rate cut of 4%.

The second stimulus package

The government in January 2009 announced the second round of fiscal stimulus package with a view to revive economy. The package includes measures such as higher public spending. RBI stepped in easing liquidity for further lending at lower interest rates etc.

The third stimulus package

The third stimulus package for the economy was announced in February 2009 cutting excise duty and service tax two percentage points.

Service tax was cut across the board from 12 per cent to 10 per cent.

The packages increased the fiscal deficit.

Financing the FD

The deficit was financed by raising Internal Debt and from Public Account surplus cash.

The unsustainably high fiscal deficit could not be continued long and had to be phased back to normal levels by a calibrated rollback since 2010-11.

FRBM Act 2003

Fiscal Responsibility and Budget Management (FRBM) Act 2003 was notified in 2004 with the following salient features

- annual targets of reduction in deficits, government borrowing and debt

- Government to annually reduce the revenue deficit by 0.5 per cent and the fiscal deficit by 0.3 per cent beginning fiscal 2004-05.
- elimination of revenue deficit and reduction of fiscal deficit to 3% of GDP by March 31, 2009
- a cap on the level of guarantees and total liabilities of the Government.
- Prohibits Government to borrow from the RBI (primary borrowing) after April 1, 2006. RBI can not print money to lend to the government.
- On a quarterly basis, that Government shall place before both the Houses of Parliament an assessment of trends in receipts and expenditure.
- Annually present the macro-economic framework statement, medium term fiscal policy statement and fiscal policy strategy statement. The three statements would provide the macro-economic background and assessment relating to the achievement of FRBM goals.
- Under exceptional circumstances, Government may be compelled to breach targets. In case of deviations, the Government would not only be required to take corrective measures, but the Finance Minister shall also make a statement in both the Houses of Parliament.

Borrowing from the RBI is permitted in exceptional situations like natural calamities.

FRBM was brought in for fiscal discipline; increase plan expenditure; reduce the amount of borrowings; meet consumption from government's own fiscal resources; leave the RBI with autonomy as far as money creation goes etc .Fiscal consolidation is necessary particularly in the era of globalization when the penalty for irresponsibility is high.

New Zealand was the first country to enact a Fiscal Responsibility Act in 1994, thereby setting legal standards for transparency of fiscal policy and reporting, and holding the Government formally responsible to the public for its fiscal performance. A similar legislation, the Charter of Budget Honesty, has been enacted in Australia. The UK, too, has enacted a Code for Fiscal Stability.

The global recession from 2008 onwards has made the government breach the FRBM targets vastly. We are still gross breach of it .Fiscal 2012-13 saw a fiscal deficit of 5.8% of GDP due to excess expenditure on subsidies, lower divestment receipts and tax receipts.

FRBM 2.0

Union Budget 2012-13 saw introduction of amendments to the FRBM Act as part of Finance Bill, 2012. Concept of "Effective Revenue Deficit" and "Medium Term Expenditure Framework" statement are two important features of amendment to FRBM Act in the direction of expenditure reforms. Effective Revenue Deficit is the difference between revenue deficit and grants for creation of capital assets. This will help in reducing consumptive component of revenue deficit and create space for increased capital spending. "Medium-term Expenditure Framework" statement set forth a three-year rolling target for expenditure indicators.

ERD

An additional fiscal indicator, namely, effective revenue deficit, has been prescribed by an amendment to the FRBM Act by the Finance Act, 2012. Effective revenue deficit has been

defined as the difference between "the revenue deficit and the grants for creation of capital assets".

Grants for creation of capital assets are defined as "the grants-in-aid given by the Central Government to the State Governments, constitutional authorities or bodies, autonomous bodies and other scheme implementing agencies for creation of capital assets".

The amendment confers a statutory status on the concept of effective revenue deficit which had already featured in the Central Budget 2011-12. The proposed amendment seeks to eliminate effective revenue deficit by 2015.

Fiscal consolidation

Fiscal consolidation means strengthening government finances. Fiscal consolidation is critical as it provides macro economic stability; cuts wasteful expenditure; can enable government to spend more on infrastructure and social sectors. Tax reforms, disinvestment, better targeting of subsidies and so on are the hallmarks of fiscal consolidation.

Enactment of FRBM Act provides an institutional framework and binds the government to adopt prudent fiscal policies. There is a need to involve states to effect overall fiscal consolidation and strengthen the growth momentum.

GST and revised DTC are an important federal effort toward fiscal reforms and consolidation.

Also, without fiscal consolidation- conversion of subsidies into capital expenditure that forms assets- it is not possible to step up public investment, especially in areas such as agriculture, where gross capital formation has dropped from 1.9 per cent to 1.3 per cent of GDP since 1990-91.

Fiscal consolidation in India includes the following reforms:

- Revenue reforms include tax reforms on both direct and indirect tax front; rationalization of tax exemptions, improving efficiency of tax collection, and tax stability.
- On the expenditure side, reform areas include cutting out non-essential and unproductive activities, schemes and projects, allocation of resources to priority areas, reducing cost of services, rationalizing subsidies; reduction of time and cost overruns on projects, getting proper 'outcome' from output

Govt have less money with her to spend. so slashing subsidies & other expenditures

Austerity measures as were announced in September 2013 : ban on five-star venues for government meetings; foreign locations for conferences, exhibitions and seminars; and executive class airline tickets for officials;keep the size of delegations going abroad at an "absolute minimum; banned recruitment for central government posts for one year and the purchase of new vehicles.

Fiscal consolidation

The FRBM targets were more or less followed till the fiscal year 2007-08. But from 2008-09, as global economic conditions turned bad and Indian economy was also affected negatively –

but interest goes into revenue receipt

slow down in growth rate-, the Government necessarily had to pump prime the economy with an expansionary fiscal policy- tax reliefs and massive public investment- infrastructure spending, NREGA being stepped up etc. As a result, the FRBM targets could not be complied with. However, the recovery plan has been made with statutory commitments in 2012-13. (More in the classroom)

13th Finance Commission and Fiscal Consolidation

Thirteenth Finance Commission recommended a calibrated exit strategy from the expansionary fiscal stance of the previous two years. The Commission recommended a capping of the combined debt of the Centre and the States at 68 per cent of the GDP to be achieved by 2014-15.

As a part of the fiscal consolidation process, government for the first time targeted an explicit reduction in its domestic public debt-GDP ratio.

Plan and Non Plan Expenditure classification and its unsustainability

In the Budget, expenditure is shown both as revenue and capital and also as plan and non-plan. 'Plan' expenditures, as the name implies, relate to expenditures on annual plan projects contributing to five-year plan; these include projects like dams, roads, power plants etc. Non-Plan expenditure relates to maintenance, consumption and welfare. Non-plan expenditure does not create assets. When a project is being built , it is a plan item of expenditure. When completed and being maintained, it is a non-plan item of expenditure.

'Non-plan' expenditure is a generic term, which is used to cover all expenditures of government not included in its annual plan programmes. But essentially covers consumption and maintenance expenditure. Non plan expenditures has the following items

- Interest payments
- Subsidies
- Defence
- Public admn

It is important to mention that not only that maintenance expenditures subsequent to the completion of plan programmes are non-plan, but even "expenditures on research projects and operating expenses of power stations are classified as non-plan.

The distinction between plan and non-plan expenditure items has become simplistic and is artificial and untenable. The building of a new school or a primary health centre is considered a Plan investment but its running and maintenance is considered non-Plan spending. Thus, very often it had led to Government allocation being reduced for maintenance as it is classified as non-plan item and will be criticized. Thus, assets are neglected. New projects are allotted money while the completed projects are neglected.

It is important to take a consolidated view of finances keeping in perspective the interdependence of Plan and non-Plan expenditures.

Untenable → Not able to be defended against criticism or attack

Rangarajan panel on public expenditure 2012

An 18-member high-level expert committee was set up in 2010 under the Chairmanship of Dr C. Rangarajan to suggest measures for efficient management of public expenditure.

This committee was mandated to see whether the classification of expenditure into Plan and Non-Plan is rational and can be continued.
The report of the Committee was presented in mid-2011 and the following are the salient points:

- The government should do away with the distinction between Plan and Non-Plan expenditure and redefine roles of the Planning Commission and the Finance Ministry.
- While the Planning Commission should be responsible for formulation of the Five-Year Plan, the task of firming up annual budgets should be entrusted to the Finance Ministry based on inputs from the Plan panel
- "Plan and Non-Plan distinction in the budget is neither able to provide a satisfactory classification of developmental and non-developmental dimensions of government expenditure. It has therefore become dysfunctional. The committee, therefore, it recommends that Plan and Non-Plan distinction in the budget should be removed.
- The report suggested a basic shift in budgeting approach from ".From input based budget to outputs and outcomes".
- As regards the new roles of key entities, it said, the Planning Commission should be made "responsible for consolidation of Five-Year Plan over all services based on the input from the Ministry of Finance... (while) Ministry of Finance (be) made responsible for the preparation of Annual Budget based on the inputs from the Planning Commission".
- The report also called for strengthening the Central Plan Monitoring System (CPMS) and empowering the citizens to seek information on flow of resources and utilisation with a view to promoting transparency and accountability.

Kelkar committee 2012

A new roadmap for fiscal consolidation worked out by a committee headed by former Chairman of the Finance Commission Vijay Kelkar envisages pruning fiscal deficit to less than 5% of the GDP by 2013-14 to put the economy in a better shape.

The committee re-assessed the fiscal deficit for 2012-13 and recommended an annual reduction of half a percent or 0.5% up to 2013-14. Fiscal deficit, as stated in the notes above, is the difference between total expenditure and total non-borrowed receipts.

The Kelkar committee said that the proposed reduction in deficit could be achieved through a combination of share sale of state-owned companies, pruning petro-product subsidies through raising prices of diesel and LPG or cooking gas and implementation of the Goods and Services Tax or GST, which has long been in the works. Administrative reforms including beefing up of IT infrastructure have also been suggested to improve compliance.

The 13th Finance Commission, which was headed by Kelkar, advised that fiscal deficit be pegged at 3% in 2013-14 when it unveiled its report.

Public debt

Public debt includes internal debt comprising borrowings inside the country like market loans; borrowing from the RBI on the basis of special securities bills; and external debt comprising loans from foreign countries, international financial institutions, NRI deposits etc. In the expression `public debt and "other liabilities",

"other liabilities" include outstanding against the various small saving schemes, provident funds etc. External debt means what the nation owes to foreign lenders- includes private sector borrowings too. However, public debt includes what the government owes to lenders inside and outside the country. (More in the classroom)

Public debt is justified as the government does not have adequate resources and taxation can not be done beyond a point. It should be for productive reasons and also welfare reasons. The spiral of deficit and debt run the risk of undermining the country's creditworthiness, devaluing the currency and destabilising the entire economy with grave social consequences. Therefore, it should be incurred judiciously.

The outstanding internal and external debt and other liabilities of the Government of India at the end of 2013-2014 is estimated to amount to ` 56,51,484.22 crore, as against `. 50,39,131.01 crore at the end of 2012-2013 .

India recorded a Government Debt to GDP of 67.57 percent of the country's Gross Domestic Product in 2012. Government Debt To GDP in India is reported by the Ministry of Finance, Government of India. From 1991 until 2012, India Government Debt to GDP averaged 74.6 Percent. Generally, Government debt as a percent of GDP is used by investors to measure a country ability to make future payments on its debt, thus affecting the country borrowing costs and government bond yields.

External Debt

India's external debt in mid-2013 stood at 388 billion US dollars on account of significant increase in commercial borrowings, short-term trade credits, and rupee denominated debt. In terms of major components, the share of ECBs continued to be the highest at 30.7 per cent of total external debt, followed by short term debt (24.9 per cent) and NRI deposits (18.3 per cent).The share of short-term debt in total debt rose over the preceding as well as corresponding quarter of the previous year. The long-term debt at US$ 291.8 billion and short-term debt at US$ 96.8 billion accounted for 75.1 per cent and 24.9 per cent, respectively, of the total external debt as at end-June 2013.The ratio of short-term debt (original maturity) to foreign exchange reserves rose to 34.3 per cent as at end-June 2013 from 33.1 per cent as at end-March 2013. Based on residual maturity, the short-term debt accounted for 43.8 per cent of total external debt as at end-June 2013. Within the short-term debt, the share of NRI deposits was 28.1 per cent.

External debt includes both the government and private debt as can be seen from the above given highlights of the external debt profile.

The share of non-government debt in total external debt is about 75%.

The strategy of the government in external debt management consists of emphasis on raising sovereign loans on concessional terms with longer maturities, monitoring short term debt and encouraging non-debt creating capital flows.

External debt consists of

- long-term external debt which is the bulk part
- NRI deposits
- multilateral loans
- commercial borrowings
- bilateral loans and
- Trade credit

As reported in the Hindu newspaper in 2013; India's short-term debt maturing within a year stood at $172 billion end-March 2013. This means the country will have to pay back $172 billion by March 31, 2014. The corresponding figure in March 2008 — before the global financial meltdown that year — was just $54.7 billion. India has accumulated short-term debt with *residual maturity* of one year after 2008. The figure has gone up over three times largely because this period also coincided with the unprecedented widening of the current account deficit from roughly 2.5 percent in 2008-09 to nearly 5 per cent in 2012-13. Much of this expanded CAD has been funded by debt flows.Short-term debt maturing within a year is now nearly 60 per cent of India's total foreign exchange reserves. In March 2008, it was only 17 per cent of total forex reserves. This shows the actual increase in the country's repayment vulnerability since 2008.

Internal debt

Internal debt includes loans raised by the government in the open market through treasury bills and government securities, special securities issued to the RBI and most importantly, various bonds like the oil bonds, fertilizer bonds etc.

The money sterilized from the market in by the Market Stabilisation Scheme (MSS) is also shown in the government's statement of liabilities. Introduced in 2004, MSS envisages the issue of treasury bills and/or dated securities to absorb excess liquidity arising out of the excessive foreign exchange inflows.

The debt of the government also includes others like the outstanding against small-savings schemes, provident funds, deposits under special deposit schemes etc.These debts are shown under a separate head titled 'other liabilities'.

Debt should be moderated for the reasons cited in the discussion on FD above.

Zero Base Budgeting

Tenth Plan Approach Paper says that ZBB will be followed for rationalization of expenditure. The ZBB methodology was taken up first in 1987 in the Union Budget and was recommended for the Government departments and PSUs. Many state governments also applied it, for example, Government of Rajasthan and Maharashtra. The Maharashtra Government renamed it ' Development –based budget '.

Under the ZBB, a close and critical examination is made of the existing government programmes, projects and other activities to ensure that funds are made available to high priority items by eliminating outdated programmes and reducing funds to the low priority items. Governmental programmes and projects are appraised every year as if they are new and funding for the existing items is not continued merely because a part of the project cost has already been incurred. Programmes are discarded if the cost-benefit ratio is below the prescribed norms.

The objective of the ZBB is to overhaul the functioning of the government departments and PSUs so that productivity can be increased and wastage can be minimised. Scarce government resources can be deployed efficiently.

ZBB as a resource planning and control technique and process yielded substantial benefits in the advanced countries like New Zealand, UK, Australia and Sweden in terms of efficiency gains, better resource use, lower costs and finally surplus budgets, particularly in New Zealand.

However, the use of ZBB to human development programmes and poverty alleviation and employment generation programmes is limited and the results are cumulative and can not be assessed annually.

Fringe benefit tax (FBT)

Fringe benefits are usually enjoyed collectively by the employees and cannot be attributed to individual employees singly.They are taxed in the hands of the employer who may or not pass it on to the employee. Examples are transport services for workers and staff, gym, club, etc.

The rationale for levying a FBT on the employer lies in the inherent difficulty in isolating the 'personal element' where there is collective enjoyment of such benefits and attributing the same directly to the employee. This is so especially where the expenditure incurred by the employer is ostensibly for purposes of the business but includes, in partial measure, a benefit of a personal nature. It is abolished in the Union Budget 2009-10.

Perquisites

Perquisites are benefits in addition to normal salary to which employee has a right by virtue of his employment. To put it simply or 'perks' as they are called colloquially, are benefits generally in cash/kind, received by an employee by virtue of his employment.

Perks are taxable as a part of salary as per the India income tax laws and includes:

- the value of rent-free accommodation
- the value of any concession in the matter of rent respecting any accommodation provided etc
- car
- club membership
- travel

Tax brackets
10%, 20%, 30%
on income.

Some words

Fiscal Drag

A situation where inflation pushes income into higher tax brackets- bracket creep. The result is increase in income taxes but no increase in real purchasing power. This is a problem during periods of high inflation. Government gains due to higher tax collections and the economy suffers as growth is dragged down due to less demand. In high-growth and high inflation economies ('overheated'), fiscal drag acts as an automatic stabiliser, as it acts naturally to keep demand stable.

Fiscal neutrality

When the net effect of taxation and public spending is neither neutral, neither stimulating nor dampening demand- a balanced budget. It is neutral, as total tax revenue equals total public spending.

Crowding Out

Excessive government borrowing can lead to shrinkage of the liquidity in the market; forces the interest rates to go up; private investment is crowed out for two reasons: liquidity availability is less and the rates are high. Investment suffers and growth decelerates. The Government also may not spend the borrowed resources well to generate returns. If the government deploys the funds well, it may have a 'crowding in effect': the infrastructure built can have a multiplier effect on investment, tax collections and growth.

Pump-priming

Deficit financing and spending by a government on public works in an attempt to revive economy during recession – countercyclical measures. It can raise the purchasing power of the people and thus stimulate and revive economic activity to the point that deficit spending will no longer be considered necessary to maintain the desired economic activity.

Small Savings

Small savings instruments are Post Office Monthly Income Schemes and Time Deposits; National Savings Scheme; Indira Vikas Patra; Kisan Vikas Patra;Public Provident Fund and so on. They are aimed at promoting safe and long-term savings by individuals. They are called small savings because the amount saved is relatively small. They are initiated by the central Government but mobilized by the State Governments ; and are deposited with and managed by the central government. As a reward State Governments receive all such savings as loan.

Small savings are a sizeable portion of the financial savings of the country. They contribute to the finances of the Government- federal and State- that is, they are an important source of borrowing for the government. These schemes have a built in tax concession that enhances their attraction for the small savers. They also earn a rate of interest that is higher in comparison to what the banks offer- approximately 8%. They are called small savings as savings are made in small amounts by low income and other groups.

Small savings instruments in India are retailed through 1.53 lakh post offices of which about 1.29 lakh are in rural areas.

The National Small Savings Fund (NSSF), in the Public Account of India has all the small savings. They are completely onlent to the state in which they are collected.

Public goods, merit goods and demerit goods

Public goods are those goods whose consumption by some does not diminish them for others. That is, they are non-rivalrous. Common examples include law and order, parks, street-lighting, defence etc. They are goods meant for the entire public. Merit goods are goods like education, health care etc that are important for the society as a whole- that is, they have positive externalities. Market may not supply them in adequate quantities. Government supplements the market.Demerit goods are those whose consumption should be discouraged. They have negative externalities. Examples include: tobacco, alcohol etc. Thirteenth Finance Commission calls them sin goods and wants them to be harshly taxed.

Giffen goods

They include goods whose demand goes up when the price increases. They are the status markers and exclusivist in nature.

Twin deficits

Budget deficit (fiscal deficit) and current account deficit-the former fuelling the latter as the borrowings increase are known as twin deficits. USA is a prime example.So is India!!!!

(Recent developments in the classroom)

'Fiscal Cliff'

A combination of expiring tax cuts and across-the-board government spending cuts scheduled to become effective Dec. 31, 2012. The idea behind the fiscal cliff was that if the federal government allowed these two events to proceed as planned, they would have a detrimental effect on an already weak economy, perhaps sending it back into an official recession as it cut government spending and investment, collected more taxes which cut down both consumption and investment, increased unemployment rates and undermined consumer and investor confidence.

Shutdown

In U.S. politics, a government shutdown is the name for the process the Executive Branch must enter into, when the Congress creates a "funding gap" by choosing not to or failing to pass legislation funding government operations and agencies. If interim or full-year appropriations are not enacted into law, the United States Constitution requires the federal government begins a "shutdown" of the affected activities. If the funding gap lasts long enough, the law requires the furlough (temporary lay offs) of non-emergency personnel and curtailment of agency activities and services. It is essentially a fiscal issue as the Congress may not like the revenue and expenditure models and priorities of the Presidency as Obamacare in 2013.

Stimulus vs Austerity (In the class)

Bailout - Financial package to ailing unit
- Buying their shares

SRIRAM'S IAS

बजट का सार Budget at a Glance

(करोड़ रुपए) (In crore of Rupees)

		2011-2012 वास्तविक Actuals	2012-2013 बजट अनुमान Budget Estimates	2012-2013 संशोधित अनुमान Revised Estimates	2013-2014 बजट अनुमान Budget Estimates
1. राजस्व प्राप्तियां	1. Revenue Receipts	751437	935685	871828	1056331
2. कर राजस्व (केन्द्र को निवल)	2. Tax Revenue (net to centre)	629765	771071	742115	884078
3. कर-भिन्न राजस्व	3. Non-Tax Revenue	121672	164614	129713	172252
4. पूंजी प्राप्तियां (5+6+7)$	4. Capital Receipts (5+6+7)$	552928	555241	558998	608967
5. ऋणों की वसूली	5. Recoveries of Loans	18850	11650	14073	10654
6. अन्य प्राप्तियां	6. Other Receipts	18088	30000	24000	55814
7. उधार और अन्य देयताएं*	7. Borrowings and other liabilities*	515990	513590	520925	542499
8. कुल प्राप्तियां (1+4)$	8. Total Receipts (1+4)$	1304365	1490925	1430825	1665297
9. आयोजना-भिन्न व्यय	9. Non-Plan Expenditure	891990	969900	1001638	1109975
10. राजस्व खाते पर जिसमें से	10. On Revenue Account of which,	812049	865596	919699	992908
11. ब्याज भुगतान	11. Interest Payments	273150	319759	316674	370684
12. पूंजी खाते पर	12. On Capital Account	79941	104304	81939	117067
13. आयोजना व्यय	13. Plan Expenditure	412375	521025	429187	555322
14. राजस्व खाते पर	14. On Revenue Account	333737	420513	343373	443260
15. पूंजी खाते पर	15. On Capital Account	78639	100512	85814	112062
16. कुल व्यय (9+13)	16. Total Expenditure (9+13)	1304365	1490925	1430825	1665297
17. राजस्व व्यय (10+14)	17. Revenue Expenditure (10+14)	1145785	1286109	1263072	1436169
18. जिसमें, पूंजी परिसम्पत्तियों के सृजन हेतु अनुदान	18. Of Which, Grants for creation of Capital Assets	132582	164672	124275	174656
19. पूंजी व्यय (12+15)	19. Capital Expenditure (12+15)	158580	204816	167753	229129
20. राजस्व घाटा (17-1)	20. Revenue Deficit (17-1)	394348 (4.4)	350424 (3.4)	391245 (3.9)	379838 (3.3)
21. प्रभावी राजस्व घाटा (20-18)	21. Effective Revenue Deficit (20-18)	261766 (2.9)	185752 (1.8)	266970 (2.7)	205182 (1.8)
22. राजकोषीय घाटा {16-(1+5+6)}	22. Fiscal Deficit {16-(1+5+6)}	515990 (5.7)	513590 (5.1)	520925 (5.2)	542499 (4.8)
23. प्राथमिक घाटा (22-11)	23. Primary Deficit (22-11)	242840 (2.7)	193831 (1.9)	204251 (2.0)	171814 (1.5)

इस दस्तावेज में वर्ष 2011-12 के वास्तविक आंकड़े अनंतिम हैं। Actuals for 2011-12 in this document are provisional.

$ बाजार स्थिरीकरण योजना के अंतर्गत प्राप्तियों को छोड़कर। Excluding receipts under Market Stabilisation Scheme.

* इसमें नकदी शेष में आहरण द्वारा कमी शामिल है। Includes draw-down of Cash Balance.

टिप्पणियां: 1. सीएसओ द्वारा जारी 2012-2013 के अग्रिम अनुमानों (₹10028118 करोड़) की तुलना में 13.4% की वृद्धि मानते हुए 2013-2014 के बजट अनुमान में सघउँ बढ़कर ₹11371886 करोड़ होने का पूर्वानुमान है।

2. इस दस्तावेज में पृथक-पृथक मदें पूर्णांकन के कारण संभवतः जोड़ से मेल न खाएं।

Notes: 1. GDP for BE 2013-2014 has been projected at ₹ 11371886 crore assuming 13.4% growth over the Advance Estimates of 2012-2013 (₹ 10028118 crore) released by CSO.

2. Individual items in this document may not sum up to the totals due to rounding off.

Monetary and Credit Policy

Definitions:

- The strategy of influencing movements of the money supply and interest rates to affect output and inflation
- The actions of a central bank that determine the size and rate of growth of the money supply, which in turn affects interest rates.
- A macroeconomic policy tool used to influence interest rates, inflation, and credit availability through changes in the supply of money available in the economy
- An attempt to achieve broad economic goals by the regulation of the supply of money
- The regulation of the money supply and interest rates by a central bank in order to control inflation and stabilise currency
- Monetary policy is the process of managing a nation's money supply to achieve specific goals—such as constraining inflation, achieving full employment etc.
- Monetary policy is made by the central bank to manage money supply to achieve specific goals—such as constraining inflation, maintaining an appropriate exchange rate, generating jobs and economic growth. Monetary policy involves changing interest rates, either directly or indirectly through open market operations, setting reserve requirements, or trading in foreign exchange markets.

Monetary Policy

The use by the Central Bank of interest rate and other instruments to influence money supply to achieve certain macro economic goals is known as monetary policy. Credit policy is a part of monetary policy as it deals with how much and at what rate credit is advanced by the banks. Objectives of monetary policy are:

- accelerating growth of economy
- price stability
- exchange rate stabilization
- balancing savings and investment
- Generating employment and

Monetary policy can be expansionary or contractionary : expansionary policy increases the total supply of money in the economy as in 2008-09 all over the world including India to beat recession/slowdown; and a contractionary policy decreases the total money supply by tightening credit conditions(2010 onwards in India). Expansionary policy is traditionally used to combat unemployment in a recession by lowering interest rates, while contractionary policy has the goal of raising interest rates to control inflation.

Historically, Monetary Policy was announced twice a year - a slack season policy (April-September) and a busy season policy (October-March) in accordance with agricultural cycles. Initially, the Reserve Bank of India announced all its monetary measures twice a year in the Monetary and Credit Policy. However, since monetary Policy has become dynamic in nature, RBI reserves its right to alter it from time to time, depending on the state of the economy. Also, with the share of credit to agriculture coming down and credit towards the industry being granted whole year around, the RBI since 1998-99 has been making the policy in April. A review of the policy takes place every quarter. Within the quarter at any time, there can be changes- major and minor, depending on the need.

The tools available for the central bank to achieve the monetary policy ends are the following

- Bank rate
- Reserve ratios
- Open market operations
- Intervention in the forex market and
- Moral suasion

Bank rate

Bank Rate is the rate at which RBI lends long term to commercial banks. Bank Rate is a tool which RBI uses for managing money supply. Any revision in Bank Rate by RBI is a signal to banks to revise deposit rates as well as prime lending rate (PLR is the rate at which banks lend to the best customers. It is not in use any more.) Bank rate is in a limbo. It has no effective use. It is a penal rate. In 2011, the bank rate was aligned with the newly introduced marginal standing facility. Today it stands at 9 %(2012).Bank Rate is aligned with Marginal Standing Facility (MSF) rate, which, in turn, is linked to the policy repo rate. Alignment was because the MSF is also a penal rate. (Read ahead) . Bank rate has been replaced with repo rate as the policy rate for many years now. The Bank Rate acts as the penal rate charged on banks for shortfalls in meeting their reserve requirements (cash reserve ratio and statutory liquidity ratio). Read ahead.

Ready Forward Contracts (Repos)

Repurchase option → Repo borrowing is limited to SLR. Banks cannot borrow if their SLR is less than or equal to SLR by repo rate.

It is a transaction in which two parties agree to sell and repurchase the same security. Under such an agreement the seller sells specified securities with an agreement to repurchase the same at a mutually decided future date and a price. Similarly, the buyer purchases the securities with an agreement to resell the same to the seller on an agreed date in future at a predetermined price.

In India, RBI lends on a short term basis to banks on the security of the government bonds (repo) . Banks undertake to repurchase the security at a later date- over night or few days. RBI charges a repo rate for the money it lends. It is 7.75 % presently (2013 October)

Window for repo auctions – in morning.

Reverse repo is when RBI borrows from the market (absorbs excess liquidity) on the basis of securities and repurchases them the next day or after a few days. The rate at which it borrows is called reverse repo rate as it is the reverse of the repo operation. Reverse repo rate 100% basis points (1%) below the repo rate.

The Repo/Reverse Repo transaction can only be done at Mumbai and in securities as approved by RBI (Treasury Bills, Central/State Govt securities). RBI uses Repo and Reverse repo as instruments for liquidity adjustment in the system.

Repo rate is known as policy rate and is used as signal to the financial system to adjust their lending and borrowing operations.

MSF

4.30 pm - 6.30 pm

In 2011, RBI introduced the Marginal Standing Facility as a window through which the commercial banks can borrow from the RBI at a rate that is 1% more than the repo rate. It is meant to ease liquidity in the market. Banks can use the repo route for the securities over and above the mandatory SLR holdings- 23% of bank deposits. MSF is open to the banks that want to borrow from the RBI even if the credit is costlier by a percentage point. Totally, 2 % of the value of deposits is the limit for the MSF window for each bank. The aim is ease liquidity.

i.e. bank should have more than 23% SLR so that it can borrow from RBI.

So MSF provides window to borrow to banks SLR ≤ 23% and also if SLR > 23%

MSF is the penal rate- because the repo limit is exhausted and also because the SLR limit is breached. Bank rate is also a penal rate- for breaching the SLR and CRR limits. Therefore, there is a need to bring the bank rate on par with the MSF as was done by the RBI in 2011-12. Both stand at 8.75% today(2013 October). Thus, the gap between the Repo rate and the MSF which as a norm has to be 1% has been restored as it was widely breached in 2013 July when the MSF was kept at 3% above the Repo rate which was a policy initiative by the RBI to stem speculation on the rupee. Since relative normalcy returned on the rupee front, MSF came back to normative levels.

MSF window also has become necessary because the repo operations are limited to a specific period during the day. (auctions of repo in morning)

Net Demand & Time liability

Banks can borrow under MSF in lieu of whatever excessive SLR they have. There is no limit here. If a bank has overshot SLR limits to 28% and needs funds, it can borrow from RBI funds worth 5% (of its NDTL).

What if a bank does not have excess SLR? Can it borrow? Yes it can. Currently RBI allows banks to borrow 2% of NDTL below SLR under MSF and and funds worth 0.5% of NDTL for providing assistance to Mutual Funds. So, say a bank has 23% SLR; it can borrow funds under MSF worth 2%. When MSF became a policy measure in May-11, banks were only given the second option of borrowing in case it does not have an excess SLR. The limit was 1%. In Dec-11, Banks were given the excess SLR choice.

LAF

Liquidity Adjustment Facility (LAF) was introduced by RBI in 2000. Funds under LAF are used by the banks for their day-to-day mismatches in liquidity. LAF covers credit at repo and reverse repo rates.

Reserve Requirements

In economics, fractional-reserve banking is the near-universal practice of banks in which banks keep a fraction of the total deposits managed by a bank as reserves that are not to be lent. The reserve ratios are periodically changed by the RBI. The reserve requirement is a bank regulation, that sets the minimum reserves each bank must hold as a part of the deposits. These reserves are designed to satisfy various needs like providing loans to the Government(SLR), safety of banking operations, regulation of liquidity, management of interest rates, checking speculation and inflation management(CRR).They are in the form of RBI approved securities (SLR) kept with themselves or cash that is kept with the RBI(CRR).

Statutory liquidity ratio (SLR)

So Bank has to buy the securities and keep the money with RBI

It is the portion of time(fixed deposits) and demand liabilities(savings bank and current accounts) of banks that they should keep in the form of designated liquid assets like government securities and other RBI-approved securities like public sector bonds ; current account balances with other banks and gold .SLR aims at ensuring that the need for government funds is partly but surely met by the banks. SLR was progressively brought down from 38.5% in 1991 to 23% (2012).

TD money has been withdrawn at bulk by customers and now it's govt needs money from bank - Bank will not have money. To avoid this - there is SLR.

SLR is a blunt instrument and was unchanged for more than a decade and half till the Lehman-induced global financial and economic crisis of 2008.

The Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949 fixed the floor and cap on SLR at 25% and 40% respectively. But the amendment made in these statutes in 2007 removed the lower limit but retained the cap at 40%. RBI has, as a result, the freedom to reduce the SLR to any rate depending on the macro economic conditions. The amendment was an enabling one.

CRR

CRR is a monetary tool to regulate money supply. It is the portion of the bank deposits that a bank should keep with the RBI in cash form. CRR deposits earn no interest. The Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949 fixed the floor and cap on CRR at 3% and 20% respectively. But the amendment made in these statutes in 2007 removed the limits- lower and upper. RBI has, as a result, greater operational flexibility to make its monetary adjustments. CRR is adjusted to manage liquidity and inflation The more the CRR, the less the money available for lending by the banks to players in the

economy. CRR was 15% in 1991 and today it is 4%(2013 October) twice . If inflation is high, money supply needs to be taken out and so CRR is generally increased. But in a regime of moderate inflation, low CRR is in place.

RBI increases CRR to tighten credit and lowers CRR to expand credit. During the downturn after the global Great Recession 2008 October onwards, CRR was reduced but as growth and inflation returned since 2009, CRR was gradually increased .

CRR as a tool of monetary policy is used when there is a relatively serious need to manage credit and inflation. Otherwise, normally, RBI relies on signaling its intent through the policy rates of repo and reverse repo . Based on these rates, RBI conducts open market operations for liquidity management.

Open Market Operations Of RBI

OMOs of the RBI can be described as outright purchase and sale of government securities in the open market (open market essentially means banks and financial institutions) by the RBI in order to influence the volume of money and credit in the economy. Purchase of government securities injects money into the market and thus expands credit; sales have the opposite effect- absorb excess liquidity and shrink credit. Open market operations are RBI's most important and flexible monetary policy tool. Open market operations do not change the total stock of government securities but change the proportion held by the RBI, commercial and cooperative banks.

Selective Credit Controls

Certain businesses can be given more and certain others may get less credit from banks on the orders of the RBI. Thus, selective credit controls can be imposed for meeting various goals like discouraging hoarding and black-marketing of certain essential commodities by traders etc by giving them less credit. Either credit can be rationed or interest rate can be hiked by RBI for certain sectors as a part of SCCs. In SCCs, the total quantum of credit does not change, but the amount lent and the cost of credit may be changed for specific sector or sectors.

Moral suasion

A persuasion measure used by Central bank to influence and pressure, but not force, banks into adhering to policy. Measures used are closed-door meetings with bank directors, increased severity of inspections, discussions, appeals to community spirit etc.

Recently the RBI Governor appealed to banks not to raise rates even though the central bank was following a tight money policy.

· During 2004 ₹ got appreciated.
· So exports fell.
· So to appreciate dollar, $ was bought by printing ₹ by RBI

Market Stabilization Bonds

In 2004, RBI floated Government securities, as a part of the Market Stabilization Scheme, to absorb excess liquidity from the market. The excess liquidity is the result of RBI buying dollars from the market. (By printing more) MSS is a sterilization effort of the central bank. The normally available government securities are not enough for the RBI to suck out the huge rupee supply (printed money called base money or reserve money or high powered money) that was caused for buying dollar. Therefore, the MSS was started.

Interest rates and their significance

Interest rates are the rates offered to money that is deposited in the banks; rates offered for investment in bonds; rates at which money is borrowed from banks and financial institutions - ; and rates charged from the borrowers etc.

Savers want higher interest rate while investors want the cost of credit to be low. There has to be a balance. The determinants of interest rates are:

If on 1st Jan cost of pen is 1 Rs so due to inflation the money fetched after purchasing will be increased i.e more than 1 Rs

- Inflation- the higher the inflation, the higher the interest rates because the same money invested in commodities and other assets should not fetch more, because of the inflation:
- Need for growth :lower interest rates reduce cost of credit and facilitate investment for growth
- Promotion of savings
- Government's need to borrow: the magnitude of government's borrowing programme also determines interest rates. The more the borrowing, the higher the interest rates.
- Need to generate demand :as interest rates come down, consumer demand for credit goes up and there will be a stimulus for growth
- Global trends as we need to retain foreign funds. For example, interest rates on NRI deposits were increased in 2013 to attract their dollar deposits under the FCNR(B) swap window.(Given elsewhere)

Deregulation of Interest Rates

As a part of banking sector reforms, interest rates have been deregulated. The rationale is that banks can adjust rates quickly according to market conditions; financial innovations should be facilitated; competitive rates can be good for savers and investors; global alignment is possible more dynamically; etc. RBI however, uses repo rates and CRR adjustments to influence interest rates.

Since 2010, they are being hiked again as inflation is a worry- food inflation being even worse.

Factors affecting interest rates -
· Inflation · Govt borrowing → Fiscal deficit
· Real gross rate

Floating and Flexible Rates of Interest

There are two types of interest rate- fixed and floating. If they are offered together (when they co exist), it is called flexible interest rate regime. Floating interest rates are linked to an underlying benchmark rate. In other words, the interest rate offered `floats' in relation to the interest rate of a government security instrument of similar maturity( 5 years or 10 years maturity etc) as determined by the market. That is, floating rates of interest are basically market driven rather than `fixed'. The effective rate is adjusted on a quarterly or semi-annually or annually.

Inflation targeting

Under this policy approach the target is to keep inflation in a particular range or at a particular level. Government and the RBI agree on convergence between the fiscal and the monetary policies to achieve the common goal. RBI is given autonomy to manage inflation while the government agrees to have a fiscal policy that will contribute to price stability- for example, not borrow excessively etc. India does not follow it.

This monetary policy approach was pioneered in New Zealand. It is currently used in the Eurozone, Australia, Canada, New Zealand, Sweden, South Africa, Norway and the United Kingdom.(See Chapter on Inflation for more)

Reserve Bank of India

The central bank of the country is the Reserve Bank of India (RBI). It was established in 1935 with a share capital of Rs. 5 crores on the basis of the recommendations of the Hilton Young Commission. The share capital was entirely owned by private shareholders in the beginning. The Government held shares of nominal value of Rs. 2,20,000.

Reserve Bank of India was nationalised in the year 1949. The general superintendence and direction of the Bank is entrusted to Central Board of Directors of 20 members, the Governor and four Deputy Governors, one Government official from the Ministry of Finance, ten nominated Directors by the Government to give representation to important elements in the economic life of the country, and four nominated Directors by the Central Government to represent the four local Boards with the headquarters at Mumbai, Kolkata, Chennai and New Delhi

The Reserve Bank of India Act, 1934 came into effect in 1935. The Act provides the

Statutory basis of the functioning of the bank.

Reserve Bank of India Functions

The Reserve Bank of India Act of 1934 entrusts all the important functions of a central bank to the reserve bank of India.

Bank of issue

Under Section 22 of the Reserve Bank of India Act, the Bank has the sole right to issue bank notes of all denominations. The distribution of one rupee notes and coins and small coins all over the country is undertaken by the Reserve Bank as agent of the Government. The Reserve Bank has a separate Issue Department which is entrusted with the issue of currency notes.

RBI should maintain gold & foreign exchange reserves of Rs. 200 cr, of which Rs. 115 cr. should be in gold. However, the amount of currency that the RBI can print depends upon the need of the economy. The only restriction is the systemic one- it should not create instability with too much or too less of money supply. Money supply should have a correspondence to the goods in the economy and the rates of growth.

Banker to Government

The second important function of the Reserve Bank of India is to act as Government banker, agent and adviser. The Reserve Bank is agent of Central Government and of all State Governments in India. The Reserve Bank has the obligation to transact Government business, to receive and to make payments on behalf of the Government and to carry out their other banking operations. The Reserve Bank of India helps the Government - both the Union and the States to raise loans . The Bank makes ways and means advances to the Governments. It acts as adviser to the Government on all monetary and banking matters.

Bankers Bank and lender of the last resort.

The Reserve Bank of India acts as the bankers' bank.

The scheduled banks can borrow from the Reserve Bank of India on the basis of eligible securities by rediscounting bills of exchange. CRR deposits of banks are kept with the RBI.

Since commercial banks can always expect the Reserve Bank of India to come to their help in times of banking crises, the Reserve Bank is the lender of the last resort.

Controller of credit

The Reserve Bank of India is the controller of credit i.e. it has the power to influence the volume of credit created by banks in India. It can do so through changing the instruments available to it(see above). According to the Banking Regulation Act of 1949, the Reserve Bank of India can ask any particular bank or the whole banking system not to lend to Particular groups or persons.

The Reserve Bank of India is armed with many more powers to control the Indian money market. Every bank has to get a license from the Reserve Bank of India to do banking business within India, the license can be cancelled by the Reserve Bank of certain stipulated

conditions are not fulfilled. Every bank has to get the permission of the Reserve Bank before it can open a new branch. Each scheduled bank must send a periodical return to the Reserve Bank showing, in detail, its assets and liabilities. This power of the Bank to call for information is also intended to give it effective control of the credit system. The Reserve Bank has also the power to inspect the accounts of any commercial bank.

Agent and Adviser of the Government

The RBI acts, as the financial agent and adviser to the Government. It renders the following functions:

(a) As an agent to the Government, it accepts loans and manages public debts on behalf of the Government.

(b) It issues Government bonds, treasury bills, etc.

(c) Acts as the financial adviser to the Government in all important economic and financial matters.

Functions as National Clearing House

In India.RBI acts as the clearing house for settlement of banking transactions. This function of clearing house enables the other banks to settle their interbank claims easily. Further it facilitates the settlement economically. It essentially means the inter-bank cheque clearing settlement.

The RBI acts as a lender of last resort or emergency fund provider to the other member banks. As such, if the commercial banks are not able to get financial assistance from any other sources, then as a last resort, they can approach the RBI for the necessary financial assistance.

In such situations, the RBI provides credit facilities to the commercial banks on eligible securities including genuine trade bills which are usually made available at repo Rate/MSF.

Custodian of Foreign Reserves

The Reserve Bank of India has the responsibility to act as the custodian of India's reserve of international currencies. It takes up operations in the forex market to stabilize the exchange rate of rupee and ensure that there is no speculation and there is order. To be able to do so effectively, it holds forex reserves which it acquires from the market(purchases). It has about 282 b of forex reserves (2013 October) which includes foreign currency assets, gold and IMF's SDRs). SDRs are increasing in importance since 2008 when dollar stability came under question. Diversification and hedging of risk is being done by all central banks. Even though rupee exchange rate is market driven, RBI watches the movement to ensure order and normalcy and there is no volatility. Thus, it maintains exchange rate oversight. Mid-2013 policy action of the RBI is ample proof that RBI will not allow excessive volatility in the rupee rate. It has many levers which we will discuss in the chapter ahead on BOP.

Supervisory functions

The Reserve Bank Act, 1934, and the Banking Regulation Act, 1949 have given the RBI wide powers of supervision and control over commercial and co-operative banks, relating to licensing and establishments, branch expansion, setting reserve ratios etc. They are:

- Granting license to banks.
- Inspect and make enquiry or determine position in respect of matters under various sections of RBI and Banking Regulation Act.
- Implementation of Deposit Insurance Scheme.
- Periodical review of the work of commercial banks.
- Giving directives to commercial banks.
- Control the non- banking finance corporations.
- Ensuring the health of financial system through on-site and off-site verifications.

More such functions are given to the RBI under the **Banking Laws (Amendment)** Act **2012.**

Promotional Functions

Since Independence, the range of the Reserve Bank's functions has steadily widened. The Bank now performs a variety of developmental and promotional functions. The Reserve Bank was asked to promote banking habit, extend banking facilities to rural and semi-urban areas, and establish and promote new specialised financing agencies. Accordingly, the Reserve Bank has helped in the setting up of the IFCI and the SFC; the Industrial Development Bank of India in 1964, the Agricultural Refinance Corporation of India in 1963 and the Industrial Reconstruction Corporation of India in 1972. These institutions were set up directly or indirectly by the Reserve Bank to promote savings, and to provide industrial finance as well as agricultural finance. NABARD was set up in 1982. It has an important role in facilitating microfinance for financial inclusion. Further, its innovations include banking correspondent model for rural banking.

Functions of central bank, in sum

- monopoly on the issue of banknotes
- the Government's banker
- bankers' bank
- Lender of Last Resort
- manages the country's foreign exchange and gold reserves
- regulation and supervision of the banking industry;
- setting the official interest rate - used to manage both inflation and the country's exchange rate.

Stabilizing Economy is the Precondition for growth.

The central bank's main responsibility is the making of monetary policy to ensure a stable economy, including a stable currency. It aims to manage inflation (rising average prices) as well as deflation (falling prices). It is the lender of last resort, and assists banks in cases of financial distress (see also bank runs). (Exodus withdrawal of money)

Furthermore, it holds foreign exchange reserves and official gold reserves, and has influence over exchange rates. Some exchange rates are managed, some are market based (free float) and many are somewhere in between ("managed float" or "dirty float"). India falls in the market-determined category largely.

Typically a central bank controls certain types of short-term interest rates(repo and reverse repo rates) These influence the stock- and bond markets as well as mortgage and other interest rates.

RBI Act amended 2006

Government made amendments to RBI Act 1934 and Banking Regulation Act for allowing the apex bank to have more flexibility to fix the SLR and Cash Reserve Ratio (CRR). It removed the floor and cap on CRR and floor on statutory liquidity ratio (SLR) to provide flexibility to RBI to manage liquidity. This would result in better liquidity management in the system.

Debt management office DMO

In the late 1990's, a working group of the Reserve Bank of India first suggested the separation of its debt management and monetary policy functions of the central bank.

In keeping with global practices of the time, the group made out a case for separating the role of a bank in managing borrowings for the central and state governments, leaving the RBI to focus mainly on setting interest rates and price stability.

Although the government first announced its intention to form a new debt management office in 2007, there has been little progress. The move came appropriately at a time when the process of fiscal consolidation was well underway.

Economic growth was buoyant then and public deficit and debt indicators, too, were under control. But the Indian central bank did not appear to be fully convinced.

Since then, in the wake of the global financial crisis, there has been some rethink about the perceived benefits of a separation of public debt management from monetary policy, especially in the context of the poor state of national balance sheets.

International hard

Several committees, including the ones headed by Jehangir Aziz - who was the principal adviser to the government in the ministry of finance - Raghuram Rajan and Percy Mistry, had listed the operational efficiencies, which could be gained by having an independent debt management office.

These include eliminating a conflict of interest involving a central bank setting shortterm interest rates and selling bonds for the government; and increasing transparency.

The primary conflict, which is generally associated with a central bank managing sovereign debt relates to its inherent responsibility as the monetary authority, and its obligations as a debt manager.

It has been argued that the central bank will be biased towards a low interest regime to cut the costs of sovereign debt, at the risk of compromising its anti-inflation stance.

The Indian central bank has countered this by saying that in countries such as India, given the large size of the government borrowing programme, the sovereign debt management is much more than merely an exercise in resource-raising, as it could impact interest rates which, in turn, could have wider public policy implications.

Other arguments which have been put forward by those backing the RBI are that the size and dynamics of government borrowing programmes have a much wider influence on interest rate movements, systemic liquidity and even loan growth through the crowding out of private sector loan demand.

Besides, management of public debt, therefore, has necessarily to be seen as part of broader macroeconomic management framework involving various trade-offs.

According to them, once this is recognised, the centrality of central banks in this regard becomes quite evident and that only central banks have the requisite market pulse and instruments which an independent debt agency, driven by narrow objectives, will not be able to do.

The concern which has been flagged off is that if debt management is moved away from the RBI to DMO, which could function as an extended arm of the ministry of finance, the possibility of conflict of interest is greater as the government is the owner of the majority of banks in India.

This conflict of interest is more potent in the backdrop of banking sector continuing to be the dominant player for government market borrowing, with banks holding over 50% of outstanding government securities.

Autonomy for RBI

RBI being the architect of the monetary policy requires autonomy to be effective.Advocates of central bank independence argue that a central bank should be autonomous to manage money, credit and exchange rate dynamics in the globalizing economy. It helps check populist pressures and schemes that the political leadership may be tempted to indulge in. For example, the RBI was under pressure in 2013 from GOI to reduce rates to allow banks to lend easy to corporates and consumers to stimulate growth even as the inflation was rising. It resisted as it had autonomy.

Others believe that the elected governments should have the final say within which RBI should be autonomous both while tendering advice and also with enough discretionary powers. For example, fixing CRR and SLR as it deems fit with the amendments to the RBI Act in 2006.

Abenomics in Japan under Shinzo Abe since 2013 has been following unconventional monetary policy where huge money supply was generated to bring down the value of Yen and export and improve economy. It is a case of political priorities dictating the monetary policy.

The recent measures to make RBI independent are

- replacement of adhoc treasury bills with WMA from 1997
- FRBM Act empowers RBI with autonomy- no primary borrowing from 1-4-2006.
- RBI Act amended in 2006

The arguments in favour of autonomy are:

- monetary stability which is essential for the efficient functioning of the modern economic system can be best achieved if professional Central bankers with the long term perspective are given charge . Otherwise, political leadership may be tempted to populism
- without such autonomy, government tends to be profligate with its policies of automatic monetization
- monetary credibility is high in public perception if professionals manage it.

Profligate → extravagant or wasteful

The arguments against are:

- democratic systems are run with Parliament and Cabinet making all important policies
- monetary policy is an integral policy of the overall economic policy and so RBI has to subordinate itself to the larger objective.

The best course is to have a middle path where autonomy should be linked to performance like in the policy of 'inflation targeting' where the central bank should justify its autonomy with performance in the field of management of prices at reasonable levels.

Ways of getting
(i) FDI (ii) Exports

Money Supply

This refers to the total volume of money circulating in the economy. Money supply can be estimated as narrow or broad money.

M1 equals the sum of currency with the public and demand deposits with the banks. It is the narrow money.

M3 or the broad money , as it is also known , includes time deposits (fixed deposits), savings deposits with post office saving banks and all the components of M1.

These notions are important for the RBI to understand the demand in the economy so that it can gauge inflation, demand and so on for it to adjust the same.

Liquidity trap

A **liquidity trap** is a situation in which injections of cash into the private banking system by a central bank fail to lower interest rates and hence fail to stimulate economic growth. A liquidity trap is caused when people hoard cash because they expect an adverse event such as deflation, insufficient aggregate demand, or war. Characteristics of a liquidity trap are short-term interest rates that are near zero and fluctuations in the monetary base(printed money) that fail to translate into fluctuations in general price levels. It means, more and easy money fails to see price rise which can signal demand growth in the economy. To come out of liquidity trap, QE is attempted.

Quantitative easing

The term quantitative easing describes an unconventional form of monetary easing used to stimulate an economy. It involves the central bank to buy financial instruments which in ordinary times are not accepted for OMOs- for example, the housing market securities that were discredited in the USA since 2008. It is a step that is taken after the interest rate reduction to very low levels and similar downward adjustment of reserve ratios like CRR fail to induce any positive change. It involves printing fresh currency and de-risking lending as rates and supply of money ease to unprecedented levels. Central bank uses unconventional means, other than the usual monetary policy tools, to flood the financial system with new money through quantitative easing.

Federal Reserve of the US (its central bank like the RBI) used quantitative easing to overcome the liquidity crisis since the fall of Lehman Brothers in 2008 September when many banks went bankrupt and credit froze. It has worked as US came out of recession. It was delivered in three tranches- QWE 1,2 and 3. By the end of 2013, QE3 is under operation and may taper- wound down ,by the middle of 2014. World is worried as US dollar is a global currency and not merely a national currency. It has impact on the economies and financial markets in other countries and want to be consulted – G20 St. Petersburg summit in 2013 where Dr.Singh urged to be consulted.

FSDC

Financial Stability and Development Council is apex-level body constituted by government of India. The idea to create such a super regulatory body was first mooted by Raghuram Rajan Committee in 2008.The recent global economic meltdown has put pressure on governments and institutions across globe to regulate the financial sector towards greater stability.

The new body envisages to strengthen and institutionalise the mechanism of maintaining financial stability, financial sector development,inter-regulatory coordination along with monitoring macro-prudential regulation of economy.

Its Chairperson is the Union Finance Minister of India

Members are :

- Governor Reserve Bank of India (RBI),
- Finance Secretary and/ or Secretary, Department of Economic Affairs (DEA),
- Secretary, Department of Financial Services (DFS),
- Chief Economic Advisor, Ministry of Finance,
- Chairman, Securities and Exchange Board of India (SEBI),
- Chairman, Insurance Regulatory and Development Authority (IRDA),
- Chairman Pension Fund Regulatory and Development Authority (PFRDA),
- Joint Secretary (Capital Markets), DEA, will be the Secretary of the Council,
- The Chairperson may invite any person whose presence is deemed necessary for any of its meeting(s).

Responsibilities

- Financial Stability
- Financial Sector Development
- Inter-Regulatory Coordination
- Financial Literacy
- Financial Inclusion
- Macro prudential supervision of the economy including the functioning of large financial conglomerates
- Coordinating India's international interface with financial sector bodies like the Financial Action Task Force (FATF), Financial Stability Board (FSB)and any such body as may be decided by the Finance Minister from time to time.

Macro prudential analysis is a method of economic analysis that evaluates the health, soundness and vulnerabilities of a financial system. Macro prudential analysis looks at the health of the underlying financial institutions in the system and performs stress tests(simulate financial crises and check impact on the banks and other financial institutions) and scenario analysis to help determine the system's sensitivity to economic shocks.

In October 2013, FSDC met in the context of rupee crisis and the global factors. The government decided to reach out to sovereign wealth funds to minimise the impact of US Federal Reserve's tapering of quantitative easing on Indian markets. FM asked the financial sector regulators to take preventive steps before stimulus rollback starts early 2014.□□At the eighth meeting of the Financial Stability and Development Council (FSDC), Chidambaram emphasized the opportunity available due to the postponement of the reversal of the monetary policies in the United States should be utilized to further address the macroeconomic imbalances. Withdrawal of the $85 billion-a-month bond buying programme by the US, which would lead to outflow of funds from emerging markets, was deferred by the Federal Reserve in September 2013.

Sovereign bond -
Bond issued outside country to raise foreign currency.

Quasi/semi sovereign bond -
PSU issue bonds outside on the gurantee of GOI.

Sovereign wealth fund -
- Acquiring resources around world.

Rediscounting of bill -
- Using bill for second time

Capital flight -
- Enmass leaving of currency from country
- Foreign investors selling assets & converting ₹ into $.

Money Market and Capital Market in India: Instruments and Details

Part-1

Money market can be defined as a market for short-term funds with maturities ranging from overnight to one year and includes financial instruments that are considered to be close substitutes of money. Money market transactions could be both secured and unsecured, i.e., without collaterals as we will see ahead.

Money market covers sources of finance - lending and borrowing short term funds- funds with a maturity of less than one year. Banks and financial institutions(IDBI, LIC etc) individuals, mutual funds, companies and government are the main lenders and borrowers. The informal market operates through small-scale money-lenders as well as others outside the RBI control.

Money market instruments broadly are: call money; bill market (both commercial bills and treasury bills) Certificates of Deposit(CD); Commercial paper(CP).

Call Money

Call/Notice money is money borrowed or lent for a very short period. If the period is more than one day and up to 14 days it is called 'Notice money' otherwise the amount is known as Call money'. No collateral security is required to cover these transactions and good will and reputation are the basis apart from the documents like promissory notes. The call market enables the banks and institutions to even out their day to day deficits and surpluses of money.

Commercial banks, Co-operative Banks, mutual funds, primary dealers and others are allowed to borrow and lend in this market Interest rates in the call and notice money market are market determined. A **primary dealer** is a firm that buys government securities directly from a government, with the intention of reselling them to others, thus acting as a market maker of government securities. The government may regulate the behavior and numbers of Its primary dealers and impose conditions of entry.

Treasury Bills (Issued by ~~RB~~ GOI & auctioned by RBI)

Treasury bills are short-term money market instruments, which are issued by the RBI on behalf of the GOI. The GOI uses these funds to meet its short-term financial requirements of the government. T-Bills are sovereign zero risk instruments. They are available in primary and secondary market; issued at a discount to face value i.e., investors may buy the T-bill at discount to face value of Rs.100 and on maturity the face value of Rs.100 is received by the investor.

Treasury bills (T-bills) offer short-term investment opportunities. They are thus useful in managing short-term liquidity. At present, the Government of India, through the RBI, issues three types of treasury bills through auctions, namely, 91-day, 182-day and 364-day. There are no treasury bills issued by State Governments.
Treasury bills are also issued under the Market Stabilization Scheme (MSS).

While 91-day T-bills are auctioned every week on Wednesdays, 182-day and 364-day T-bills are auctioned every alternate week on Wednesdays.
Treasury bills are available for a minimum amount of Rs.25,000 and in multiples of Rs. 25,000. Treasury bills are issued at a discount and are redeemed at par.
Treasury bills are zero coupon securities and pay no interest. They are issued at a discount and redeemed at the face value at maturity. For example, a 91 day Treasury bill of Rs.100/- (face value) may be issued at say Rs. 98.20, that is, at a discount of say, Rs.1.80 and would be redeemed at the face value of Rs.100/-. The return to the investors is the difference between the maturity value or the face value (that is Rs.100) and the issue price.
A considerable part of the government's borrowings takes place through T bills of various maturities. The usual investors in these instruments are banks, insurance companies and FIs.

Cash Management Bills (CMBs) (2010)

Government of India, in consultation with the Reserve Bank of India, has decided to issue a new short-term instrument, known as Cash Management Bills (CMBs), to meet the temporary mismatches in the cash flow of the Government. The CMBs have the generic character of T-bills but are issued for maturities less than 91 days. Like T-bills, they are also issued at a discount and redeemed at face value at maturity.

Inter Bank Term Money

Inter bank market for deposits of maturity beyond 14 days and upto three months is referred to as the term money market.

Certificates Of Deposit

After treasury bills, the next lowest risk category investment option is the certificate of deposit (CD) issued by scheduled commercial banks and FIs. Regional rural banks and Local area banks can not issue CDs.

CD is a negotiable promissory note, secure and short term (up to a year) in nature. A CD is issued at a discount to the face value, the discount rate being negotiated between the issuer and the investor. CDs can be issued by scheduled commercial banks and select all-India Financial Institutions. Minimum amount of a CD should be Rs.1 lakh The maturity period of CDs issued by banks should be not less than 15 days and not more than one year. The FIs can issue CDs for a period not less than 1 year and not exceeding 3 years from the date of issue. CDs can be issued to individuals or firms.

→ Govt Securities
· CBM, T Bill & bond for more than 1 year.

Inter Corporate Deposits Market

Apart from CPs, corporates also have access to another market called the inter corporate deposits (ICD) market. An ICD is an unsecured loan extended by one corporate to another. Existing mainly as an avenue for low rated corporates, this market allows fund- surplus Corporate to lend to other corporates.

Commercial Paper

It represents short term unsecured promissory notes issued by top rated corporates, primary dealers(PDs),satellite dealers(SDs) and the all-India financial institutions(FIs).
CP can be issued for maturities between a minimum of 7 days and a maximum of up to one year from the date of issue. However, the maturity date of the CP should not go beyond the date up to which the credit rating of the issuer is valid.CP can be issued in denominations of Rs.5 lakh or multiples thereof.

The main features of these papers are

- corporates having tangible net worth of not less than Rs.4 crore can issue them
- All CPs require credit rating from a credit rating agency Minimum amount invested by single investor is Rs.five lakh or multiple thereof.
- CPs are issued at a discount to face value.

Ready Forward Contracts (Repos)

See chapter on Monetary policy.

Commercial Bills

Bills of exchange are negotiable instruments drawn by the seller (drawer) of the goods on the buyer (drawee) of the goods for the value of the goods delivered. These bills are called trade bills. These trade bills are called commercial bills when they are accepted by commercial banks. If the bill is payable at a future date and the seller needs money immediately, he may approach his bank for discounting the bill.

Discount and Finance House of India (DFHI)

Set up in 1988 by RBI to strengthen the bill market. It has been established to deal in money market instruments in order to provide liquidity. Thus the task assigned to DFHI is to develop a secondary market in the existing money market instruments.The main objective of DFHI is to facilitate the smoothening of the short term liquidity imbalances by developing an active money market and integrating the various segments of the money market.
At preset DFHI's activities are restricted to:
1. Dealing in Treasury Bills
2. Re-discounting short term commercial bills.
3. Participating in the inert bank call money, notice money and term deposits and
4. Dealing in Commercial Paper and Certificate of deposits.
5. Government dated Securities

Libor

The London Interbank Offered Rate is the average interest rate estimated by leading banks in London that they would be charged if borrowing from other banks. It is usually abbreviated to BBA Libor (for British Bankers' Association Libor). It is the primary benchmark, along with the Euribor, for short term interest rates around the world.

Many financial institutions, mortgage lenders and credit card agencies set their own rates relative to it. At least $350 trillion in derivatives and other financial products are tied to the Libor.

Mibor - Mumbai Inter-Bank Offer Rate

The Committee for the Development of the Debt Market that had studied and recommended the modalities for the development for a benchmark rate for the call money market. Accordingly, NSE had developed and launched the NSE Mumbai Inter-bank Bid Rate (MIBID) and NSE Mumbai Inter-bank Offer Rate (MIBOR) for the overnight money market in 1998. The **MIBID/MIBOR** rate is used as a bench mark rate for majority of deals.

Money market reforms

The recommendations of the Sukhmoy Chakravarty Committee on the Review of the Working of the monetary system, and the Narasimham Committee Report on the Working of the Financial System in India, 1991, The Reserve Bank of India initiated a series of money market reforms basically directed towards the efficient discharge of its objectives.

Reforms made in the Indian Money Market are:- Deregulation of the Interest Rate ; Money Market Mutual Fund (MMMFs) are allowed to sell units to corporate and individuals. The Discount and Finance House of India (DFHI) was set up in April 1988 to impart liquidity in the money market. It was set up jointly by the RBI, Public sector Banks and Financial Institutions. DFHI has played an important role in stabilizing the Indian money market. Liquidity Adjustment Facility (LAF) - Through the LAF, the RBI remains in the money market on a continue basis through the repo transaction. LAF adjusts liquidity in the market through absorption and or injection of financial resources. In order to impart transparency and efficiency in the money market transaction the electronic dealing system has been started. It covers all deals in the money market. Similarly it is useful for the RBI to watchdog the money market. Establishment of the CCIL: The Clearing Corporation of India limited (CCIL) was set up in April 2001. Development of New Market Instruments like CMBs.

Money Market and Capital Market in India: Instruments and Details: Part-2

Capital Market

It refers to market for funds with a maturity of 1 year and above, refered to as term funds that include medium and long term funds. The demand for these funds comes from both the government for its investtment purposes and also the private sector. Banks, public financial institutions like LIC and GIC; development financial institutions like ICICI, IDBI etc; mutual funds like UTI are the main participants in the market.The elements of the capital market in India are the following:

Government securities,industrial securities that include the shares and debentures of Indian companies- both the primary and secondary market(please refer to the section on stock market) DFIs(IFCI, IDBI, State Financial Corporations(SFCs);UTI, ICICI(private sector) Financial intermediaries: merchant banks; mutual funds;leasing companies; venture capital companies;and others.

G-Secs (Gift edged securities)

A Government security is a tradable instrument issued by the Central Government or the State Governments. It acknowledges the Government's debt obligation. Such securities are short term (usually called treasury bills or Cash Management Bills with original maturities of less than one year) or long term (usually called Government bonds or dated securities with original maturity of one year or more). In India, the Central Government issues both, treasury bills and bonds or dated securities while the State Governments issue only bonds or dated securities, which are called the State Development Loans (SDLs). Government securities carry practically no risk of default and, hence, are called risk-free gilt-edged instruments. Government of India also issues savings instruments (Savings Bonds, National Saving Certificates (NSCs), etc.) or special securities (oil bonds, Food Corporation of India bonds, fertiliser bonds, power bonds, etc.). They are, usually not fully tradable and are, therefore, not eligible to be SLR securities.

Dated Government securities are long term securities and carry a fixed or floating coupon (interest rate) which is paid on the face value, payable at fixed time periods (usually half-yearly). The tenor of dated securities can be up to 30 years.

The G-Sec instrument is in the nature of a bond.

GOI Dated Security can be held by any person, firm, company, corporate body or institution, State Governments, Provident Funds and Trusts. Non-Resident Indians (NRIs, viz., Indian citizens and Individuals of Indian origin), Overseas corporate bodies predominantly owned by NRIs and Foreign Institutional Investors registered with SEBI and approved by Reserve

Bank of India are also eligible to invest in the government stock. G-Sec are issued both in demat and physical form.

The minimum investment in G-Secs is Rs 10,000. G-Secs could be of the following types:

- Dated Securities: They have fixed maturity and fixed coupon rates payable half yearly and are identified by their year of maturity.

- **Floating Rate Bonds:**

  They are bonds with variable interest rates with a fixed percentage over a benchmark rate. There may also be a cap and a floor rate attached, thereby fixing a maximum and minimum interest rate payable on it.

- Capital Indexed Bonds: They are bonds where the interest rate is a fixed percentage over the wholesale price index or CPI.

IIB Inflation Indexed Bonds

- Capital Index Bond (CIB), 2002 was issued in 1997 where only principal repayments at the time of redemption were indexed to inflation. A new version of IIB has been designed with protection from inflation to both interest payments and principal repayments linking them to Wholesale Price Index (WPI) by the RBI and may be issued (2013).

New principal amount = $\frac{\text{inflation index (prevailing)}}{\text{inflation index during deposit}}$ × Principal

2012 reforms in G-Secs

The existing limit for investment by Securities and Exchange Board of India (SEBI) registered foreign institutional investors (FIIs) in Government securities (G-Secs) has been enhanced to $30 billion.(2013) and it may be further relaxed.

RBI has decided to allow long term investors like Sovereign Wealth Funds (SWFs), multilateral agencies, endowment funds, insurance funds, pension funds and foreign central banks to be registered with SEBI, to also invest in G-Secs.FII debt is rupee debt and so is welcome.

SDL

State Governments also raise loans from the market. SDLs are dated securities issued through an auction similar to the auctions conducted for dated securities issued by the Central Government. Interest is serviced at half-yearly intervals and the principal is repaid on the maturity date. Like dated securities issued by the Central Government, SDLs issued by the State Governments qualify for SLR. They are also eligible as collaterals for borrowing through market repo as well as borrowing by eligible entities from the RBI under the Liquidity Adjustment Facility (LAF).

DFIs or Development Banks

Financial institutions assume a critical role in the provision of long term credit, especially in the absence of a well-developed long-term debt market. The financial institutions could be categorised into three broad heads, viz., all-India financial institutions (AIFIs), state-level institutions and other institutions. Of the three categories, AIFIs are the most dominant in terms of assets and range of operations.

The major AIFIs are the Industrial Development Bank of India (IDBI), IFCI Ltd., Industrial Investment Bank of India Ltd. (IIBI), Small Industries Development Bank of India (SIDBI), National Housing Bank (NHB), National Bank for Agriculture and Rural Development (NABARD), Export Import Bank of India (EXIM Bank), Tourism Finance Corporation of India Ltd. (TFCI), Unit Trust of India (UTI), Life Insurance Corporation of India (LIC), General Insurance Corporation of India (GIC) and its subsidiaries and Infrastructure Development Finance Company of India Ltd. (IDFC). All these institutions operate on all-India basis. Other institutions comprise Export Credit and Guarantee Corporation (ECGC) and Deposit Insurance and Credit Guarantee Corporation (DICGC).

The state level institutions consist of state financial corporations (SFCs) and state industrial development corporations (SIDCs).

Merchant Banks / Investment Banks

Underwriting means one could buy shares if not bought by others

MBs are those who manage and underwrite (Underwriting an issue means to guarantee to purchase any shares in a new issue or rights issue not fully subscribed by the public.) new public issues floated by companies to raise funds from public. They advise corporate clients on fund raising. They are also called investment banks (I banks) .They deal only with corporates and not general public, essentially.

Lehman Brothers was a global financial services firm. Before declaring bankruptcy in 2008, Lehman was the fourth-largest investment bank in the US (behind Goldman Sachs, Morgan Stanley, and Merrill Lynch), doing business in investment banking, equity ,trading (especially U.S. Treasury securities), research, investment management, private equity and private banking.

On September 15, 2008, the firm filed for Chapter 11 bankruptcy protection following the massive exodus of most of its clients, drastic losses in its stock, and devaluation of its assets by credit rating agencies.

Collective investment schemes

For the last few years, the Securities Exchange Board of India (Sebi) has been coming down hard on companies running collective investment schemes (CIS). These schemes, much in the news since the Saradha scam(2013), are those in which people invest to create a pool of money which is then utilised to realise some income for the investors, or acquire some produce, or some properties which are then looked after by a manager on behalf of the investors. In other words a property is owned by an individual, but is maintained jointly with the manager. A mutual fund is also called a collective investment scheme. SEBI introduced regulations for CISs in 1999. In 2013, they are further rendered more stringent.

Tightening the controls on entities running illegal collective investment schemes (CIS), in September 2013, the Securities and Exchange Board of India (Sebi) has notified new norms to classify such activities as frauds and impose penalties of up to three times of their profits.

Besides, the new rules expand the list of activities to be covered under fraudulent and unfair trade practices to hold individuals as well as companies equally guilty for manipulations.

The amendments have been made to Sebi's 'prevention of fraudulent and unfair trade practices' (PFUTP) regulations.
In the backdrop of Sahara / Sharada scams, SEBI modified the definition of CIS to include any scheme / arrangment floated by any person (instead of a company as was defined earlier); and any such scheme with corpus of more than Rs. 100 Crore shall also be deemed to be a CIS by SEBI.

Alternative Investment Funds

AIFs is a newly created class of pooled-in investment vehicles for real estate, private equity and hedge funds. The AIFs have been divided into three categories. The Category I AIFs include those investing in start-ups, social ventures, SMEs, infrastructure or other areas that can get government incentives for being 'socially or economically desirable'. The Category II AIFs include private equity funds and debt funds which do not get any incentives or concessions from the government and do not undertake leverage or borrowing other than to meet day-today operational requirements. The Category III includes hedge funds or funds which trade with a view to make short-term returns.
Angels are the new category introduced in September 2013. (Read ahead)
AIFs are basically funds established or incorporated in India for the purpose of pooling in capital from Indian and foreign investors for investing as per a pre-decided policy. Sebi regulates them. it excludes Mutual funds or collective investment Schemes, family trusts, Employee Stock Option etc.

Mutual Funds

Mutual funds raise money from public and invest them in stock market securities; bonds etc.Mutual funds were virtually synonymous with the Unit Trust of India(UTI) till two decades ago when India witnessed financial sector liberalization and many more public sector and private mutual funds came up. SEBI regulates mutual funds.

Hedge fund

Hedge fund is an MF though it is limited to few; non-transparent and is not fully regulated. The investment styles of the HFs are also criticised as they are not safe and aim at fast returns thus creating volatility in the markets. SEBI does not allow them. To sum up and explain: A hedge fund is a pooled investment vehicle administered by a professional management firm. Hedge funds invest in a diverse range of markets and use a wide variety of investment styles and financial instruments.The name "hedge fund" refers to the hedging techniques traditionally used by hedge funds, but hedge funds today do not necessarily hedge. Hedge funds are made available only to certain investors and cannot be offered or sold to the general public. As such, they generally avoid direct regulatory oversight, bypass licensing requirements applicable to investment companies, and operate with greater flexibility than mutual funds and other investment funds. They are a form of AIFs.

Venture Capital

Invests public money

Venture capital is money provided by financial institutions who invest alongside management in young, rapidly growing companies that have the potential to develop into significant economic contributors. Venture capital is an important source of equity for start-up companies.

Angel Investors

An angel investor or angel (also known as a business angel or informal investor) is an affluent individual who provides capital for a business start-up, usually in exchange for convertible debt or ownership equity. They invest their own money unlike a venture capitalist who invests public money. They became popular in recent years after the web-based enterprises came up in the 1990's.
With an aim to encourage entrepreneurship in the country by financing small start-ups, market regulator Sebi in September 2013 notified new norms for angel investors, who provide funding to companies at their initial stages.

Angel investors are allowed to be registered as Alternative Investment Funds (AIFs) -- a newly created class of pooled-in investment vehicles for real estate, private equity and hedge funds.

In order to ensure investment by angel funds is genuine, the Securities and Exchange Board of India (Sebi) has restricted investment by such funds between Rs 50 lakh and Rs 5 crore.

Among other norms included, angel funds can make investments only in those companies which are incorporated in India. These funds need to be invested in a firm for at least three years, can invest in companies not older than 3 years.

Angel funds are required to have a a corpus of at least Rs 10 crore and minimum investment by an investor should be Rs 25 lakh.

The regulator also stipulated that the fund must not have any family connection with the investee company.

The new norms would help in encouraging entrepreneurship in the country by financing small start-ups at a stage where such start-up finds it difficult to obtain funds from traditional sources of funding such as banks, financial institutions among others.

Finance Minister P Chidambaram in his budget speech had announced that Sebi would frame guidelines for angel investor pools by which they can be registered under AIF venture capital funds (VCF).

Under Sebi guidelines, AIFs already have sub-categories such as Venture Capital Funds, Social Funds and SME Funds. Angel fund is likely to be a separate sub-category.

Regarding raising of funds by an individual investor, the person need to have an experience of 10 years and should possess assets of at least Rs 2 crore.

Hundi

Hundis were legal financial instruments that evolved in India. These were used in trade and credit transactions; they were used as remittance instruments for the purpose of transfer of funds from one place to another. In the era of bygone kings and the British Raj these Hundis served as Travellers Cheques. They were also used as credit instruments for borrowing and as bills of exchange for trade transactions.

Technically, a Hundi is an unconditional order in writing made by a person directing another to pay a certain sum of money to a person named in the order. Being a part of an informal system, hundis now have no legal status and were not covered under the Negotiable Instruments Act, 1881. They were mostly used as cheques by indigenous bankers.

Chit funds :-

Saradha Group run as a collective investment scheme (CIS), which is regulated by the Securities and Exchange Board of India, collapsed and caused severe losses to many people.

There are various such financial schemes such as chit funds, multi-level marketing schemes or ponzi schemes which are all different from one another.

In simple terms, a chit fund is an arrangement that a group of people arrive at to contribute money in a defined manner at periodic intervals into a pool or a kitty. During the process of collection, any member can draw a lump sum through various ways like a lucky draw, an auction or a member can even fix a payout date based on a known expenditure.

These schemes are very popular in tier II and III towns in India and even in rural India, thanks to under-penetration of banking services, as they are a way of raising quick money or catering for sudden liquidity needs or even a planned expenditure. Also, banks haven't recognised the fact that the common man with a small income finds it very difficult to undergo the entire procedure of getting a loan, adjusting to bank working hours and other demands.

There are many organised companies incorporated to do this as a business and these are governed by state or central laws. There is a central Chit Funds Act of 1982, apart from a number of state chit fund Acts. There is an office of "registrar of chit funds" in every state that monitors operations which are quite stringent. Utilisation and appropriation of subscribers money is strictly prohibited.

The first step of regulation comes at the state level; hence it's the state government which is responsible for any fraudulent activities by chit fund companies.

QIPs

The QIP Scheme is open to investments made by "Qualified Institutional Placement " (which includes public financial institutions, mutual funds, foreign institutional investors, venture capital funds and foreign venture capital funds registered with the SEBI) in any issue of equity shares/ fully convertible debentures/ partly convertible debentures or any securities which are convertible into or exchangeable with equity shares at a later date (Securities).

Since the beginning of 2009, Indian companies are raising billions of dollars from the QIP route.

NBFC

A company is treated as an NBFC if its financial assets are more than 50% of total assets and income from financial assets is more than 50% of the gross income

NBFC means Non-banking financial company. A non-banking financial company (NBFC) is

a company registered under the Companies Act, 1956 and is engaged in the business of loans and advances, housing finance, acquisition of shares/stock/bonds/debentures/securities issued by government or local authority or other securities of like marketable nature, leasing, hire-purchase, insurance business, chit business, but does not include any institution whose principal business is that of agriculture activity, industrial activity, ale/purchase/construction of immovable property. NBFCs are similar to banks; however they do not accept demand deposits.

Some microfinance companies are registered as NBFCs and are regulated by the RBI while other MFIs are either registered as money lenders or Societies.
The Reserve Bank of India (RBI) in 2011 approved creation of a separate category of non-banking financial companies for the MFI sector and specified that such institutions need to have a minimum net owned fund of Rs 5 crore.

An RBI-appointed panel headed by Y H Malegam had recommended setting up of a special category of NBFCs operating in the micro finance sector in 2011.These are called Non Banking Financial Company-Micro Finance Institution(NBFC-MFI)..

NBFC factor

The Reserve Bank of India (RBI) in mid-2012 introduced a new category called Non-Banking Financial Company-Factors. Under this new class, a company has to seek registration from the regulator with a minimum net owned fund (capital + reserve) of Rs 5 crore.Thus, Factoring is the business of selling invoices (receivables) to a factoring company (Factor) at a discount . Consequently, the selling corporate can get cash quickly and avoid risk of collecting debt. In India, it is still at a nascent stage. So far, there are around 10 'factors' including SBI Factors and Commercial Services, Canbank Factors, HSBC Factoring and others. Out of all factors, seven or eight companies are on standalone basis. Factoring can be of two types: domestic and export oriented, the latter being called forfaiting. Forfaiting is the purchasing of an exporter's receivables (the amount importers owe the exporter) at a discount by paying cash. The forfaiter, the purchaser of the receivables, becomes the entity to Whom the importer is obliged to pay its debt.

RBI measure will help expand the factoring industry in India.Earlier in January, 2012; the Parliament had passed a bill on the Factoring Regulations Act, 2011 wherein similar proposal were mentioned. The RBI directives came in line with that.

The factoring mechanism mostly assists smaller companies, which run relatively shorter fund flow cycle. Factoring bails them out by supporting their fund system instantly.

ECBs

ECB (External Commercial Borrowings) is an instrument used to facilitate the access to foreign money by Indian corporations and PSUs (Public Sector Undertakings). ECBs include commercial bank loans, buyers' credit, credit from official export credit agencies and commercial borrowings from the private sector window of Multilateral Financial Institutions such as International Finance Corporation (Washington), ADB and Investment by

ECB funds into equity

Foreign Institutional Investors (FIIs) in dedicated debt funds. ECBs cannot be used for investment in stock market or speculation in real estate. The DEA(Department of Economic Affairs), Ministry of Finance, Government of India along with Reserve Bank of India, monitors and regulates ECB guidelines and policies. In India, External Commercial Borrowings are being permitted by the Government for providing an additional source of funds to Indian corporates and PSUs for financing expansion of existing capacity and as well as for fresh investment, to augment the resources available domestically. ECBs can be used for any purpose (rupee-related expenditure as well as imports) except for investment in stock Market and speculation in real estate.

augment- add to

Applicants are free to raise ECB from any internationally recognised source like banks, export credit agencies, suppliers of equipment, international capital markets etc.

heavy rain

ECB access may be restricted when the there is a deluge of foreign inflows and the rupee is getting strong. It may be relaxed when the opposite happens as we have seen since 2009. ECBs help diversify risk for the companies. Also, the interest rates are softer abroad. They help Indian companies with foreign funds.

Country benefits as it has access to forex.

ECBs can be raised through two routes : Automatic Route and the Approval Route. The former does not require permit from the Regulator whereas the latter requires the same. RBI policy allows corporates registered under the Companies Act, 1956, except financial intermediaries such as banks, financial institutions (FIs), housing finance companies and Non-Banking Finance Companies (NBFCs) to access ECBs. However, in September 2013, 23rd Governor of RBI Raghuram rajan allowed banks to borrow from abroad to meet their Tier 1 requirements of capital(Basel norms will, to be covered later).
NGOs engaged in micro-finance activities have been permitted to raise ECB up to certain limits.

Financial institutions dealing exclusively with infrastructure or export finance such as IDFC, IL&FS, Power Finance Corporation, Power Trading Corporation, IRCON and EXIM Bank are considered on a case-by-case basis.

The priority end use of ECBs includes investment (such as import of capital goods, new projects, modernization/expansion of existing production units) in real sector - industrial sector including small and medium enterprises (SME) and infrastructure sector, power exploration, telecom, railways, roads & bridges, ports and exports.

RBI in June 2012 decided to allow Indian companies to avail of ECBs for repayment, within limits, of Rupee loan(s) availed of from the domestic banking system .Only companies in the manufacturing and infrastructure sector will be eligible to avail of such ECBs.
Policy helps source loans cheap;domesric liquidity constraints are softened;country gets forex;rupee slide could be contained;infrastructure benefits.

Euro issues

Indian companies are permitted to raise foreign currency resources through issue of Foreign Currency Convertible Bonds (FCCBs), ordinary equity shares through Global Depository Receipts (GDRs) to foreign investors i.e. institutional investors or individuals (including NRIs) residing abroad. That is, Euro-issues include Euro-convertible bonds and GDRs.

Private equity

In finance, private equity means equity in companies that is privately placed by the management to a finance firm. It generally has a lock in period during which they are not publicly traded on a stock exchange. Bulk private placement is done.Private equity firm also is given a place in the management of the company . Capital for private equity is raised primarily from institutional investors. The term private equity has different connotations in different countries.

Stock Market (Given as a separate chapter)

Apart from the above mentioned sources of capital for Indian companies from within the country, the International Finance Corporation (IFC) of the World Bank (WB) also provides funds for the private sector. (Given in the chapter on Bretton Woods institutions).

Credit Default Swap

It is a form of insurance against debt default. When an investor buys corporate (or government) bonds he/she faces the risks of default on part of the issuing agent. The investor can insure its investment in such bonds against default through a third party. The investor pays a premium to the party providing insurance. In the event of default by the bond issuer, the insurer would step in and pay the investor. A CDS is just like insurance, which is bought by those who fear default.

Corporate debt

Corporate debt is necessary for their investment, acqusitions etc.

The following are some of the different types of corporate debt securities issued:

Non-Convertible Debentures

Partly- Convertible Debentures

Fully-Convertible Debentures (Convertible into Equity shares)

Bonds

IDF

IDFs are investment vehicles which can be sponsored by commercial banks and NBFCs in India in which domestic/offshore institutional investors, specially insurance and pension funds can invest through units and bonds issued by the IDFs. Infrastructure Debt Funds (IDFs), can be set up either as a Trust or as a Company. A trust based IDF would normally be a Mutual Fund (MF), regulated by SEBI, while a company based IDF would normally be a NBFC regulated by the Reserve Bank.IDF-MFs can be sponsored by banks and NBFCs. Only banks and Infrastructure Finance companies can sponsor IDF-NBFCs. "Sponsorship" means equity participation up to a certain permissible level.

FCCBs (see elsewhere in this chapter)

Bonds are issued to domestic and foreign investors. They are traded on the stock market.

FIIs investment in debt

FIIs can invest in government and corporate debt- primary and secondary market. These limits and the rules are relaxed from time to time depending on the needs of the economy.FII debt is rupee debt.

Take-out financing

It came into effect in 2010. It is a method of providing finance for longer duration projects (for example, 15 years) by banks by sanctioning medium term loans (like 5-7 years). It is the understanding that the loan will be taken out of books of the financing bank within pre-fixed period, by another institution thus preventing any possible asset-liability mismatch.

Under this process, the institutions engaged in long term financing such as IDFC, agree to take out the loan from books of the banks financing such projects after the fixed time period when the project reaches certain previously defined milestones. On the basis of such understanding, the bank concerned agrees to provide a medium term loan, say 5 years. At the end of five years, the bank could sell the loans to the institution and get it off its books. This ensures that the project gets long-term funding though various participants. Banks otherwise cannot lend for infrastructure as their deposits are for a short period and the loans are for a long period- asset liability mismatch.

External sources of financer for India

a. Stock market(partly touched above under Euro issues) like ADRs and GDRs

b. FCCB

c. ECB

d. IBRD and IFC

e. Private equity

f. Bilateral loans by Governments abroad

IFC rupee bond

International investors subscribed to the first ever global rupee bond, setting aside worries about rupee depreciation and other macroeconomic concerns. The first tranche of International Finance Corporation's (IFC) rupee bond saw unprecedented demand from global pension funds, banks, asset management companies and central banks.

The response to the first offshore rupee bond also paves the way for Indian corporates to raise cheaper funds as the currency risk will be borne by the investor.

The bond with a tenor of three years has a coupon of 7.75%, lower than the current G-sec reference rate by 70 basis points.

IFC, which has already raised local currency bonds in Chinese renminbi, Russia's rouble and Brazilian real, proposes to use these funds to finance private sector investment in India.

Internationalisation of rupee(in the class)

Coupon – The interest rate stated on a bond when it's issued.
or
Coupon rate
or
Coupon percent rate

Stock Market
India and General

A stock exchange is an organization which provides a platform for trading shares- either physical or virtual. The origin of the stock market dates back to the year 1494, when the Amsterdam Stock Exchange was first set up. In a stock exchange, investors through stock brokers buy and sell shares in a wide range of listed companies. A given company may list in one or more exchanges by meeting and maintaining the listing requirements of the stock exchange.

In financial terminology, stock is the capital raised by a corporation, through the issuance and sale of shares. In common parlance, however, stocks and shares are used interchangeably .A shareholder is any person or organization which owns one or more shares issued by a corporation. The aggregate value of a corporation's issued shares , at current market prices, is its market capitalization. Stock broker buys and sells for an investor and does the work of arranging the transfer of stock from a seller to a buyer.

Importance of Stock Exchanges

- For efficient working of the economy and for the smooth functioning of the corporate form of organization, the stock exchange is an essential institution.
- an efficient medium for raising long term resources for business
- Help raise savings from the general public by the way of issue of equity / debt capital
- attract foreign currency
- exercise discipline on companies and make them profitable
- investment in backward regions for job generation
- another vehicle for investors' savings

Stock Exchanges in India

The first company that issued shares was the VOC or Dutch East India Company in the early 17th century (1602). Since then we have come a long way.With over 25m shareholders today, India has the third largest investor base in the world after the USA and Japan. Over 9,000 companies are listed on the stock exchanges, which are serviced by approximately 7,500 stockbrokers. The Indian capital market is significant in terms of the degree of development, volume of trading and its tremendous growth potential.

Stock exchanges provide an organised market for transactions in securities and other securities. There are 25 stock exchanges in the country, 21 of them being regional ones with allocated areas. BSE, National Stock Exchange (NSE), the Over the Counter Exchange of India Limited (OTCEI) , MCX-SX, USE and Inter-connected Stock Exchange of India Limited (ISE) are the pan Indian stock exchanges(read ahead). Important Stock Exchanges in India are Bombay Stock Exchange, popularly known as BSE and National Stock Exchange located in Bombay. MCX-SX began equity trading in 2013. MCX,-SX is a joint venture

between Financial Technologies India (FTIL) and Multi Commodity Stock Exchange (MCX).

Stock Exchanges in India

1. Ludhiana	2. New Delhi	3. Jaipur	4. Meerut
5. Ahmedabad	6. Rajkot	7. Indore	8. Vadodara
9. Bombay	10. Pune	11. Hyderabad	12. Mangalore
13.Bangalore	14. Ernakulam	15. Coimbatore	16. Madras
17. Patna	18. Kanpur	19. Bhubaneshwar	20. Calcutta
21. Guwahati			

National Stock Exchange (NSE)

It is stock exchange located in Mumbai, India. National Stock Exchange (NSE) was established in 1992 and starts trading in 1993. It was recognised as a stock exchange in 1993. NSE has played a critical role in reforming the Indian securities market and in bringing transparency, efficiency and market integrity.

NSE has a market capitalisation of more than US$ 1 trillion 989 and 1,635 companies listed as on July 2013. Though a number of other exchanges exist, NSE and the Bombay Stock Exchange are the two most significant stock exchanges in India, and between them are responsible for the vast majority of share transactions. NSE's flagship index, the **CNX NIFTY 50**, is used extensively by investors in India and around the world to take exposure to the Indian equities market.

There are many domestic and global institutions and companies that hold stake in the exchange. Some of the domestic investors include LIC, GIC, State Bank of India and IDFC Ltd. Foreign investors include Citigroup.

The Standard & Poor's CRISIL NSE Index 50 or S&P CNX Nifty -Nifty 50 or simply Nifty is the leading index for large companies on the National Stock Exchange of India. The Nifty is a well diversified 50 stock index accounting for 21 sectors of the economy

The CNX Nifty Junior is an index for companies on the National Stock Exchange of India. It consists of 50 companies on the National Stock Exchange of India. It has the second tier of stocks in terms of market cap and don't make it into Nifty

The Inter-Connected Stock Exchange of India Limited (ISE)

The Inter-Connected Stock Exchange of India Limited (ISE) is being promoted by regional stock exchanges to set up a new national level stock exchange. The ISE would provide a national market in addition to the trading facility at the regional stock exchanges.

Indonext

BSE, Federation of Indian Stock Exchanges and regional stock exchanges have promoted IndoNext. The regional stock exchanges that are part of Indonext include Madras Stock Exchange, Bangalore Stock Exchange, Interconnected Stock Exchanges of India, Ludhiana Stock Exchange and Vadodara Stock Exchange. IndoNext is envisaged to bring liquidity and attention to stocks that are listed on RSEs.

MCX Stock Exchange Limited (MCX-SXAT)

It is an Indian stock exchange. It commenced operations in the Currency Derivatives (CD) segment in 2008 and equities in 2013. **SX40** is the flagship Index of MCX-SXAT.

USE

The **United Stock Exchange of India (USE)** is an Indian stock exchange. It is the 4th pan India exchange launched for trading financial instruments in India. USE represents the commitment of 21 Indian public sector banks, private banks, international banks (Standard Chartered) and corporate houses to build an institution of repute.

USE launched its operations in 2010 and deals in currency futures.

OTC Exchange Of India (OTCEI)

It also known as Over-the-Counter Exchange of India based in Mumbai.It is the first exchange for small companies.

OTCEI is promoted by the Unit Trust of India, the Industrial Credit and Investment Corporation of India, the Industrial Development Bank of India, the Industrial Finance Corporation of India and others and is a recognised stock exchange.

BSE

Bombay Stock Exchange (BSE) is the 11th largest stock exchange in the world by market capitalisation. Established in 1875, it has more than 5000 companies listed making it world's No. 1 exchange in terms of listed members. The companies listed on BSE Ltd command a total market capitalization of USD Trillion 1.32 as of January 2013.

BSE's popular equity index - the S&P BSE SENSEX [Formerly SENSEX] - is India's most widely tracked stock market benchmark index. It is traded internationally on the EUREX as well as leading exchanges of the BRICS nations (Brazil, Russia, China and South Africa). On Tuesday, 19 February 2013 BSE has entered into Strategic Partnership with S&P DOW JONES INDICES and the SENSEX has been renamed as "S&P BSE SENSEX".

One of the unique features inside the BSE includes the automatic online trading system known as BOLT that ensures an efficient and transparent market for trading in equity, debt instruments and derivatives.

In 2005, the status of the exchange changed from an Association of Persons (AoP) to a full fledged corporation under the BSE (Corporatization and Demutualization) Scheme, 2005 and its name was changed to The Bombay Stock Exchange Limited.

[Only public limited company is listed on stock market & Not Private limited.]

Classification of companies listed in BSE

Group	Classification
A	Companies with large capital base, large shareholder base, and good growth record with regular dividends & greater volumes in secondary market.
B1	Relatively liquid scrips with good management & satisfactory growth prospects & volumes
F	Segment for Non-convertible debentures
G	Central and State Government Securities
Z	It comprises of companies not complying with clauses of the listing agreement and are not redressing the grievances of the investor.

Sensex

Sensex or Sensitive Index is a value-weighted index composed of 30 companies with the base 1978-1979 = 100. It consists of the 30 largest and most actively traded blue chip stocks, representative of various sectors, on the Bombay Stock Exchange. Inclusion of the company is basically on the basis of market capitalization. The 30 companies in the index are revised periodically- some are replaced by others and new sectors may find representation as the economy evolves.The Sensex is generally regarded a mirror or barometer of the Indian stock markets and economy.

Demutualization

Mutualization refers to ownership and management of the exchange being combined in the same hands- brokers elected by the broker community from among themselves. Brokers are the owners of the BSE. Demutualization is when management and ownership are separated . Ownership is divested from the brokers and the company becomes a public company . All stock exchanges are to be demutualised according to the Government law made in 2004. Demutualization, thus means that ownership, management and trading rights are separated in a stock exchange.

Global rankings of BSE and NSE

The Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE) are among top five bourses across the emerging economies of the world in terms of market capitalisation.Listing out a total of 14 stock exchanges across emerging countries, Sebi said the BSE stood at fourth position and the NSE at fifth among these bourses in terms of cumulative market capitalisation of all The BSE stood at the fourth position with a market cap of $1,101.87 billion as on June 30, 2012.The NSE stood at fifth spot with market valuation at $1,079.39 billion at June-end.

Debt financing → loans
Equity financing → shares (so no debt)

BSE SME and NSE Emerge

Leading bourses BSE and NSE in 2012 launched their SME exchange platforms to enable small and medium enterprises to raise funds and get listed as public entities. While BSE kick-started its SME platform under the brand name of BSE SME Exchange NSE followed suit by announcing the launch its own platform 'Emerge'.

The exchange provides an opportunity to small entrepreneurs to raise equity capital for growth and expansion. It will also provide immense opportunity for investors to identify and invest in good SMEs at early stage.

The government has been taking a number of steps for SMEs to address challenges of globalisation, higher cost of funds, IT upgrade, infrastructure constraints faced by SMEs.

SMEs have huge listing potential but so far there have been only debt-financing options, without any access to alternative equity options There is a general lack of awareness among SMEs about equity capital, stock markets and funding options, other than banks.

SEBI

The capital markets in India are regulated by the Securities and Exchange Board of India. (SEBI) It was established in 1988 and given a statutory basis in 1992 on the basis of the Parliamentary Act- SEBI Act 1992 to regulate and develop capital market. SEBI regulates the working of stock exchanges and intermediaries such as stock brokers and merchant bankers, accords approval for mutual funds, and registers Foreign Institutional Investors who wish to trade in Indian scrips. Section 11(1) of the Sebi Act says that it shall be the duty of the Board to protect the interests of investors in securities.

SEBI promotes investor's education and training of intermediaries of securities markets. It prohibits fraudulent and unfair trade practices relating to securities markets, and insider trading in securities, with the imposition of monetary penalties, on erring market intermediaries. It also regulates substantial acquisition of shares and takeover of companies and calling for information from, carrying out inspection, conducting inquiries and audits of the stock exchanges and intermediaries and self regulatory organizations in the securities market

SEBI has its head office in Mumbai and its three regional offices in New Delhi, Calcutta and Chennai.

SEBI's powers were enhanced in 2002 - strengthen the SEBI's board, enlarge it to nine from six and appoint three full-time directors; given enhanced powers to conduct search and seizure etc.

SEBI and the Reforms

The Stock Exchange Scam of 1992 (Harshad Mehta) and the scam in 2000 (Ketan Parekh) led to led to various measures by the Government to protect the interests of the small investors. SEBI introduced reforms like improved transparency, computerisation, enactment against insider trading, restrictions on forward trading, introduction of T + 2 system of settlement etc. The restriction and elimination of forward or Contango trading,

referred to in India as 'Badla' is a bold step to check speculation and manipulation of the market. Some more steps taken by SEBI to strengthen markets are

- SEBI reconstituted governing boards of the stock exchanges, introduced capital adequacy norms for brokers, and makes rules for making client/broker relationship more transparent.
- SEBI enforces corporate disclosures.
- Enforces ban on insider trading
- Protects retail investors
- SEBI is empowered to register and regulate mutual funds.
- introducing a code of conduct for all credit rating agencies operating in India.
- Clause 49 of the listing agreement that SEBI introduced mandates that all listed companies should have half the Directors on the Board as Independent Directors

SEBI ordinance 2013

Government promulgated ordinance a second time in 2013 September. The ordinance is for granting greater powers to Sebi to check illicit investment schemes and other market manipulations.

The Securities Laws (Amendment) Second Ordinance, 2013 would amend the Sebi Act, the Securities Contracts (Regulation) Act and the Depositories Act .Ordinance has given Sebi greater powers to crack down on ponzi schemes, seek call data records to check insider trading and carry out search and seizure operations.

The amendments also give Sebi the legal backing to clamp down on unscrupulous entities "using newer methods to take gullible investors for a ride", as per a government statement issued at the time of promulgating the first ordinance.

As per the amended law, Sebi can regulate any money pooling scheme worth Rs 100 crore or more and attach assets in cases of non-compliance, while Sebi Chairman has been authorised to order "search and seizure operations".

Sebi has also got powers to seek any information, including telephone call data records, from any person or entity in respect to any securities transaction being investigated by it.

The amendments has also sought to clear the air over regulatory gaps and overlaps with regard to different types of instruments used in raising funds illegally

Capital market reforms

Since 1991 when the Government launched economic reforms, the following measures were taken

- SEBI given statutory status- that is Act of Parliament
- Electronic trade
- Rolling settlement to reduce speculation
- FIIs are permitted since 1992
- setting up of clearing houses
- settlement guarantee funds at all stock exchanges
- compulsory dematerialization of share certificates so as to remove problems associated with paper trading; and speed up the transfer
- clause 49 of the listing agreement for corporate governance
- restrictions on PNs

Primary market

The primary market is that part of the capital markets that deals with the issuance of new securities directly by the company to the investors. Companies, governments or public sector institutions can obtain funding through the sale of a new stock or bond issue. In the case of a new stock issue, this sale is called an initial public offering (IPO). If the company already issued shares and is going to the market again with a new issue, it is called Folllow on Public Offer(FPO).

Sebi made some far reaching reforms in favour of the retail investor in August 2012- allowed electronic bidding(e-IPO) for cost effective bidding; and made the rule that retail applicant will be allotted some shares compulsorily.

Secondary market

The secondary market is the financial market for trading of securities that have already been issued in an initial public offering. Once a newly issued stock is listed on a stock exchange, investors and speculators can trade on the exchange as there are buyers and sellers.

Types of shares

There are essentially two types of shares: common stock and preferred stock.

Preferred stock is generally issued to banks by the companies though retail investors are also eligible for them. They are preferred for the following reasons

- In terms of dividend payment, generally, they are given dividends even if the common stock holders are not
- When the company is to be closed, preference stock holders are given money first from the proceeds of the sale of the assets of the companies.
- They may have enhanced voting rights such as the ability to veto mergers or acquisitions or the right of first refusal when new shares are issued (i.e. the holder of the preferred stock can buy as much as they want before the stock is offered to others).

Derivatives

eg:- A & B arrive at a deal in (Jan) which A will sell wheat to B in Aug on a price fixed in Jan. So here wheat is underlying asset.

Derivative is a financial instrument.It derives from an underlying asset- securities, shares, debt instruments, commodities etc.. The price of the derivative is directly dependent upon the value of the underlying asset in the present and the projected future trends. Futures and options are the two classes of derivates.

Futures

Futures are financial instruments based on a physical underlying (commodity, equities etc.). A futures contract is an agreement between two parties to buy or sell an asset at a certain time in the future for a certain price.

deal or price
Price discovery

Futures are part of a class of securities called derivatives, so named because such securities derive their value from the worth of an underlying investment. Futures are different from forwards as the former are traded on exchange while the later may be merely a signed contract between two parties.

Options are a class of futures where the buyer or seller has the option whether to buy or not – put option is the right but not the obligation to sell. Call option is right but not the obligation to buy.

If you want to sell I have to buy

Buyback of Shares

Buyback of shares is the process of a corporation's repurchase of stock it has issued. In the case of stocks, this reduces the number of shares outstanding, giving each remaining shareholder a larger percentage ownership of the company. This is usually considered a sign that the company's management is optimistic about the future and believes that the current share price is undervalued. The company also should have reserves to do so.

Buying back shares to fill fiscal deficit (since govt will also have its shares in PSUs & other companies) is a

Reasons for buybacks include

- putting unused cash to use
- raising earnings per share
- reducing the number of shareholders to reduce the cost for servicing them, etc.

Shares bought back need to be cancelled and thus the total equity shrinks and the shareholders benefit. Buyback price is more than the market prices.Companies can buy back with the reserves but can not borrow to buyback.It is allowed in India since 1998.

Rolling Settlement

Rolling Settlements is a mechanism of settling trades. In Rolling Settlements, trades done on a single day are settled separately from the trades of another day on the basis of Trade day + 2 days(T+2). Such netting of trades is done only for the day. As such, in Rolling Settlement, settlement is carried out on a daily basis. Since trades done on a given day can not be bunched with those of another day. Thus, speculation is drastically reduced.

Commodity exchanges

Commodity exchanges are institutions which provide a platform for trading in 'commodity futures' just as how stock markets provide space for trading in equities and their derivatives. They thus play a critical role in price discovery where several buyers and sellers interact and determine the most efficient price for the product. Indian commodity exchanges offer trading in 'commodity futures' in a number of commodities. Presently, the regulator, Forward Markets Commission allows futures trading in over 120 commodities. There are two types of commodity exchanges in the country: national level and regional. There are five national exchanges:

- National Commodity & Derivatives Exchange Limited (NCDEX)
- Multi Commodity Exchange of India Limited (MCX)
- National Multi-Commodity Exchange of India Limited (NMCEIL)
- ACE Derivatives and Commodity Exchange
- Indian Commodity Exchange (ICEX)

The unique features of national level commodity exchanges are:

- They are demutualized,
- They provide online platforms or screen based trading
- They allow trading in a number of commodities and are hence multi-commodity exchanges.

They are national level exchanges which facilitate trading from anywhere in the country.

FMC

Forward Markets Commission (FMC) headquartered at Mumbai is a regulatory authority, which was overseen by the Ministry of Consumer Affairs and Public Distribution, Govt. of India. It is a statutory body set up in 1953 under the Forward Contracts (Regulation) Act, 1952. The Commission consists of 2-4 members. Its administrative control was shifted to Finance Ministry.

It monitors and disciplines the working of the exchanges. It recognizes an exchange or can withdraw such recognition. It collects and whenever the Commission thinks it necessary, publishes information regarding the trading conditions in respect of goods.

It makes inspection of the accounts and other documents of any recognized association or registered association or any member of such association whenever it considerers it necessary.

Forward Contracts (Regulation) Amendment Bill, 2010 was introduced in the Parliament. It seeks to make FMC into a Sebi-like regulator that is independent.

Forward Markets Commission is at present is a part of the department of consumer affairs. FMC will be given more teeth to regulate exchanges and all market participants.

In addition, the bill proposes to increase the monetary penalty for contravention of the legal provisions to up to Rs 25 lakh from a meagre Rs 1,000 at present..

New products will also be traded.

Mutual Fund

Mutual fund – a financial intermediary that mops up money , from a group of investors, to invest in capital market so as to generate returns for the investors. Mutual fund does it for a fees. There are two types of MFs.

Open-ended Funds

out of the securities in fund

Open-ended or open mutual funds issue shares(units) to the investors directly at any time. The price of share is based on the fund's net asset value. Open funds have no time duration, and can be purchased or redeemed at any time on demand, but not on the stock market.

An open fund issues and redeems shares on demand, whenever investors put money into the fund or take it out.

Closed-ended fund

It is a collective investment scheme issued by a fund. Only a fixed number of shares are issued in an initial public offering which may be called New Fund Offering(NFO). They trade on an exchange. Share prices are determined not by the total net asset value (NAV), but by investor demand.

Once the offering closes, new shares are rarely issued. They can be traded only on the secondary market(stock exchanges). Shares are not normally redeemable until the fund

liquidates. On the other hand, an open-end fund where the fund company creates new shares and can redeem existing shares .

The total value of all the securities in the fund divided by the number of shares in the fund is called the net asset value. [NAV]

FIIs

Foreign institutional investors are organisations which invest huge sums of money in financial assets - debt and shares- of companies and in other countries- a country different from the one where they are incorporated . They include banks, insurance companies, retirement or pension funds, hedge funds and mutual funds.

Foreign individuals are not allowed to participate on their own but go through FIIs.

FIIs are allowed to invest in the primary and secondary capital markets in India through the portfolio investment scheme (PIS). The ceiling for overall investment for FIIs varies from company to company.

FIIs called hot money invested in Indian equities and debt about $30 billion in 2010.The number of registered FIIs is 1,660 and that of registered sub-accounts is above the 5,000 mark. Besides buying equities from the market, FIIs have participated in Qualified Institutional Placements (QIPs), directly from the promoters requiring huge capital.

SEBI prescribes norms to register FIIs and also to regulate FII investments.

There are more than 1700 FIIs registered in India(2012). The FII's total investments in domestic markets amount to $ 122 billion in debt and equity , since India allowed them to invest here in 1992.In the calendar year 2012 upto July, about 11b dollars of FII came into India.

Reasons for FIIs having India as a favourite destination

- growing economy
- corporate profits are high
- government policies are encouraging
- compared to other countries, India has brighter prospects

FII investment is referred to as hot money for the reason that it can leave the country at the same speed at which it comes in.

QFIs

A QFI is an individual, group or association resident in a foreign country that is compliant with Financial Action Task Force (FATF) standards.Till 2012, they were investing in India through the FIIs registered with the SEBI. From 2012, they are allowed to invest in India directly for which Sebi and RBI have made the necessary rules.

They can invest in corporate debt, equities and mutual funds.

The move comes against the backdrop of significant foreign capital outflows from the domestic equity market in recent times, which has resulted in rupee depreciation.

Its aim is to widen the class of investors, attract more foreign funds and reduce market volatility and deepen the Indian capital market.

With regard to foreign portfolio investments, till 2012, only FIIs/sub-accounts and NRIs are allowed to directly invest in the Indian equity market.

The RBI would grant general permission to QFIs for investment under the Portfolio Investment Scheme (PIS) route, similar to FIIs.

The individual and aggregate investment limit for QFIs shall be 5 per cent and 10 per cent, respectively, of the paid-up capital of an Indian company.These limits shall be over and above the FII and NRI investment ceilings prescribed under the PIS route for foreign investment in India, it added.

In mid-2012, government set a separate $1-billion corporate bond investment limit for QFIs. The finance ministry also expanded the list of countries from which such investments will be permitted.A separate sub-limit of $1 billion has been created for QFI investment in corporate bonds and mutual fund debt schemes.The foreign investment limit in corporate debt, which consequently increased by $1 billion to $21 billion will boost debt inflows.

In July 2012, Sebi allowed QFIs to invest in those debt mutual fund schemes that hold atleast 25% of their assets (either in debt or equity or both) in the infrastructure sector.

The scheme was earlier open to only residents of countries that are members of Financial Action Task Force, or FATF, a global body to check money laundering and terror funding.

Government relaxed the eligibility condition to allow investors from Gulf Cooperation Council (GCC) and also the European Commission to invest in Indian debt if they meet the local rules. A resident of IOSCO can also be a QFI.

IOSCO

The **International Organization of Securities Commissions** (IOSCO) is an association of organisations that regulate the world's securities and futures markets.

Members are typically the Securities Commission or the main financial regulator from each country. IOSCO has members from over 100 different countries, who regulate more than 90 percent of the world's securities markets. The organisations role is to assist its members to promote high standards of regulation and act as a forum for national regulators to cooperate with each other and other international organisations.India is a member.

IOSCO is has a permanent secretariat based in Madrid.

Investment First

Who are qualified foreign investors (QFIs)?

A resident of a country that is a member of the Financial Action Task Force (FATF) or member of a group which, in turn, is member of this global body against money laundering and terror funding.

Resident of a country signatory to International Organization of Securities Commissions (IOSCO) or has signed a bilateral agreement with Sebi.

Where can they invest?

QFIs are now allowed to invest in all the three important segments of capital market – mutual funds, equities and corporate debt

Why has this been done?

India's current account deficit is said to have widened to over 3.6% of GDP

The capital flows needed to fill this current account gap have been muted

With weak appetite for risky assets very low, the government is trying to spur debt flow to

FATF

The **Financial Action Task Force (on Money Laundering) (FATF)** is an intergovernmental organization founded in 1989.The purpose of the FATF is to develop policies to combat money laundering and terrorism financing. The FATF Secretariat is housed at the headquarters of the OECD in Paris.

FATF is responsible for setting global standards on anti-money laundering (AML) and combating financing of terrorism (CFT).

Following its inclusion into the select club, India and its tax enforcement authorities — the Financial Intelligence Unit, the Enforcement Directorate, the Central Economic Intelligence Bureau and the Directorate of Revenue Intelligence — would be able to exchange vital information from member-countries on money laundering and terrorist financing activities.

Global Depository Receipts (GDR)

Indian companies are allowed to raise equity capital in the international market through the issue of Global Depository Receipt (GDRs). GDRs are designated in dollars/euros or any other foreign currency.

Investors invest in ADRs just like in India investor invest in shares of the buyshares

The proceeds of the GDRs can be used for financing capital goods imports, capital expenditure including domestic purchase/installation of plant, equipment and building and investment in software development, prepayment or scheduled repayment of earlier external borrowings, and equity investment in JVs in India.

Stock Exchange

GDRs are listed on London SE or Louxembourg or elsewhere. They are also called euroissues in a general sense.

Whatever hasn't come till yet may come in 2014.

ADRs

American depository receipts are like shares. They are issued to US retail and institutional investors. They are entitled like the shares to bonus, stock split and dividend. They are listed either on Nasdaq or NYSE.

Like GDRs, they help raise equity capital in forex for various benefits like expansion, acquisition etc.

ADR route is taken as non-USA companies are not allowed to list on the US stock exchanges by issuing shares.

Similarly with Indian Depository Receipts(IDRs) as and when they are allowed.

Participatory notes

Participatory notes are instruments used for making investments in the stock markets. In India, foreign institutional investors (FIIs) use these instruments for facilitating the participation of overseas funds like hedge funds and others who are not registered with the Sebi and thus are not directly eligible for investing in Indian stocks.

Any entity investing in participatory notes is not required to register with SEBI (Securities and Exchange Board of India), whereas all FIIs have to compulsorily get registered. Participatory notes are popular because they provide a high degree of anonymity, which enables large hedge funds to carry out their operations without disclosing their identity and the source of funds. KYC(know your customer norms are not applied here)

Since the source of funds is not revealed, the PNs are potentially unsafe. Therefore, SEBI in 2007 October imposed certain conditions like limits on the PNs that a single FII can issue etc. SEBI wants the PN holders to register with the SEBI and invest directly as India is a long term growth story. Sebi policy paid off with the number of FIIs registering with the regulator going upto over about 1750(2011).

The SEBI action aims at ensuring that the quality of flows into stock markets and Indian forex market is clean.

Rajiv Gandhi Equity Savings Scheme

It was presented in as a part of the Union Budget 2012-13 for the new investors in stocks with an annual income of less than Rs.10 lakh. He gets 50 percent tax deduction on investments upto Rs 50,000. Money will be locked for three years. Details are still being worked out.

Hedge fund

A hedge fund is an investment fund open to only a limited range of investors. They are mostly unregulated. The term- hedge funds , is used to distinguish them from regulated investment funds such as mutual funds and pension funds, and insurance companies. Hedge funds are not allowed into India as they do not disclose data required by the Sebi.

Clearing house

An organisation which registers, monitors, matches and guarantees the trades of its members and carries out the final settlement of all futures transactions. The National Securities Clearing Corporation is the clearing house for the NSE.

Equity

Common stock and preferred stock that is, shares issued by the company.Also, funds provided to a business by the sale of stock.

Share

Share is a certificate representing ownership of the company that issued it. Shares can yield dividends and entitle the holder to vote at general meetings. The company may be listed on a stock exchange. Shares are also known as stock or equity.

Bond

A debt instrument issued for a period of more than one year with the purpose of raising capital by borrowing.

Debenture

Debt not secured by a specific asset of the corporation, but issued against the issuer's general credit- that is, it is unsecured debt. Investment earns an interest for the debenture holder. The following are various types of debentures

- convertible debentures can be converted into equity at a future date
- Non-convertible debentures will not be converted
- Partly convertible debentures will have some part converted into shares.

Bear

Bear is an investor who believes that market will go down.

Bull

Bull is an investor who believes that the market will go up- optimistic

Bear Market

A sustained period of falling stock prices usually preceding or accompanied by a period of poor economic performance known as a recession.

Bull Market

A stock market that is characterized by rising prices over a long period of time. The time span is not precise, but it represents a period of investor optimism, lower interest rates and economic growth. The opposite of a bear market.

Gilt

Gilt is a bond issued by the government. It is issued by the Central Bank of a country on behalf of the government. In India, Reserve Bank of India issues the treasury bills or gilts. Gilt Edged Market is the market for government securities.

Blue chip

Blue chip shares are the shares of the companies that are the most valuable. Companies that are profit making; usually dividend –paying and are liquid in the market- that is there is almost always in demand on the market.

Midcap company

Generally, companies with a market capitalization that is very high are called large caps and the next rung below is mid cap and the bottom one is small cap companies. Limits are not statutorily laid dwn and vary from institution to institution.

Small investor

Market regulator SEBI set the investment limit for retail investors in an initial share sale offer to Rs 2 lakh. This will cut the numerous applications investors sometimes make in the name of relatives to get more shares.

Sebi allows price discount for retail investors and company discount participating in initial public offers and follow-on offers. This discount is offered to attract retail investors into the market and broad base ownership.

Primary Dealers

The Reserve Bank of India introduced a system of Primary Dealers (PDs) in government securities market in 1995 with the objective to strengthen the infrastructure in the government securities market in order to make it vibrant, liquid and broad-based. The following can be the PD: subsidiaries of scheduled commercial banks and all India financial institutions and engaged predominantly in securities business and in particular the government securities market; or companies incorporated under the Companies Act, 1956 and engaged predominantly in securities business and in particular the government securities market.;The company should have net owned funds of Rs.50 crore.

Market depth

It is a dimension of market liquidity and it refers to the ability of a market to handle large trade volumes without a significant impact on prices.

Liquidity is the ease to find a trading partner for a given order.

Market breadth means the following:The fraction of the overall market that is participating in the market's up or down move. The greater the breadth, the more the companies that are participating.

Trading volumes means the number of shares traded.

Negotiated Dealing System

Negotiated Dealing System (NDS) is an electronic platform for facilitating dealing in Government Securities and Money Market Instruments.

Short selling

The sale of a security made by an investor who does not own the security. The short sale is made in expectation of a decline in the price of a security, which would allow the investor to then purchase the shares at a lower price in order to deliver the securities earlier sold short.

Market capitalization

Price per share multiplied by the total number of shares outstanding; also the market's total valuation of a public company.

P/E ratio

Also known as the P/E multiple, this is the latest closing price divided by earnings per share EPS). P/E is perhaps the single most widely used factor in assessing whether a stock is overvalued or cheap. A company's P/E should be looked at against those of similar companies, and against that of the stock market as a whole, since different industries and even different company are characterized by markedly different P/Es. In general, fast-growing technology companies have high P/Es, since the stock price is taking account of anticipated growth as well as current earnings. A high P/E is often a reflection of high expectations for a stock.

EPS

The portion of a company's profit allocated to each outstanding share of common stock. The amount is computed by dividing net earnings by the number of outstanding shares of common stock. For example, a corporation that earned Rs10 million last year and has 10 million shares outstanding would report earnings per share of Rs.1.

Insider Trading

Insider trading occurs when any one with information related to strategic and price-influencing information purchases or sells stocks so as to make speculative profits. SEBI is formulating rules which are tougher for the insider trading.

Depository

A depository holds securities (like shares, debentures, bonds, Government Securities, units etc.) of investors in electronic form. Besides holding securities, a depository also provides services related to transactions in securities. Benefits of a depository are reduction in paperwork involved in transfer of securities; reduction in transaction cost.

National Securities Depository Limited (NSDL)

In the depository system, securities are held in depository accounts, which is more or less similar to holding funds in bank accounts. Transfer of ownership of securities is done through simple account transfers.The enactment of Depositories Act in 1996 paved the way for establishment of NSDL, the first depository in India.

NSDL offers facilities like dematerialisation i.e., converting physical share certificates to electronic form; rematerialisation i.e., conversion of securities in demat form into physical certificates etc.

Nasdaq

Nasdaq stands for the National Association of Securities Dealers Automated Quotation System. Unlike the New York Stock Exchange where trades take place on an exchange, Nasdaq is an electronic stock market that uses a computerized system to provide brokers and dealers with price quotes. It is an electronic stock market- first in the world- run by the National Association of Securities Dealers. Many of the stocks traded through Nasdaq are in the technology sector.

Dow Jones Index

The New York Stock Exchange (NYSE) index, which reflects the movement of the world's first stock market. It is composed of the 32 most traded stocks of the NYSE. Currently there are three Dow Jones Indices: The Dow Jones Industrial Average (DJIA). The Dow Jones Transport Average (DJTA) and finally DJUA (Dow Jones Utility Average).

In recent years, broader indices such as the Standard & Poor's 500 (for large companies), the Russell 2000 (for smaller companies) and the Wilshire 5000 (for an especially broad measure) have gained currency, in part due to the rising popularity of index investing.

Important indices in the world

Market index is a number to indicate the average movement of prices of a securities market. It usually tracks select stocks.

- American Dow Jones Industrial Average and S&P 500 Index
- British FTSE 100: It is a share index of the 100 most highly capitalised companies listed on the London Stock Exchange. The index began in 1984 with a base level of 1000.The index is maintained by the FTSE Group, an independent company which originated as a joint venture between the Financial Times and the London Stock Exchange.
- French CAC 40
- German DAX
- Japanese Nikkei 225
- Indian Sensex and Nifty
- Australian All Ordinaries
- Hong Kong Hang Seng Index
- South Korea's Kospi
- Straits Times Index (STI) of Singapore
- Bovespa Index, Sao Paulo (Brazil)
- RTS Index (RTSI) is an index of 50 Russian stocks that trade on the RTS Stock Exchange in Moscow
- SSE (Shenzhen Stock Exchange) Composite Index- China
- SSE (Shanghai Stock Exchange) composite index-China

Ethical investing

A notable specialised index type is those for ethical investing indexes that include only those companies satisfying ecological or social criteria, e.g. those of Dow Jones Sustainability Index.

Ponzi scheme or pyramid scheme

A **Ponzi scheme** is a fraudulent investment operation that pays high returns to investors and promises higher returns to those who join the scheme later. The payments are done from investors own money or money paid by subsequent investors rather than from any actual profit earned because it is not possible to earn such high reurns on any investment.The system

is destined to collapse because the earnings, if any, are less than the payments. The scheme is named after Charles Ponzi,who became notorious for using the technique after emigrating from Italy to the United States in 1903.

Decoupling

It means that a nation's economy may have an autonomous logic and need not be entirely dependent on the global economy. For example, if the world goes into a recession, all counties need not. India, for example grew at 6.7%(2008-09) while the USA and the west were contracting. Reflecting the economic realities, equity markets also perform autonomously after a point. It is called decoupling- that is, isolation from the rest.

China is more integrated with the world as itss economy is driven by exports. However, even China is decoupled as it has a lot of domestic consumption driving its growth.

Clause 49

Clause 49 of the Listing Agreement to the Indian stock exchange came into effect in 2005.

It has been formulated for the improvement of corporate governance in all listed companies as it mandates that there should be certain independent directors on the Board of a Company.

IDR

Indian Depository Receipts are issued by a non-Indian company to Indian investors for its listing on Indian stock exchanges. It is like ADR.

Shariah index

Asia's oldest stock exchange, the Bombay Stock Exchange (BSE), launched its Shariah index in December 2010. The index, structured in partnership with Taqwaa Advisory Shariah Investment Solutions has 50 stocks selected from the BSE-500 bracket.

Infrastructure, capital goods, IT, telecom and pharmaceuticals shares will form a large chunk of the 'BSE Tasis Shariah-50 Index', as the new index is known. But no stock will have more than an 8% weightage. The stock screening has been done by Taqwaa Advisory (Tasis) scholar board, and the index construction, by BSE.

The new index will attract investments from Arab and European countries, where Shariah funds are already popular.

a restriction, a critical remark

Shariah, the religious law of the followers of Islam, has strictures regarding finance and commercial activities permitted for believers. Arab investors only invest in a portfolio of 'clean' stocks. They do not invest in stocks of companies dealing in alcohol, conventional financial services (banking and insurance), entertainment (cinemas and hotels), tobacco, pork meat, defence and weapons.

The index will be rebalanced every quarter though stocks that do not comply (at some point of time) with Shariah statutes will be excluded immediately. National Stock Exchange S&P CNX Shariah Index and Dow Jones Islamic India Index are other Shariah benchmarks that are tracked by investors. Shariah-based equity investments do not allow investors to invest in heavily indebted.

Brics cooperation among exchanges

In 2011 October seven major stock exchanges in Brazil, Russia, India, China and South Africa announced plans to cross-list derivatives on their benchmark indexes. The five founding members of the BRICS Exchanges Alliance began cross-listing benchmark equity index derivatives on each other"s trading platforms from 2012. The five exchanges, BM&FBOVESPA from Brazil, Open Joint Stock Company MICEX-RTS from Russia, BSE Limited from India, Hong Kong Exchanges and Clearing Limited (HKEx) as the initial China representative, and JSE Limited from South Africa, announced the formation of the alliance on 12 October 2011 at a World Federation of Exchanges" conference in Johannesburg, South Africa. In this initial stage of implementation, the exchanges aim to expand their product offerings beyond their home markets and give investors of each exchange exposure to the dynamic, emerging, and increasingly important BRICS economies.
The move was endorsed in the March 2012 Delhi summit of Brics.

Power exchanges

A power exchange created within the regulatory framework is an institution that is responsible for conducting auctions in a non-discriminatory fashion to sell power at competitive market prices . CERC has permitted trading of Electricity through Power Exchange with effect from June 2008. Currently, two exchanges viz. Indian Energy Exchange (IEX) and Power Exchange of India Limited (PXIL) are in operation in India which facilitate an automated on-line platform for physical day-ahead contracts.It is the core of an **electricity market** which is a system for effecting purchases, through bids to buy and sell.It would bring about efficiency as well as liquidity as power companies bought and sold electricity.

SGX Nifty

SGX Nifty is Indian Nifty traded in Singapore Stock Exchange. It moves with respect to Indian Nifty. SGX Nifty is open at 8.00 am Indian standard time (IST) on all working days and mostly it becomes initial direction to the Indian Market.

Inflation
Concepts, Facts and Policy

Inflation means a persistent rise in the price of goods and services. Inflation reduces the purchasing power of money. It hurts the poor more as a greater proportion of their incomes are needed to pay for their consumption. Inflation reduces savings; pushes up interest rates; dampens investment; leads to depreciation of currency thus making imports costlier.

Depending upon the rate of growth of prices, inflation can be of the following types
Creeping inflation is a rate of general price increase of 1 to 5 percent a year. Creeping inflation of 3 to 5 percent erodes the purchasing power of money when continued over many years, but it is "manageable." Furthermore, a low creeping inflation could be good for the economy as producers and traders make reasonable profits encouraging them to invest.
Trotting inflation is usually defined as a 5 to 10 percent annual rate of increase in the general level of prices that, if not controlled, might accelerate into a galloping inflation of 10 to 20 percent a year. If it aggravates, galloping inflation can worsen to "runaway" inflation which may change into a hyperinflation. Hyperinflation is inflation that is "out of control," a condition in which prices increase rapidly as a currency loses its value. No definition of hyperinflation is universally accepted. One simple definition requires a monthly inflation rate of 20 or 30% or more- 'an inflationary cycle without any tendency toward equilibrium'. The worst is a monetary collapse, if prices are not reined in , in time.
Other related concepts are

- deflation when there is a general fall in the level of prices
- disinflation which is the reduction of the rate of inflation
- stagflation which is a combination of inflation and rising unemployment due to recession and
- Reflation, which is an attempt to raise prices to counteract deflationary pressures.

Measures of inflation

GDP deflator

GDP stands for gross domestic product, the total value of all final goods and services produced within that economy during a specified period.GDP deflator is a measure of the change in prices of all new, domestically produced, final goods and services in an economy. The GDP deflator is not based on a fixed market basket of goods and services but applies to all goods and services domestically produced.

Cost of living index

The cost of living is the cost of maintaining a certain standard of living. It is defined with reference to a basket of goods and services. When their cost goes up, CoL is said to be dearer and the index will go up. It has a value of 100 in the base year. An index value of 105 indicates that the cost of living is five percent higher than in the base year.

PPI

Producer price index (PPIs) measures the change in the prices received by a producer. The difference with the WPI is accounted for by logistics, profits and taxes, mainly. Producer price inflation measures the price pressure due to increase in the costs of raw materials. It

may be absorbed by them or made up by increases in productivity or passed on to the consumers. It depends on the market conditions.

WPI

Wholesale price indices, which measure the change in price of a selection of goods at wholesale, prior to retail sales thus excluding sales taxes. These are very similar to the Producer Price Indexes.

CPI

Consumer price index measures the changes in prices paid by the consumer at the retail level. It can be for the whole community or group-specific- for example, CPI for industrial workers etc as in India.

Types of inflation based on causes

There are four major types of inflation

- **Demand-pull inflation:** inflation caused by increases in demand due to increased private and government spending, etc. It involves inflation rising as real gross domestic product rises and unemployment falls. This is commonly described as "too much money chasing too few goods". For example, India in 2010 when the economy is said to have overheated and demand outstripped supply and prices rose. Since supplies will be augmented to adjust to demand, prices will come down. It may be refered to as `growth inflation' too. Demand-pull inflation can be caused by money supply increasing. For example, the expansionary monetary policy of the RBI in 2009 saw rates come down and easy and cheap credit pushed up prices as demand grew. From 2010 March till the end of 2011, repo rates went up 13 times and thus RBI sought to control prices by controlling demand. Wage inflation, money supply growth etc create this type of inflation.
- **Cost-push inflation:** It is also refered to as "supply shock inflation," caused by reduced supplies due to increased prices of inputs, for example, crude prices globally have gone up causing supply constraints which means higher costs of production and so higher prices. Crude and food prices shot up in 2008 July, came down and again increased. Food prices are shooting up again due to deficient monsoon and global shortages. Other examples are higher cost of capital, increases in prices of imported raw materials. Just as a shortage of goods tends to push prices up, an oversupply of commodities tends to induce the opposite effect on prices.
- **Structural inflation:** A type of persistent inflation caused by deficiencies in certain conditions in the economy such as a backward agricultural sector that is unable to respond to people's increased demand for food, inefficient distribution and storage facilities leading to artificial shortages of goods, and production of some goods controlled by some people. Food inflation currently being witnessed (2012) is structural in nature as the preference for protein foods is far ahead of its supplies and this is a phenomenon driven by income rise.
- **Speculation**
- **Cartelization**
- **Hoarding**

High Inflation hurts

If inflation is high in an economy, the following problems can arise

- low income groups are particularly hurt
- People on a fixed income (e.g. pensioners, students) will be worse off in real terms due to higher prices and equal income as before
- inflation discourages exports as domestic sales are attractive and BOP problems can be caused. Inflation may erode the external competitiveness of domestic products if it leads to higher production costs such as wage increases, higher interest rate and currency depreciation.
- inflation can drag down growth as investment climate turns bad due to instability and uncertainty and also as interest rates are raised and cost of credit increases
- Inflation may discourage saving and thus hit investment. The savings pattern also gets skewed in favour of unproductive assets like gold as inflation may be higher than interest rates and yield is negative.
- Inflation tax happens. When a government borrows and spends, the cash held by people erodes in value due to inflation
- It will redistribute income from those on fixed incomes, such as pensioners, and shifts it to those who draw an inflation-linked income and businesses.
- strikes can take place for higher wages which can cause a wage spiral. Also if strikes occur in an important industry which has a comparative advantage the nation may see a decrease in productivity, exports and growth.
- Govt fiscal deficit may go up as the need to subsidise is more to make goods and services affordable

Small amount of inflation can be good

Inflation means growth, normally- higher incomes and more demand and so more inflation. It can be argued that a low level of inflation can be good if it is a result of innovation. New products are launched at high prices, which quickly come down through competition. Therefore, there is encouragement for innovation and the problem is short lived. Also, a small price rise is necessary for wages to go up. It further helps the economy keep off deflation which can otherwise set off a recession. Besides, inflation at a moderate level is an incentive to the producer. Some see mild inflation as "greasing the wheels of commerce."

Anticipated inflation: When inflation is anticipated, individuals know what is coming, and how to deal with it. For example, banks may raise interest rates to compensate for the anticipated inflation, workers may ask for raises to maintain their real incomes, wealth holders will put their wealth into assets that will rise in value at least at the same rate as the increase in the price index, etc.

Unanticipated inflation: When inflation is unanticipated, individuals do not realize that they should protect their real purchasing power against a rising price level until the price level has already risen and their real purchasing power has already fallen. In this instance, there will be gainers and losers, in terms of purchasing power, from the inflation.

Losers: Individuals on fixed incomes, retirees, all creditors (who lent at fixed rate of interest.)

Gainers: Individuals whose incomes rise faster than inflation, debtors (who will pay back at fixed rate of interest).

In December 2013, the WPI and CPI inflation figures are as follows:
WPI showed 7% plus and CPI almost 11% rise.

To control inflation

There are fiscal, monetary, supply-side and administrative measures to control inflation to ideal/optimal rates though zero rate of inflation is never preferred for the reasons cited elsewhere in the lesson.

- Fiscal measures include reduction in indirect taxes
- Dual pricing like in sugar.
- Monetary measures include rate and reserve requirements changes. Open market operations can stabilize prices under normal conditions Also, sterilization through Government bond transactions as in the case of MSBs
- Supply side factors include making goods available- import of edible oil in India.
- Administrative measures include implementation of dehoarding and anti-black-marketing measures. Wage and price controls can also be used

Indices of Inflation

Changes in the price levels at the wholesale and retail level are tracked by various price indices in India- WPI and CPI. 3 CPIs exist for different consumer groups each of which is homogenous.

All price indices use a particular year as a "base year". That means that rises or falls in prices are measured with reference to the price in that year. For example, the base year used for the Wholesale Price Index is 2004-05. Wholesale prices of all products in the basket with their respective weightages in that year add upto "100". If, in 04-05, the wholesale price of gur was Rs 2 a kg, and rose by 50 paise the following year, it would mean that the wholesale price index for gur would rise to 125 in 2005-06. But the movement of an index is based on the average of price movement of all the goods in the basket and not just one article. Different base years are used for different price indices due to convenience, data availability, logistics etc.

$2 \rightarrow 100$
$2.5 \rightarrow x$
$2x = 2.5 \times 100$
$\therefore x = 125$

WPI

The Wholesale Price Index

Government launched a new series of wholesale price index (WPI) with 2004-05 as base from 2010. Earlier, 1993-94 was used as base year to calculate WPI. The new series of WPI has 676 items as against 435 items in the previous series. Consumer items widely used by the middle class like ice-cream, mineral water, flowers, microwave oven, washing machine, gold and silver are reflected in the new series of WPI. This would give better picture of the price variation. Readymade food, computer stationary, refrigerators, dish antenna, VCD, petroleum products and computers will also be part of the new series.

Under primary article group of the new WPI, there are 102 items against earlier 98, while fuel and power category remains static at 19. In the new series, there are 555 items of manufactured products compared to 318 items earlier.

241 new items are there in the basket of commodities making up the official wholesale price index in a bid to reflect changes in India's price line and consumption pattern better. The new series altered the weight attached to each commodity group.

Manufactured items now have a higher weight of 64.972 as against 63.749 earlier. The weight for fuels has also increased to 14.910 against 14.226. But for primary articles, the weight is down at 20.118 against 22.025.

In a bid to reflect the actual consumption pattern, the new series drops as many as 200 items sach as typewriters, video cassette recorders, to make a room for items like computers, refrigerators, televisions and video disc players.

Government is also working on a two new indices to reflect the changes in the cost of services — one on financial services and the other on trade and transport.

The Indian WPI is now updated on a monthly basis. The WPI is published by the Economic Advisor in the Ministry of Commerce and Industry, with a two week lag, tracks the wholesale traded price of 676 items that include agricultural commodities (such as rice, tea, raw cotton, groundnut oil seed), industrial commodities (such as iron ore, bauxite, coking coal), intermediate products for industry (such as cotton yarn, polyester fiber, synthetic resins, iron & steel, sheet glass), products for consumers (atta, sugar, paper, electricity, ceiling fans) and energy items (petrol, kerosene, electricity for commercial use). The weight attached to each item in the index is meant to reflect the volume (by value) of wholesale trade in that item in the Indian market.

The index is a vital guide in economic analysis and policy formulation. WPI covers primary goods, power/fuel and manufactured goods.

The WPI is not intended to capture the effect of price rise on the consumer though it generally and broadly indicates it.

WPI has an All India character. It is due to these attributes that it is widely used in business and industry circles and in Government and is generally taken as an indicator of the rate of inflation in the economy.

To reflect the structural changes in the economy that have taken place over a decade, a large number of commodities have been added and a few with diminished importance have been dropped.

WPI is announced with a time lag of two weeks. The data is made final after a period of 8 weeks.

The inflation rate is calculated on point to point basis i.e. on the basis of the variation between the index of the latest week of the current year and for the corresponding week of the previous year.

There are a number of agricultural commodities, especially, some fruits and vegetables, which are of a seasonal nature. Such seasonal items are handled in the index in a special manner. When a particular seasonal item disappears from the market and its prices are not quoted, the index of such an item ceases to get compiled and its weight is distributed over the remaining items and new seasonal items, if any, in the concerned sub-group.
The advantage of the WPI is that it covers more goods; is available with relatively small time lag of fortnight; is convenient to compile. Disadvantages are that it does not include services like transport, health, education etc.

Limitations on WPI

The accuracy of WPI is unsatisfactory even after the introduction of the revised series in 2010. Services such as rail and road transport, health care, postal, banking and insurance, for example, are not part of the WPI basket. Neither are the products of the unorganised sector that are estimated to constitute about 35 per cent of the total manufactured output of the country. The index thus falls well short of being a broad based indicator of the price level even in its construction.

WPI: new reporting method

From 2009, government presented WPI inflation figures on a monthly basis instead of weekly system. Analysts say since weekly data on wholesale price index-based inflation do not adequately capture the movement of prices of manufactured goods, government has to often revise the figures later. Therefore, the government decided to have weekly release of inflation data on food and fuel prices and monthly data on WPI. Inflation of primary goods within the WPI is reported on a weekly basis. But from 2011, the WPI is reported every month, including the food and primary article data

Comparative Statement of Commodities and price quotations

	No of Commodities		No of Price Quotations	
	1993-94	2004-05	1993-94	2004-05
All Commodities	435	676	1918	5482
Primary Articles	98	102	455	579
Fuel and Power	19	19	72	72
Manufactured Products	318	555	1391	4831

Weightage of the Sub Indices

	1993-94	2004-05
All Commodities	100%	100%
Primary Articles	22.025%	20.118%
Fuel and Power	14.226%	14.910%
Manufactured Products	63.749%	64.972%

CPI

There are three Consumer Price Indices in India. Each tracks the retail prices of goods and services for specific group of people, because the consumption patterns of different groups differ.

For Industrial Workers (CPI-IW), a basket of 370 commodities is tracked; for Urban Non-Manual Employees (CPI-UNME), 180 commodities; for Agricultural Labourers (CPI-AL), 60 commodities. The respective base years are 2001, 1984-85 and 1986-87. The first two indices have services in them. These baskets and the weightages to each item have been determined on the basis of surveys of consumption patterns. Information also differs from centre to centre around the country; the all-India figures declared are averages.

Mahatma Gandhi NaREGA wages are to be indexed to the CPI(AL) from the beginning of the year 2011.

CSO decided to discontinue CPI(UNME) from 2008.

Each commodity is given a specific weightage, which differs from one index to another index. For example, the CPI-AL would give a greater weightage to foodgrains than the CPI-UNME, since a greater proportion of the agricultural labourer's expenditure would go toward foodgrains, and he would be unlikely to buy the sort of items the office-goer would buy.

The coverage of CPI IW is broader than the other indices of CPI like the CPI for agricultural laborers (AL) and the CPI for urban non-manual employees (UNME).

In the organised sector, CPI-IW is used as a cost of living index.

CPI-AL and CPI-UNME are not considered as robust national inflation measures because they are designed for specific groups of population with the main purpose of measuring the impact of price rise on rural and urban poverty.

In accordance with the Government of India (Allocation of Business) Rules, 1961, as amended from time to time, it is the responsibility of the Ministry of Labour to compile and release the data on the CPI for Industrial Workers and the data on the CPI for Rural Labourers. It is the responsibility of the Ministry of Statistics and Programme Implementation to compile and release the data on the CPI for Urban Non-Manual Employees.

The Government of India (Allocation of Business) Rules, 1961, with subsequent amendments, assigns the responsibility for compiling the WPI to the Office of the Economic Adviser in the Department of Industrial Policy and Promotion under the Ministry of Commerce and Industry. The Economic Adviser holds the final authority for all decisions regarding the WPI.
The national income deflator(GDP deflator) is a comprehensive measure statistically derived from national accounts data released by the Central Statistical Organization (CSO). Since it encompasses the entire spectrum of economic activities including services, the scope and coverage of national income deflator is wider than any other measure. At present, the GDP deflator is available only annually with a long lag of over one year and hence has very limited use for the conduct of policy.

Difference between wholesale prices and consumer prices
WPI measures price rise at the wholesale level. Wholesale means sale in large quantities and meant for resale It covers a certain set of goods that are traded at the wholesale level. CPI on the other hand measures price rise at the retail level. There is a difference between the two. The difference is due to a number of factors. A substantial portion of the differential is accounted for by the retailers' margins which are built into what the consumer pays. Besides, the way the two indices are calculated differs both in terms of weightage assigned to products as well as the kind of items included in the basket of products.

While wholesale prices are more or less the same throughout the country, consumer prices or retail prices vary across regions (rural and urban) and also across cities according to the consumer preferences for certain products, supplies and purchasing power. Besides, taxes levied by states comprise an important component of the variation in prices of many products.

Therefore, give WPI an important place in government policy as it is more representative ; figues come quickly relatively; and has an all India character.

Divergence between WPI and CPI

Why do WPI and CPIs differ? They differ in terms of their weighting pattern. First, food has a larger weight in CPI ranging from 46 per cent in CPI-IW to 69 per cent in CPI-AL whereas it has a weight of only 27 per cent in WPI. The CPIs are, therefore, more sensitive to changes in prices of food items. Second, the fuel group has a much higher weight in the WPI (14.2 per cent) than the CPIs (5.5 to 8.4 per cent). As a result, movement in international crude prices has a greater bearing on WPI than on the CPIs. Third, services are not covered under WPI while they are, to different degrees, covered under CPIs. Consequently, service price inflation has a greater influence on CPIs.

New CPI series

The Central Statistics Office (CSO) of the Ministry of Statistics & Programme Implementation introduced the new series of Consumer Price Index (CPI) numbers for Rural, Urban and Combined (Rural +Urban) on base 2010 =100 taking all segments of rural and urban population for the States/UTs and all- India . Since 2011, the new series is force. These indices are available for five major groups namely Food, beverages and tobacco; Fuel and light; Housing; Clothing, bedding and footwear, and Miscellaneous.

Present CPI numbers do not encompass all the segments of the population in the country and as such they do not reflect the true picture of the price behavior in the country. It is therefore necessary to compile a CPI which takes into account the consumption patterns of all segments of the population and includes services.

New series of CPI for urban areas

CPI (Urban) numbers are compiled at State/UT as well as at all- India level. Weighting diagrams (consumption patterns) of the CPI (Urban) have been derived from the results of the NSS 61st round of Consumer Expenditure Survey (2004-05). For regular price collection, 310 towns have been selected, which include all State/UT capitals. From each selected town, price data are collected in respect of items consumed by the population of the respective State/UT. In all, 1114 price schedules containing an average of 250 items are canvassed every month. House rent data are also collected from a fixed set of rented dwellings from the selected towns. Prices of items are collected by the field officials of the National Sample Survey Office (NSSO).

New series of CPI for rural areas

CPI (Rural) numbers are compiled at state/UT and all- India levels. Weighting diagrams of the CPI (Rural) have also been derived from the results of the NSS 61st round of Consumer Expenditure Survey (2004-05).

Considering the fact that the CPI (Rural) would provide the price changes for the entire rural population of the country, a total of 1181 villages have been selected at all India level. Regular prices are collected by the officials of the Department of Posts. One schedule containing an average of 225 items from each selected village is canvassed for collection of prices every month.

National CPI

CSO will also compile national CPI by merging CPI (Rural) and CPI (Urban) with appropriate weights, as derived from NSS 61st round of Consumer Expenditure Survey (2004-05) data.

Weighting diagrams

The share (weight) of the Food, beverages and tobacco group in the all India CPI (Rural) is 59.31% and it is 37.15% in the all India CPI (Urban). Fuel and light group has a weight of 10.42% in CPI (Rural) and 8.40% in CPI (Urban). Clothing, bedding and footwear group has weight of 5.36% in CPI (Rural) and the weightage of 3.91% in CPI (Urban). Housing group has not been given any weightage in the rural areas CPI as its share is around 1% and it has been distributed to other groups on pro rata basis. CPI (Urban) has a weightage of 22.53% in respect of Housing group. The Miscellaneous Group consisting of education, medical care, transport and communication etc has 24.91% weight in the all India CPI (Rural) and the corresponding weight in the all India CPI (Urban) is 28%.

Release of indices

Index numbers for both rural and urban areas and also combined for each month and released. Indices are released with a time lag of one month.

(need to check)

Revision of indices

These new CPI numbers would be revised on the basis of the results of the next round of Consumer Expenditure Survey scheduled to be conducted during 2011-12 by the NSSO. Thereafter, revision will be undertaken every five years or so (whenever large scale Consumer Expenditure Survey data become available).

New series of CPI-- All India weights			
Sub group/group	**Rural**	**Urban**	**Combined (Rural+Urban)**
Cereals and products	19.08	8.73	14.59
Pulses and products	3.25	1.87	2.65
Milk and milk products	8.59	6.61	7.73
Oils and fats	4.67	2.89	3.90
Egg, fish and meat	3.38	2.26	2.89
Vegetables	6.57	3.96	5.44
Fruits	1.90	1.88	1.89
Sugar etc	2.41	1.26	1.91
Condiments and spices	2.13	1.16	1.71
Non- alcoholic beverages	2.04	2.02	2.03
Prepared meals etc	2.57	3.17	2.83
Pan, tobacco and Intoxicants	2.73	1.35	2.13
Food, beverages and tobacco	**59.31**	**37.15**	**49.71**
Fuel and light	**10.42**	**8.40**	**9.49**
Clothing and bedding	4.60	3.34	4.05
Footwear	0.77	0.57	0.68
Clothing, bedding and	**5.36**	**3.91**	**4.73**

footwear			
Housing		**22.53**	**9.77**
Education	2.71	4.18	3.35
Medical care	6.72	4.34	5.69
Recreation and amusement	1.00	1.99	1.43
Transport and communication	5.83	9.84	7.57
Personal care and effects	3.05	2.74	2.92
Household requisites	4.48	3.92	4.30
Others	1.12	0.99	1.06
Miscellaneous	**24.91**	**28.00**	**26.31**
All Groups	**100.00**	**100.00**	**100.00**

The new series is broad based and covers the entire rural and urban population. In the new series compiled by Central Statistics Office, the consumption patterns have been derived from the results of the Consumer Expenditure Survey conducted by the National Sample Survey Office during 2004-05. Food group weights in all-India CPI (Rural), CPI (Urban) and CPI (Combined) are 59.31%, 37.15% and 49.71% respectively. Remaining weights are for non-food groups i.e. housing, fuel & light, clothing & footwear and miscellaneous group.

Which index should one use?

The WPI is useful in certain contexts. For example, for industrialists, the costs of setting up a factory over the course of several years; and further to calculate the costs of production and returns over several years. The basket of items in the CPI does not include machinery, chemicals, and so on; secondly, the price of electricity in the CPI is the consumer tariffs, not the industrial tariffs; and so on.

Figures for inflation in the WPI are on the average much lower than those in the CPI indices. There could be two reasons for this difference in rates between the WPI and CPI: first, prices of the items in the CPI basket might have risen more sharply than items excluded from it — this would mean that prices of mass consumption goods have risen more sharply than inputs for production; secondly, the retail prices of commodities might have grown more sharply than the wholesale prices, indicating that middlemen have taken a bigger share.

Services and price index

While the WPI now does not include services, the two consumer price indices (CPI) meant for urban non-manual employees and industrial workers, do include certain services such as medical care, education, recreation and amusement, transport and communication. On the other hand, some of the other major services such as trade, hotels, financing, insurance, real estate and business services do not find a mention either in the WPI or in the CPIs.

In India, the services sector accounts for about 57 per cent of the GDP.

In August 2010, Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce & Industry constituted an Expert Committee to render technical advice for development of Service Price Index (SPI) and its related issues. The Committee is chaired by Prof. C. P. Chandrasekhar.

Producer price index

The process of introducing the producer price index (PPI) is also underway in India, according to Dr Abhijit Sen, Member of Planning Commission. It means prices of goods as they are sold to the wholesalers by the producers. The difference between WPI and PPI is accounted for by the margins and other transport and distribution costs.

'Core' or' Underlying Inflation'

Core or underlying inflation measures the long-run trend in the general price level. Temporary effects on inflation are factored out to calculate core inflation. For this purpose, certain items are usually excluded from the computation of core inflation. These items include: changes in the price of fuel and food which are volatile or subject to short-term fluctuations and/or seasonal in nature like food items. In other words, core or underlying inflation is an alternative measure of inflation that eliminates transitory effects .The main argument here is that the central bank should effectively be responding to the demand side- for example, the money available in the market, demand for credit and so on and not the supply shocks like energy and food. Core inflation in India on the WPI is about 2%.Headline inflation on the other hand includes the official rate of increase in prices that excludes no item in the basket. Core includes the primary articles and the food processing part of manufacturing.

Inflation Targeting

Inflation targeting focuses mainly on achieving price stability as the ultimate objective of monetary policy. This approach entails the announcement of an inflation target- either a number or a range, that the central bank promises to achieve over a given time period. The targeted inflation rate will be set jointly by the RBI and the government, the responsibility of achieving the target would rest primarily on the RBI on the demand side and supply side is that of the government. This would reflect an active government participation in achieving the goal of price stability with fiscal discipline by way of a rational borrowing programme (not borrowing in excess).

Monetary policy and fiscal policy have to converge for achievement of inflation targeting. Advantage is that it promotes transparency in the conduct of monetary policy. Further, it increases the accountability of monetary authorities to the inflation objective.

Prices impact on the macro economy in many ways – welfare of people, growth and stability of the economy in a globalised order.

We do not adopt this policy in India.

Ideal level of Inflation

Ideal inflation rate is one that takes into consideration human, social and economic impact. It is the level of inflation beyond which the adverse consequences are strong. Chakravarty Committee (1985) had indicated 4 per cent as an acceptable level of inflation on a long-term basis However, such a level of inflation cannot be fixed at one level for all times. It depends on growth rate. It also depends on what the global levels are. RBI sees about 5.5% rate of inflation as 'comfortable'- neither does it hurt in human terms nor in growth terms.

Collection of Statistics Act, 2008

Collection of Statistics Act, 2008 was made to bring in new rules aimed at improving data collection.

Government will levy higher penalty for not sharing data and tougher punishment will be imposed in cases where manipulation of data is involved, they say.

Under the new Act, people or companies not divulging data would have to pay a fine of Rs 1,000 and they would be given a 14-day notice period to comply. If the information is not provided even after two weeks, the penalty will rise to Rs 5,000 per day.

Under the old Act, which was passed in 1953, the penalty was only Rs 500 for the first default and Rs 200 per day thereafter.

The new penalty scheme will ensure that data collection is done on time. It will increase the accuracy of the data

The Act also makes wilful manipulation or omission of data a criminal offence, punishable by a prison term that may extend up to 6 months. This penalty will also apply if a company prevents or obstructs any employee from collecting data.

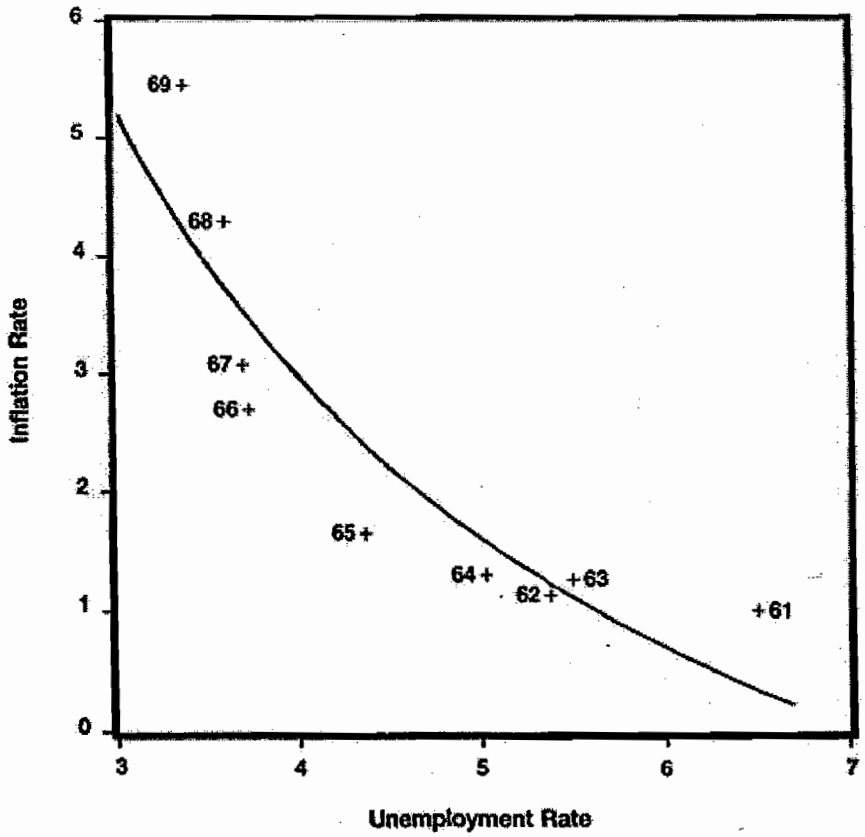
The Collection of Statistics Act, 2008, gives powers to the government to classify any statistics as "core statistics" and also determine the method to collect and disseminate the same

Philips's curve

The inverse relationship between rate of inflation and rate of unemployment is shown in the **Phillips curve:** price stability has a trade-off against employment. Some level of inflation could be considered desirable in order to minimize unemployment.

Potential output (sometimes called the "natural gross domestic product") is an important concept in relation to inflation. It is the level of GDP where the economy is at its optimal level of production, given various constraints- institutional and natural.

This level of output corresponds to the Non-Accelerating Inflation Rate of Unemployment, NAIRU. If GDP exceeds its potential, inflation will accelerate and if GDP falls below its potential level, inflation will decelerate as suppliers attempt to use excess capacity by cutting prices.



Deflation

Deflation is a prolonged and widespread decline in prices that causes consumers and businesses to curb spending as they wait for prices to fall further. It is the opposite of inflation, when prices rise, and should not be confused with disinflation, which merely describes a slowdown in the rate of inflation.

Deflation occurs when an economy's annual headline inflation indicator -- typically the consumer price index -- enters negative territory.

Deflation is hard to deal with because it is self-reinforcing. Put simply, unless it is stopped early, deflation can breed deflation, leading to what is known as a deflationary spiral.

When an economy has fallen into deflation, demand from businesses and consumers to buy products falls because they expect to pay less later as prices fall. But as producers struggle to sell and go bankrupt, unemployment rises, reducing demand further. That causes deflation to become more pronounced.

It makes it more expensive to service existing debts. This is as true of governments, who have borrowed trillions of dollars globally to prop up the financial sector, as it is for consumers.

As debt becomes more expensive to pay off, the risk of default and bankruptcy rises too, making banks more wary of lending. This reduces demand and further exacerbates the deflationary problem.

Remedy

- Tax cuts to boost demand from consumers and businesses
- Lowering central bank interest rates to encourage economic activity
- Printing more currency to boost money supply
- Capital injections into the banking system
- Increase government spending on projects that boost the return on private investment

India did not face the threat of deflation as demand has not dropped so much. Also, food scarcity meant food prices did not fall. In fact they rose.

India and deflation

On the WPI, we faced disinflation- rate of growth of prices fell but not prices themselves till the first quarter of 2009. In the second quarter and later, there was 'deflation' on the WPI. This negative inflation is due to higher base as inflation peaked in July 2008 due to international energy and food price rises because of speculation.

The deflationary phase was short lived for a few weeks as the fiscal as well as monetary measures of the government started showing results and demand and growth returned.

Growth -inflation trade off

With high growth, economy overheats. .Overheating of the economy means demand overshoots supply and there is pressure on prices. As growth creates more employment and incomes rise, demands rises pushing up prices.

As prices rise, the central bank intervenes and raises rates to cool consumption and so prices fall relatively. Repo rates- the policy rate- is the tool along with CRR and OMOs available to the central bank as signals to the economy that it is ready to act to soften prices -partly because the poor suffer disproportionately and partly because inflation can derail the medium and long term growth.

Such intervention by the central bank has a dampening impact on growth as higher interest rates prevent easy borrowing and thus demand slackens.

We witnessed the same in India with CRR and repo rates going down from 2009 for one year and later till 2011 going up in reponse to priceline in the country. Today they stand at 4% and 7.75% respectively (December 2013)The primary goal of the RBI is to moderate and stabilize prices.

Thus, growth and inflation are intimately connected- one being traded for the other depending upon where the growth situation stands.

As prices stabilise, growth resumes and a new and higher base is set for the growth process. Growth and inflation do have a trade off but that is only in the short term. As Dr.C.Rangarajan says, growth is a marathon while overheating and slow down are temporary pauses to gain greater strength.

Further, unless the RBI raises the policy rates with inflation going up, there is a danger of banks failing to attract deposits as real interest rates become negative and savings may be diverted to unproductive assets like gold with serious consequences- inside and outside for the economy.

tax bracket

Fiscal drag operates in an overheated economy. That is the tax liability increases as wages rise. That leaves less purchasing power in the hands of the people and so demands drops automatically. It acts as an automatic stabilizer.

Inflation in India

Reasons for the current inflation

In spite of the steps of the government, prices are relentlessly on rise. WPI at 7.5% and CPI above 10% in mid-2012 have many reasons

- Growth
- The bad monsoons and the decline in production raised inflationary expectations
- Even as the buffer stocks accumulated to huge surplus, governance problems and the fiscal pressures of the states prevented them from being distributed
- Narega
- MSP increases
- Fuel price deregulation for petrol and increase in the prices of diesel and LPG
- Hoarding and cartelization as in the case of food items, cement
- Middle men
- APMC Acts of States
- Diesel price deregulation in phases
- Imported inflation due to rupee depreciation since late 2011

For food inflation, Dr. Subba Rao gave the following reasons in November 2011 and they continue to be relevant

1. Shift in dietary habits towards protein foods.
2. Pressure stemming from inclusive growth policies.
3. Large increases in MSPs of food grains.
4. Shocks from global food inflation.
5. Financialisation of commodities.

Cartel- A group of manufacturers or suppliers acting together to control prices

Government steps to control inflation

The Government has taken a number of short term and medium term measures to improve domestic availability of essential commodities and moderate inflation.

It has procured record food grains. Even after keeping the minimum buffer stock, there are enough food grains to intervene in the market to keep the prices at reasonable level.

A Strategic Reserve of 5 million tonnes of wheat and rice has also been created to offload n the open market when prices are high. This is in addition to the buffer stock held by FCI every year.

Issue price of grains supplied through PDS outlets are frozen.
The price situation is reviewed periodically at high-level meetings such as the Cabinet Committee on Prices (CCP).

Fiscal Measures

- Reduced import duties on food items
- Import duties are raised on gold etc to contain CAD

Administrative Measures

- Ban on exports of food items
- Dehoarding

Monetary Measures

Repo rates were raised and CRR also went up to make credit dearer.

Inflation and corruption

The link is as follows

a. through black money
b. hoarding not being checked
c. commodity prices being manipulated through speculation as NSEL crisis shows.

Open inflation

When the government does not attempt to prevent a price rise, inflation is said to be open. Thus, inflation is open when prices rise without any interruption. In open inflation, the free market mechanism is permitted to fulfill its historic function of rationing the short supply of goods and distribute them according to consumer's ability to pay. Therefore, the essential characteristics of an open inflation lie in the operation of the price mechanism as the sole distributing agent.

Repressed / suppressed inflation

When the government interrupts a price rise, there is a repressed or suppressed' inflation. Thus, it refers to those conditions in which price increases are prevented at the present time through an adoption of certain measures like price controls and subsidies like diesel subsidy etc.

Inflation tax

Price rise means more money being paid by the consumers for what they buy. Thus, it is a type of tax.

TAXATION IN INDIA: Concepts and Policies

Tax is a payment compulsorily collected from individuals or firms by government. A direct tax is levied on the income or profits of an individual or a company. The word `direct' is used to denote the fact that the burden of tax falls on the individual or the company paying the tax and can not be passed on to anybody else. For example, income tax, corporate tax, wealth tax etc. An `indirect' tax is levied on manufacturing and sale of goods or services. It is called `indirect' because the real burden of such a tax is not borne by the individual or firm paying it but is passed on to the consumer. Excise duty, customs duty, sales tax etc.

Funds provided by taxation are used by governments to carry out the functions such as:

- military defense
- enforcement of law and order
- redistribution of wealth
- economic infrastructure — roads, ports etc
- social welfare
- social infrastructure like education, health etc
- social security measures like pensions for the elderly, unemployment benefits

Taxation System in India

India has a well developed tax structure. Being a federal country, the authority to levy taxes is divided between the central government and the state governments. The central government levies direct taxes such as personal income tax and corporate tax, and indirect taxes like customs duties, excise duties and central sales tax (CST). CST is assigned to the States in which it is collected. (Art.269). The states have the constitutional power to levy sales tax apart from various other local taxes like entry tax, octroi, etc.

Taxation has always played an important role in the formulation of the government's economic policy. Taxation policy in a developing country like India can play an important part to raise resources for growth; to bring in reduction in inequalities; to direct growth in backward regions; to reduce consumption of luxury goods; to direct investment into small scale sector; to promote savings etc. In the wake of the economic reforms, the tax structure and procedures have been rationalised and simplified. Since 1991, the tax system in India has undergone substantial rationalization- reduced rates and slabs and better administration.
Some of the changes are:

- Broadening the tax base to include services, fringe benefits, stock market transactions etc
- Reduction in customs and excise duties. Peak customs rate is today 10%
- Lowering of corporate tax rates to 30%
- Rationalizing the personal income tax rates and slabs starting from 1997 `dream budget'
- Sales tax reforms at the State level as a preliminary step towards their integration into GST
- introduction of VAT from 2005 at the state level; GST is expected to be introduced in 2011
- Simplifying income tax return filing procedures. For example, Saral, Towards better taxpayer services, in 2011-12, the IT department has introduced simple and user friendly

SAHAJ (Form) for individual salary tax-payers; SUGAM for small tax-payers availing presumptive tax scheme.(For presumptive tax, see ahead)

Tax revenue as a percentage of GDP decreased initially, after reforms began in 1991, as rates came down and growth of economy was not very robust. Compliance also did not increase proportionate to rate reduction. Since the Tenth Plan period, there has been a consistent rise in tax collections but it dipped due to global financial crisis of post-2008 period. GOI expects Rs.1.24 lakh crore for service tax collection during 2012-13 due to wider coverage and higher rate (12%).In 2011-12, the tax-GDP ratio stood at 5.5 per cent for direct taxes and 4.4 per cent for indirect taxes.

Government expected to increase its gross tax revenue by 19.5% to Rs 10.77 trillion in the financial year 2012-13.

The gross tax revenue is estimated at 10.6% of the gross domestic product (GDP) in the Budget estimates 2012-13.

Revenue from corporation tax is the highest contributor at Rs 3.73 trillion to the government's total revenue, while income tax, customs, union excise duties, and service tax yielded Rs 1.95 trillion, Rs 1.86 trillion, Rs 1.94 trillion and Rs 1.24 trillion, respectively.

Direct tax revenue growth is estimated at Rs 5.7 trillion, up 13.9% and indirect tax revenue growth is estimated at Rs 5.05 trillion, up 26.7%.

The government targeted a net tax revenue of Rs 7.71 trillion in 2012-13, after devolution to the states.

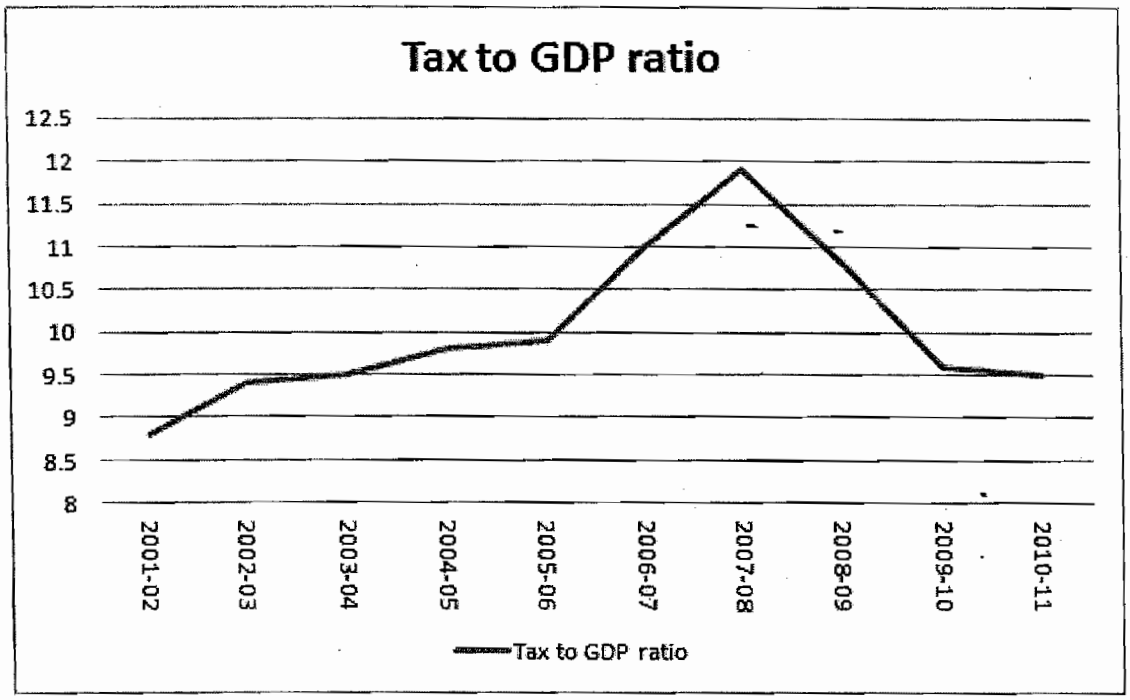
The non-tax revenue receipts are estimated at Rs 1.64 trillion and non-debt capital receipts are estimated at Rs 416.5 billion.

Expenditure:
The government's total expenditure is budgeted at Rs 14.9 trillion for 2012-13.
Of this, the plan expenditure is projected 22.13% higher at Rs 5.21 trillion.
Non-plan expenditure for 2012-13 is budgeted at Rs 9.69 trillion.

Measures for broadening tax base, strengthening compliance and simplification

- Rates and slabs are rationalized
- Negative list of services for taxation from 2012 at 12%
- adoption of VAT by almost all the states
- GST introduction
- Tax to be deducted at source on various items like interest on bank deposits; dividend distribution etc
- Quoting of permanent account number made compulsory for many transactions so more people can be brought into tax net
- securities transactions tax

Other measures suggested are: minimizing exemptions and concessions; drastic simplification of laws and procedures; building a proper information system and computerization of tax returns, and a thorough revamping and modernization of the administrative and enforcement machinery.



PROFILE OF CENTRE'S GROSS TAX RECEIPTS

(In Rs crore)

	1990-91	2000-01	2007-08	2008-09	2009-10 (BE)	2009-10 (RE)	2010-11 (BE)
DIRECT*	11024	68306	295938	319859	370000	380608	422500
Income	5371	31764	102644	106046	112850	125021	120566
Corporation	5335	35696	192911	213395	256725	255076	301331
INDIRECT	45158	118681	278845	269433	269477	244477	315000
Excise	24514	68526	123425	108613	106477	102000	132000
Customs Customs	20644	47542	104119	99879	98000	84477	115000
Service	Nil	2613	51301	60941	65000	58000	68000
TOTAL**	57576	188603	593147	605298	641079	613095	746651
DIRECT %	19.15	36.22	49.89	52.84	57.72	60.12	56.59
TAX-GDP %	10.11	8.97	11.99	10.86	10.95	10.27	10.77

*Includes taxes on interest, expenditure, estate, gift and wealth;
**Includes 'other taxes & duties' and 'taxes of Union Territories';
BE: Budget Estimates; RE: Revised Estimates.

Hierarchy can be asked in Prelims

Tax collections 2012-13

As can be seen from the table above, Government of India's tax receipts were growing healthily. It helps government spend more on social projects.

The reasons for the tax collections being so healthy till recently

- economy is growing at a satisfactory pace- 6.5% in 2011-12
- incomes of individuals have gone up
- lower tax rates help compliance
- procedures are simple and citizen-friendly
- base has been widened
- a drive has been mounted to bring more people to pay income tax with proper investigation

Direct and Indirect Taxes in India: The Changing Scenario

As can be seen from table, direct tax collections are more than indirect tax collections. In 1990-91, less than a fifth of the Centre's gross tax revenues came from direct taxes.

The biggest taxation source of the Centre now is corporate tax and next is income tax.

The general level of prosperity in the country is increasing making more people have taxable incomes. Also, when companies are growing in number and also in their profitability, corporate tax collections increase. Global opportunities mean more profits. Stock market transactions and wealth build-up also contribute to direct tax collections by way of STT, capital gains tax, income tax. Apart from the above reasons, the Government's measures as given below also helped increase the direct tax collections

- reduction of peak income tax rates that helps compliance
- reduction in the number of slabs
- strengthening the administration- e-governance etc
- simplification of laws(Saral etc)
- promote voluntary compliance (But end use of taxes is still unimproved)
- Technology; manpower

The increase in the relative share of direct tax collections shows that the tax system is becoming more progressive as direct taxes are paid by the well off in general while the indirect taxes are paid equally by all consumers. Direct taxes can be used to promote growth with equity.

Direct taxes help in income redistribution. Decline in the relative share of indirect taxes is also seen as good because it promotes the competitive nature of Indian economy-attracts investment.

By taxing earnings of individuals and corporates rather than production and trade, there is less stifling of economic activity and there is employment generation.
In developed countries, direct taxes contribute more to the tax collections.

Cost of direct tax collection

Buoyant economic growth along with higher tax compliance have led to a desirable decline in the cost of direct tax collections as a proportion of total direct tax collections: all-time low of 0.54 per cent in 2007-08.That is, the income-tax department spends 54 paise for every Rs 100 direct tax collected by it, which is among the lowest in the world. The income tax department has a tax base of 3.5 crore assesses..

Income-tax slabs and rates

10 per cent rate on a slab extending up to Rs 5 lakh. Likewise, the 20 per cent rate will now apply on income slabs beyond Rs 5 lakh and up to Rs 8 lakh. The maximum marginal rate of 30 per cent on an income slab of above Rs 8 lakh.

Service Tax

Service tax was first imposed in 1994. A new service tax regime, based on a negative list of exempted services, came into effect in July 2012.

With this, all services — except the 38 activities put on the negative list — came under the tax at the increased rate of 12 per cent, as announced in the Union budget 2012-13.

Till June 2012, service tax was being levied on 119 services based on a positive list. The switch-over to a negative list-based approach is aimed at aligning the indirect taxation system to the proposed Goods and Services Tax (GST) regime, which is sought to be introduced to unify the levies of the Centre and the States into a composite system.

With the services sector now accounting for 60 per cent of the gross domestic product, the Finance Ministry has set a target of Rs.1.24 lakh crore for service tax collection during 2012-13. This is significantly higher than the Rs.97,000 crore mopped up during the previous fiscal.

As per the negative list-based approach, services such as metered taxis, auto-rickshaws, transport of goods or passengers and transmission and distribution of electricity by distribution companies will not come under the service tax net.

Other important services exempted from the levy are solemn activities such as funeral, burial and transport of deceased. In the education sector, school and university courses, as also approved vocational studies, have been exempted.

Likewise, auxiliary educational services and renting of immovable property by educational institutions in respect of education will not be taxed. However, coaching classes and training institutions will be taxed.

Among the other services included in the negative list are those provided to government, local authorities or a government authority for repair and maintenance of an aircraft. Likewise, services provided by advocates to other advocates and business entities up to a turnover of Rs. 10 lakh in the preceding financial year will be exempt from the tax.

Services provided by way of public convenience, such as bathroom, washroom, urinals or toilets, are included in the negative list, just as services relating to work contracts for a scheme under the Jawaharlal Nehru National Rural Urban Renewal Mission or the Rajiv Awas Yojana.

The service sector has emerged as an important area of economic activity. Reasons for taxing services

- Its share in the country's Gross Domestic Product (GDP) has increased from about 28% in 1951, to 55% (2011).
- Taxing services is important to raise resources and increasing the tax-GDP ratio
- service providers should share the tax burden with others-industry - there should be horizontal equity that is all sectors of the economy should bear the tax burden equitably.
- as the share of industry in GDP decreases while that of services expands, the tax base shrinks unless services are taxed.
- failure to tax services distorts consumer choices, encouraging spending on services at the expense of goods and savings.
- as most of the services that are likely to become taxable are positively correlated with expenditure of high income households, subjecting them to taxation will improve equity.

Service Tax and Indian Constitution

In the Seventh Schedule to the Constitution, under Article 246, the item relating to "taxes on services" was not specifically mentioned in any entry either in the Union List or in the State List.

However, Entry 97 of the Union List empowers Parliament to make laws in respect of any other matter not enumerated in List II (State List) or List III (Concurrent List), including any tax not mentioned in either of those lists. Since "taxes on services" is not there in any of the lists, service tax was levied by the Central Government in exercise of the powers under Entry 97 of the Union List.

The 88th amendment to the Constitution(2004) amended Article 270 (made it divisible)and inserted in the Union List (List I) entry No. 92C — `taxes on services'.

The amendment to the Constitution places services tax formally under the Union List. This will pave the way for the Centre to levy and collect the tax.

The amendment becomes redundant with the introduction of GST in 2011 where the services will be jointly taxed by Centre and States.

The amendment did not come into effect as it has never been notified and thus services are still taxed on a residuary basis.

GST

Goods and Services Tax is a multi-point sales tax with set off for tax paid on purchases of inputs. There is no cascading (tax on tax) effect as there is deduction or credit mechanism for taxes paid for the inputs. The tax is levied on the value added and on consumption only. Total burden of the tax is exclusively borne by the domestic consumer. Exports are not subject to GST.

India introduced VAT at the state level in 2005. Before that, union excise duties were renamed Central Vat (Cenvat). But when states called their slaes tax Vat, centre reverted to the earlier name of excise duty. The earliest form of Vat was however taken in 1986 in the form of Modvat- modified VAT that included set off for a few commodities only and was confined to excise duties only.

Cenvat in replacement of central excise duties came into effect earlier in the decade. VAT as a replacement for state sales tax was adopted from the beginning of the fiscal year 2005-2006.Cenvat has come back to being called union excise duty to prevent confusion.

Need for GST

In the Union Budget for the year 2006-2007, Finance Minister proposed that India should move towards national level Goods and Services Tax that should be shared between the Centre and the States. World over, goods and services are integrated and taxed as a comprehensive domestic indirect taxation system based on value addition. They attract the same rate of tax. That is the foundation of a GST. The basis of GST is value addition.

The goods and service tax (GST) is proposed to be a comprehensive indirect tax levy on manufacture and sale of goods as well as services at a national level. Integration of goods and services taxation would give India a world class tax system and improve tax collections.

It would end the long standing distortions of differential treatments of manufacturing and service sector. The introduction of goods and services tax will lead to the abolition of taxes such as octroi, Central sales tax, State level sales tax, entry tax, etc and eliminate the cascading effects tax on tax.

It is aimed at forging a common domestic market, removing multiplicity of taxes, eliminating the cascading effect of tax on tax, making the prices of the Indian products competitive and, above all, benefiting the end consumers

GST: Q and A

The central and state governments moved closer to ushering in a nationwide goods and services tax on April 1, 2011, a reform intended to cut business costs and boost government revenue. The reform would eliminate multiple indirect taxes levied by states and the central government, leading to a reduction in the average tax burden on companies and a rise in the country's tax-to-GDP ratio.

HOW WILL THE GST WORK?

The GST is an indirect tax that would replace existing levies such as excise duty, service tax, and value-added tax (VAT).Both the states and the central government would impose the tax on almost all goods and services produced in India or imported. Exports would not be subject to GST. For the first two years of operation, the proposal is for two rates both at the federal and state levels, converging to a single rate in the third year. Producers would receive credits for tax paid earlier, which would eliminate multiple taxation on the same product or service. Direct taxes, such as income tax, corporate tax and capital gains tax would not be affected.

WHAT'S THE RATIONALE FOR THE GST?

Eliminating a multiplicity of existing indirect taxes would simplify the tax structure, broaden the tax base, and create a common market across states and centrally administered districts. Increased compliance and fewer exemptions to GST would lift India's federal tax-to-GDP ratio.

At the same time GST would lower the average tax burden for companies that now pay "cascading" taxes on top of taxes through the production process.

By lowering business costs it would boost economic growth and increase exports, proponents argue, and bring India in line with practices in many developed economies.

Reducing production costs would make exporters more competitive.

The GST may usher in the possibility of a collective gain for industry, trade, agriculture and common consumers as well as for the central government and the state governments for reasons cited above.

Black money and evasion will reduce as GST is transparent.

WHAT ARE THE PROPOSED GST RATES?

For the first year: 10 percent of CGST of Centre and 10% of SGST of states for goods and 6 percent each for essential items. 8% each for services. Thus, it is dual rate. Also, goods and services are taxed separately initially.

↳ State & Centre

The higher rate would come down to 9 percent in the second year, and the two rates would converge at 8 percent in the third year.

ARE THERE EXEMPTIONS PROPOSED?

Yes. Goods deemed necessary or of basic importance would be taxed at a lower rate. The government will review the various lists of exempted goods to align them at the federal and state levels.

Alcohol, petroleum and electricity would not come under GST. (Since GST has levied on experimental basis)

WILL THE STATES LOSE OUT?

GOI will compensate states for potential lost revenue and central government has assured states that if needed, it would increase a 50,000 crore -rupee ($10.6 billion) fund that the 13th Finance Commission recommended as an incentive for the states to buy into GST.

WHAT HAPPENS NEXT?

The legislation to make constitutional amendments needs to be finalised and the mechanism for administering the tax needs to be created. The government also needs to set up the technology infrastructure to manage the tax- TAGUP (see ahead)

WHAT IS THE REVENUE IMPACT?

The GST is initially intended to be revenue-neutral but is eventually expected to increase the tax collections due to more efficient collection, expanded base, transparency and increased compliance.

WHAT ABOUT THE ECONOMIC IMPACT?

Implementation of a comprehensive GST would lift India's economy of over $1 trillion by between 0.9 percent and 1.7 percent, according to a report by the New Delhi-based economic think tank the National Council of Applied Economic Research. Exports would rise by between 3.2 percent and 6.3 percent, while imports would increase 2.4 percent to 4.7 percent, the study found.

Constitutional Amendment for GST

Constitution (One Hundred and Fifteenth Amendment), Bill, 2011 (GST Bill)

Constitution (One Hundred and Fifteenth Amendment), Bill, 2011 (GST Bill) was introduced in the Parliament in the budget session in March 2011, deals with GST. The Bill seeks to introduce Goods and Services Tax (GST) and the GST Council. As per the existing structure of indirect taxation, the Parliament has the power to make laws on the manufacture of goods and the provision of services (Union List) while the State Legislatures have the power to make laws on the sale and purchase of goods within their respective states (State List). The Parliament has retained the exclusivity to make laws pertaining to sale of goods in the course of inter-state trade or commerce.

Definition of Goods and Services – Article 366

1. The above Article which defines 'Goods and Services Tax' to mean, any tax on supply of goods or services or both except taxes on the supply of petroleum products and alcohol

Seventh Schedule

- The Union Government has the exclusive power to levy excise duty on the manufacture or production of
- Petroleum Crude
- High Speed diesel
- Petrol
- Natural Gas
- Aviation Turbine Fuel
- Tobacco and Tobacco Products

The State Governments shall have the power to levy tax on the sale (other than in the course of inter-state trade or commerce) of petroleum crude, high speed diesel, petrol, natural gas, aviation turbine fuel and alcoholic liquor for human consumption.

Article 249

The Parliament has been vested with the power to make laws pertaining to GST on behalf of the state Legislature in circumstances of national interest. The power to make such laws would be pursuant to a resolution passed by the Council of States supported by not less than a two-thirds majority of the members present and voting.

Power of Parliament to make laws on subjects in State List in the case of Emergency – Article 250

The Parliament has been vested with the power to makes laws pertaining to GST on behalf of the State Legislature when there is a proclamation of Emergency.

GST Council – Article 279A

The President shall constitute a GST Council within sixty days from the Commencement of the GST Act.

Membership of the GST Council

The Union Finance Minster would be the Chairperson, the Union Minister of State for Revenue shall be one of the members, the Finance Minister or any other minister nominated by each State Government shall be the members of the GST Council.

The Members of the GST Council shall decide on the Vice-Chairperson of the GST Council for such period as decided by the members.

Functions of the GST Council

The GST Council while being guided by the need for a harmonized structure goods and services tax and for the development of a harmonised national market for goods and services shall make recommendations to the Union and the States on:

Taxes, cesses and surcharges levied by the Union and the States and local bodies which may be subsumed within the GST

- Exemptions from GST for such goods and services
- Threshold limit of turnover below which GST may be exempted
- The GST rates
- Any other matter relating to GST

Every decision of the GST Council taken at a meeting shall be with the consensus of all the members present at the meeting.

GST Dispute Settlement Authority – Article 279B

The Parliament, by law, will provide for the creation of a Goods and Services Tax Dispute Settlement Authority (DSA) which shall adjudicate any dispute or complaint referred to the DSA by the State Government or the Union Government arising out of deviation from any recommendation of the GST Council which results in the loss of revenue to the State Government of the Union Government or affects the harmonised structure of the GST. The DSA shall consist of three members namely, the Chairperson, who has been a Supreme Court Judge or the Chief Justice of a High Court, appointed by the President, recommended by the Chief Justice of India; the remaining members shall be persons who shall have expertise in the field of law, economics or public affairs appointed by the President recommended by the GST Council.

The DSA shall pass suitable orders including interim orders only the Supreme Court shall exercise jurisdiction over such adjudication or dispute or complaint.

Fiscal autonomy issues

Constitutional amendments are required to enable the Centre and the states to impose tax on the same base of goods and services. Currently, the states cannot impose tax on services. They also can not impose tax on manufacturing of goods. Centre cannot levy tax sales tax. States feel that their fiscal autonomy is being eroded for the following reasons:

- they are surrendering the power to tax sales
- they can not change rates according to their fiscal needs
- all states can not have the same rates
- centre may not compensate the states fully

The position of states is rejected on the other points for the following reasons

- centre is also surrendering and sharing its powers regarding service tax and union excise duties.
- states are free to tax sin goods like liquor and also the petroleum products

It is said that like VAT, GST would also increase the revenue of the states as they will have powers to impose tax on services, which are growing at a rapid pace. However, in case..... (in the classroom)

Contentious federal issues on GST

GST rates, the division of taxing powers between the Centre and the states, compensation amount; exemptions and on certain design elements of the GST.

Goods and Services Tax (GST): Challenges for implementation

The GST is a necessary condition for a common market to exists, this permits free and unimpeded movement of goods and services across a federation, thus encouraging efficient regional specialization.

Such harmonization will significantly reduce the vertical imbalance between the Centre and the states by enhancing the tax base of the states. It is going to be the biggest ever tax reform in India.

Challenges to address:

- Integration of a large number of Central & State Taxes
- multiplicity of taxes and tax rates to be unified
- federal distribution of powers to levy and collect taxes
- necessary constitutional amendments.
- Rationalisation of thresholds and exemption limits.
- Standardisation of systems and procedures.
- road based computerizations across the Nation.
- Dispute settlement procedure and machinery.
- Training of tax administrators and assessee.
- Protecting and balancing the present and future revenues of the Centre and the States.
- Safeguarding the interests of less developed States with lower revenue potential.
- Taxing of Alcohol, tobacco, petroleum products which are out of the GST regime.

GST and fiscal federalism

Being the largest indirect tax reform requiring the centre and the states to adjust their constitutional taxing powers, GST has opened up fiscal federal challenges like never before. There is mutual surrender of powers to a uniform national taxation system where both gain. But there are apprehensions of loss of fiscal autonomy by states and central dominance as mentioned above.

The Constitutional changes proposed and being debated by the Empowered Committee of State Finance Ministers are likely to bring the federal units together for a new and innovative system of fiscal federal sharing and cooperation.

Technology Advisory Group for Unique Projects (TAGUP)

An effective tax administration and financial governance system calls for creation of IT projects which are reliable, secure and efficient. IT projects like Tax Information Network, New Pension Scheme, National Treasury Management Agency, Expenditure Information Network, Goods and Service Tax, are in different stages of roll out. To look into various technological and systemic issues, Finance Minister announced in the Union Budget 2010-11 to set up a Technology Advisory Group for Unique Projects under the Chairmanship of Shri Nandan Nilekani. It has been set up in mid-2010.

GST and tax efficiency

In the system existing now, the rates, tax imposition and collection are inefficient. Rates are not efficient as they depend on lobbying and there is no transparent basis. Exemptions are also similarly granted. Thus, deployment of labour and land along with capital and enterprise becomes subject to lower returns and waste- GST is expected to lead to efficient allocation of factors of production thus leading to gains in GDP and exports. This would translate into enhanced economic welfare and returns to the factors of production, viz. land, labour and capital. In an earlier taxation system, people paid taxes at various levels. There was no system of getting a rebate on the taxes paid previously while paying the inputs. This is also called as cascading effect. It is irrational as there is tax on tax. Ideally the taxes should be based on value addition and the producer should pay taxes on whatever value he adds to the product. In the absence of such a system, producers ended up paying much higher taxes. Higher taxes are a barrier for business and discourage business activity.

Rebate
A partial refund

High taxes also lead to lobbying activities where producers of a certain sector ask the government to lower/waiver taxes for their sector. This also leads to multiple taxation rates for multiple products and further increases inefficiency in the system.

Before VAT States had sales taxes with multiple rates. States were often seen in a sales tax war with other states- rate war as it is called . In the war states competed with each other offering lower tax rates to certain industries to set units in their states. This resulted in revenue loss for both the states and investment decisions wre determined by tax rates in states and not other merit factors.

However, the design of VAT system in each state has also been done in a uniform fashion keeping the distinctive state economy in mind.

Tax Reforms in India

Since the beginning of the last decade as a part of the economic reforms programme, the taxation system in the country has been subjected to consistent and comprehensive reform.

The need for the tax reforms arises from the fact that

- tax resources must maximised
- international competitiveness must be imparted to the Indian economy
- transaction costs must be reduced
- the high-cost nature of Indian economy needs to be corrected so that
- compliance increases
- equity improves
- investment flows

On the direct tax front, the reforms are the following:

- Reduction and rationalization of rates- there are only three rates of income tax today with the highest rate at 30%
- Simplification of procedures
- Strengthening of administration
- Widening of the tax base to include more tax payers in the tax net
- Exemptions are gradually being withdrawn.
- MAT was introduced for the `zero tax' companies
- The Direct Tax Code of 2010 is meant to replace the outdated Income Tax Code of 1961

Indirect Taxes

- Reduction in the peak tariff rates- 10% is the peak customs duty today which was more than a 90% reduction since 1991.
- The number of slabs has come down drastically
- There is a progressive change from specific duty to ad valorem tax
- VAT is introduced
- GST is being rolled out
- Negative list of service tax from 2012

Tax expenditure

Tax expenditure refers to revenue forgone as a result of exemptions and concessions (personal, corporate, indirect tax). It was introduced for the first time in 2006-07 Union Budget. The revenue foregone due to tax incentives in 2009-10 is estimated at Rs 5,40,269

crore. Such exemptions have been justified for promoting balanced regional growth; dispersal of industries; neutralisation of disadvantages on account of location; and incentives to priority sectors, including infrastructure. These should be subject to a sunset clause, as tax exemptions often create pressure groups for their perpetuation.

While some may be justified as they enhance investment and generate nmore taxes for the government, others are not.

Such exemptions and concessions can distort resource allocation and stunt productivity. They also result in a multiplicity of rates, legal complexities, classification disputes, litigation etc. If these exemptions are rationalized, they can help the government spend more on social and infrastructure and help reduce the fiscal deficit.

Tax havens and G20

A **tax haven** is a country or territory where certain taxes are levied at a low rate or not at all. Individuals and/or corporate entities can find it attractive to move themselves to areas with reduced or nil taxation levels. This creates a situation of tax competition among governments. Different jurisdictions tend to be havens for different types of taxes, and for different categories of people and/or companies. For example, income tax, wealth tax or corporate tax etc.

The important features of a tax haven arte:

- nil or nominal taxes;
- lack of effective exchange of tax information with foreign tax authorities, that is, personal finance information is not shared with other countries
- no requirement for a substantive local presence; and
- self-promotion as an offshore financial center.

OECD

Switzerland, Singapore, the Cayman Islands, Monaco, Luxembourg and Hong Kong are among 45 territories blacklisted by the Organisation for Economic Co-operation and Development and threatened with punitive financial retaliation for their banking secrecy. Among the sanctions being considered by the G20 are the scrapping of tax treaty arrangements, imposing additional taxes on companies that operate in non-compliant countries and tougher disclosure requirements for individuals and businesses that use shelters.

Words

Tax-incidence: It shows the entity on whom tax is imposed. It is different from the tax burden as shown below: if government increases tax on petrol, oil companies may absorb it if competition is intense or they may pass it on to private motorists. Tax incidence here refers is on companies and the burden may be on the consumer.

Tax Burden: It means those who actually pay taxes- from whom tax is collected. Depending on the market forces involved, a tax can be absorbed by the seller or by the buyer (in the form of higher prices), or by a third party like sellers' employees in the form of lower wages.

Tax Base: The value of goods, services and incomes on which tax is imposed. When economists speak of the tax base being broadened, they mean a wider range of goods, services, income, etc. has been made subject to a tax. In the case of income tax, the tax base is taxable income. Some kinds of income are excluded from the definition of taxable income, such as savings. For sales tax, the tax base is the value/volume of items that are subject to tax; essential goods , for example, are not part of the tax base.

Tax rate: It indicates how much tax is due from each source. Some tax systems have high rates but have a narrow base allowing generous deduction of business expenses. Other tax systems have a wide base with few exemptions and lower rates.

Tax Shelters: Any technique which allows one to legally reduce or avoid tax liabilities. It is a way in which the taxpayer can invest his income in a particular kind of investment that gives tax concessions.

Difference between tax avoidance and tax evasion: There are provisions in the law that allows one to save and invest in a manner that leads to reduction in taxable income. If these provisions are used for the benefit, it is called tax avoidance. It is lawful to take all available tax deductions.

Tax evasion, on the other hand, is a punishable offence. Tax evasion typically involves failing to report income, or improperly claiming deductions that are not authorized.

Hidden taxes: are taxes that are concealed in the price of articles that one buys. Hidden taxes are also referred to as implicit taxes. The most well-known form of the hidden tax is the indirect tax. Examples of hidden taxes are import duties.

Proportional, progressive and regressive tax
An important feature of tax systems is whether they are proportional tax (the tax as a percentage of income is constant over all income levels), progressive tax (the tax as a percentage of income rises as income rises), or regressive tax (the tax as a percentage of income falls as income rises). Progressive taxes reduce the tax incidence on people with smaller incomes, as they shift the incidence disproportionately to those with higher incomes.

Specific duty: Weight or quantity or number is the basis for taxation.
Ad Valorem - A Latin term meaning "according to worth," referring to taxes levied on the basis of value. Taxes on real estate and personal property are ad valorem. Luxury goods are taxed higher even if they weigh the same or number the same as ordinary goods.

Compound duties are a combination of value and other factors based on which tax is imposed.

Excise Duty: Excise duty is a tax on manufacture and is levied on the manufacture of goods within the country.

Customs Duty: When goods are imported or exported, customs duty is imposed and collected by the Union Government. Peak customs duty today is 10%.

Negative income tax: Subsidy is a negative income tax. It is a taxation system where income subsidies are given to persons or families that are below the poverty line. The government will send financial aid to a person who files an income tax return reporting an income below a certain level.

Pigovian tax
The Pigovian tax is imposed on bodies that have a negative externality. For example, pollution. Externality means impact of one person's actions on the well being of an outsider (bystander or third party). For example, the seller and consumer of cigarettes together will

harm the third person with pollution. Example of negative externality is exhaust fumes from automobiles. Positive externality refers to a good effect on the third party. For example, restoration of historic buildings, research into new technologies. Carbon tax is one example in the context of the need to discourage fossil fuels and encourage renewable sources due to climate change threat.

Octroi: Entry 52 of the State List, VII Schedule, which specifies tax on the entry of goods into a local area is the octroi. Octroi has been a main source of revenue for most of the urban local bodies in India. It is criticized for the fact that it is an obsolete method of tax collection; and involves stoppage of vehicles at the check posts outside the city limits, thereby obstructing a free flow of vehicular traffic; waste of business hours; loss of fuel etc.

-ve buoyancy ↓ growth↑; tax collection↓

Tax Buoyancy: It refers to the percentage change in tax revenue with the growth of national income. That is, growth-based increase in tax collections.

Tax Elasticity: Tax elasticity is defined as the percentage change in tax revenue in response to the change in tax rate and the extension of coverage. Buoyancy, on the other hand is the response to economic growth when the base increases but there is no change in the rate.

Tax Stability: It means no frequent changes and continuity of policy in a predictable and transparent manner. Although revenue from different taxes varies from year to year, revenue stability is desirable because it makes it easier for a government to build a credible spending and borrowing plan for the year ahead. Taxes whose revenue is relatively stable contribute to overall revenue stability. Market players also can plan better.

Tobin tax

James Tobin, an economist, proposed a worldwide tax on all foreign exchange transactions- when foreign capital enters a country and when it leaves. The aim is to check speculative flows. Long term investment – generally FDI, will not suffer as it does not invest for speculative (short term) reasons like FIIs.

Tobin justified the tax on two grounds.

First, it would reduce exchange rate volatility and improve macroeconomic performance.
Second, the tax could bring in revenue to support for development efforts or exchange rate stabilization.

The defining characteristic of a Tobin tax is that the tax is levied twice- once when one acquires foreign exchange, and again when one sells the foreign exchange.

The south East Asian currency crisis (1997) is attributed to the `dynamics of hot money'(portfolio investments or FII flows).

Tobin tax can be imposed only if all the countries accept the proposition. Otherwise, FIIs can go to countries where the tax is not imposed.

India does not prefer it as we need foreign inflows as we are a CAD country and don't have a surplus.

In the EMU, there is a proposal to see a microtax levied at 0.1% on share and bond transactions, and 0.01% on deals involving complex securities such as derivatives. It is called

the Financial Transaction Tax. The FTT, or "Tobin tax" as it is also known is a "Robin Hood tax", - collected from speculators and used for rescuing the financial system when there is such a need. Angele Merkel and Francois Hollande both want it.

India and FTT

Group of-20 saw the European countries like Germany and France propose a tax on their transactions so that fund could be mobilised in order to bail out future bank failures. The idea is to avoid taxing ordinary people. India along with Brazil and other countries opposed it on the following grounds

- Regulation is the remedy
- Banks can pay the tax and not shed their reckless behavior
- It may in fact induce them to be more reckless as there is a ready fund available and bailout is guaranteed
- India has a well regulated banking system and so did not suffer the same fate as the banks in developed economies. The problems of the advanced countries should not be imposed on others
- banks, as private entities, would simply push the added costs onto consumers.

India has a similar tax though not for the same purpose- securities transaction tax (STT)

Minimum Alternative Tax (MAT)

Normally, a company is liable to pay tax on the income computed in accordance with the provisions of the Income Tax Act, but the profit and loss account of the company is prepared as per provisions of the Companies Act. There were large number of companies who show book profits as per their profit and loss account (according to the Companies Act) but do not pay any tax by showing no taxable income as per provisions of the Income Tax act . Although the companies show book profits and may even declare dividends to the shareholders, they do not pay any income tax. These companies are popularly known as Zero Tax companies. In order to bring such companies under the income tax act net, MAT was introduced in 1996. They are required to pay MAT at 18% (2012).

Book profit is Profit which is notional made but not yet realized through a transaction, such as a stock which has risen in value but is still being held. It is also called unrealized gain or unrealized profit or paper gain or paper profit.

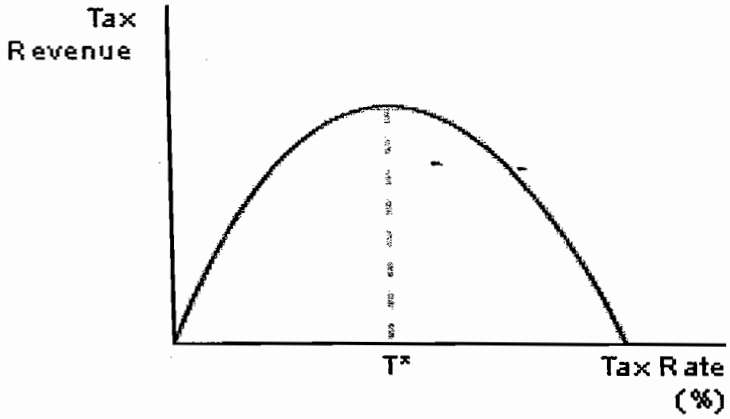
Presumptive Tax

Presumptive Tax the Estimated Income Method of assessment for certain categories of businesses is prevalent in several countries. Presumptive taxation involves the use of indirect means to ascertain tax liability, which differ from the usual rules based on the taxpayer's accounts. The term presumptive is used to indicate that there is a legal presumption that the taxpayer's income is no less than the amount resulting from application of the indirect method.

The reason for the presumptive tax is that in a number of businesses the assessees do not maintain books of accounts or the books of accounts maintained are irregular and incomplete. It was introduced in India in the early nineties for traders but was withdrawn as the success rate was low.

Laffer curve

Developed by Arthur Laffer, this curve shows the relationship between tax rates and tax revenue collected by governments. The chart below shows the Laffer Curve:



The Laffer curve has been debated in the country since 1997-1998 Budget reduced rates and slabs in the income tax regime in the country.

Inverted duty structure

Higher import duty on the raw materials than on the finished product are called inverted duty structure .It puts the domestic manufacturers at a disadvantage making them uncompetitive. For instance, compact fluorescent lamps (CFLs), where the import duty on raw materials for manufacturing CFLs is 9.7 per cent more than on finished bulbs. This skewed duty structure makes domestic CFL manufacturers uncompetitive.

There is no Basic Customs Duty for import of solar cells and modules. However, under the existing duty structure, the inputs (like EVA, Tedlar, Toughened Glass) which go into the manufacturing of solar cells and modules attract duty .This results in an inverted duty structure, which favours the import of the cells / modules and puts the domestic manufacturers to a disadvantage.

Similarly, if rubber is imported at a higher duty than tyre, manufacturing in India is discouraged.

The Economic Survey (2010-11) said FTAs also lead to a new type of inverted duty structure with duties for final products being lower from FTA partners compared to duties for the previous-stage raw materials imported from non-FTA countries. "This acts as a disincentive to local manufacturing which is not competitive against FTA imports because of the inverted duty structure phenomenon," the Survey said.

Import duty on raw silk is more than silk fabric (2013 December)

Dividend Distribution tax

Companies giving dividend have to pay tax on the amount distributed as dividend.

Withholding tax

It means withholding of tax from certain payments including interest, salaries paid to employees, professional fee, payments to contractors etc. It is the same as TDS.

Capital gains tax

It is the tax on the gains made from buying and selling assets like land, shares etc.

Bought at 10 sold at 12 gain = 2 tax on Rs 2 gain tax

If the gain is made in the assets held for over three year (one year for shares) , it is called long term capital gain and taxed. For shares, there is no long term capital gains tax. For short term capital gains (less than one year), it is 15% for shares.

Wealth Tax

When income accumulates into wealth, it gets taxed after a point. Wealth tax is levied only in respect of specified non-productive assets such as residential houses, urban land, jewellery, bullion, motor cars etc.

Securities transaction tax

Introduced in the Union Budget 2004-2005, it is a tax on the value of all the transactions of purchase of securities that take place in a recognised stock exchange of India. It is meant to make up revenue loss from the abolition of long term capital gains tax.

main & Prelis

Transfer Pricing

Transfer pricing involves charging for goods supplied to the subsidiary. The international norm in this regard is the 'arms length principle' which means that when two related parties deal in goods and services, pricing must be done objectively and commercially. If the principle is not followed, it means losses for the government. For example, an MNC has a subsidiary in India and elsewhere. The corporate tax rates are high in India. Therefore, the price of goods sold by the MNC to the two subsidiaries in the two countries is shown differently- higher in India and less in the other country. In that case, Indian subsidiary shows less profits or more losses and tax liability (corporate tax) is less.

TP also applies to linked companies like ITC, Tata.

Thus, transfer pricing is generally done in a way as to show high profit in countries where the corporate tax rate is low and low profits/losses where the rate is high. Therefore, transfer pricing norms existing today need to be rationalised so that the tax revenues that are due to the government are not eroded. Tax evasion and money laundering has to be checked by tightening the transfer pricing regime.

Nike (MNC) having subsidiaries at India & Srilanka

Profit tax in India is 30% & in Srilanka 10%

So Nike will sale a shoe to subsidiary at higher price in India. so that the subsidiary will gain less profit. & so profit tax ↓.

The introduction of Advance Pricing Agreement (APA) under Transfer Pricing Regulations in the union budget of year 2012 -13 is positive step to reduce the litigation as it will be based on bilateral understanding between two countries.

According to the memorandum of union budget, Advance Pricing Agreement is an agreement between a taxpayer and a taxing authority on an appropriate transfer pricing methodology for a set of transactions over a fixed period of time in future. The APAs offer better assurance on transfer pricing methods and are conducive in providing certainty and unanimity of approach.

Death tax (in the class)

Rupee is raised and spent like this

For every rupee in government kitty, 29 paise will come from market borrowing in 2012-13.

The government's dependence on debt has gone up from 27 paise in the previous Budget to 29 paise in the coming year, reflecting the pressure on revenue collections.

The net borrowings of the government in 2012-13 are pegged at Rs 4.79 lakh crore against Rs 4.36 lakh crore for the current fiscal.

On the expenditure side, central Plan will account for an outgo of 22 paise, followed by 18 paise of interest payments.

Defence allocation has been maintained at 11 paise. As the single largest source of revenue income, the collection from corporate tax has decreased to 21 paise to 24 paise as a per centage of every rupee earned, indicating the sluggish growth in the industry.

However, with increase in the service tax rate, the government expects revenue collection from service tax and others to go up to 7 paise against 6 paise in 2011-12.

Besides, other indirect tax component excise and customs would earn 21 paise for the government.

Despite tax incentives given to individuals, direct tax contribution has been retained at 9 paise.

With rising crude oil price due to global economic uncertainty, the subsidy burden on the government would go up 10 paisa against 9 paise for the year ending March 2012.

At the same time, other non-plan expenditure is expected to account for 11 paise of every rupee spent by the government in 2012-13, while the states' share of taxes and duties would amount to 17 paise of every rupee earned.

Plan assistance to states and Union Territories has been retained at 7 paise in 2012-13. (Figures to be revised after the General Budget is presented in June 2014).

- (027)(9) counter vailing duty (google)
  - To level field betn domestic producer & foreign exporter. If one country is subsidizing more than other country to which it exports.
- Safeguard duty (028) (google)
  - To safeguard insignificant producer against the exporting country.
  - So state will put some duty on ~~producer~~ imported goods for some transitional period.
  - These need to be compensated somewhere (← google)

Any body/corpus meant for special Purpose undisturbed by dynamics of entity which is keeping it.

- ~~Round tripping~~
- Dual pricing (6 min) ✓ (previous)

eg:- Sugar
10% levy ; 90% market price

eg:- LPG
9 cylinders ; others at market price

- Round tripping

Indian money coming to India through country having DTAA with India.
(with 80 countries)

Mauritian company only.
↳ even USA company having (021) address of mauritius (residency) - so they are called mail box/Post box company

- Treaty shopping

Choosing a ~~st~~ country with required treaty so that it can benefit us.

- ~~LOB (9 min) (021)~~
- GAAR (11:)
- General Anti Avoidance Rule

Tax is liable if actions/deals done to avoid tax deliberately

- eg: vodafone
- domestic law
- LOB (022) ✓ (023)
- Safe harbour rule (like GAAR)
- only after that you can claim advantages of DTAA.

- GST (024) (Aug) ✓

(Selling of company should not be based on tax rate)

- To avoid tax on tax
- Deciding floor (14 min)

VAT
- To avoid arbitrary taxation
- valued added tax
↓
goods

- (025) Cenvat

Union excise duty ~~was~~ subject to value addition

- Modvat

limited vat. for few commodities.

- How ~~Cenvat~~ vat or state's Sale tax
- Cenvat → union excise duty.
- Benefits of GST (9 min)
- State's opposing
  - Council dominated by centre
  - State had monopoly on ~~Sales~~ service tax,
- Advantages of GST.

google - Inverted duty structure (026)

- Peak customs duty (5) ✓
- Anti dumping duty (027) ✓
- Less than fair value

less than MP of your country

eg: Selling chinese product in china at 10 & selling same at 9 in India.

→ Reasons
- Production ↑ inventory problem
- So to avoid dumping ADD is imposed provided domestic (India) manufacturer is hurt

Final (Growth oriented tax system)

Banking System in India-I

A commercial bank is a type of financial intermediary. It is a financial intermediary because it mediates between the savers and borrowers. It does so by accepting deposits from the public and lending money to businesses and consumers. Its primary liabilities are deposits and primary assets are loans and bonds.

"Commercial bank" has to be distinguished from another type called "investment bank". Investment banks assist companies in raising funds in the capital markets (both equity and debt), as well as in providing strategic advisory services for mergers, acquisitions and other types of financial transactions. It is also called merchant bank.

The commercial banking system in India consists of public sector banks; private sector banks and cooperative banks.

Currently, India has 88 scheduled commercial banks (SCBs) - 26 public sector banks (that is with the Government of India holding majority stake) that include SBI and its associates and the IDBI Bank; there are private banks and foreign banks also. Public sector banks hold over 75 percent of total assets of the banking industry, with the private and foreign banks holding 18.2% and 6.5% respectively

Public Sector Banks

They are owned by the Government- either totally or as a majority stake holder.

- State Bank of India and its five associate banks called the State Bank group
- 19 nationalised banks(earlier there were 7 associate banks but recently 2 were merged with SBI- SB of Saurashtra and Indore)
- Regional Rural Banks mainly sponsored by Public Sector Banks

Private Sector Banks include domestic and foreign banks

Co-operative Banks are another class of banks and are not considered as commercial banks as they have social objectives and profit is not the motive. (Explained later)

Reserve Bank of India lays down the norms for banking operations and has the final supervising power.

Development Banks

Development Banks are those financial institutions which provide long term capital for industries and agriculture : Industrial Finance Corporation of India (IFCI) ;Industrial Development Bank of India (IDBI) ;Industrial Credit and Investment Corporation of India (ICICI) that was merged with the ICICI Bank in 2000 ;Industrial Investment Bank of India (IIBI) ;Small Industries Development Bank of India (SIDBI) ;National Bank for Agriculture and Rural Development (NABARD) ;Export Import Bank of India ; National Housing Bank(NHB).

The commercial banking network essentially catered to the needs of general banking and for meeting the short-term working capital requirements of industry and agriculture. Specialised development financial institutions (DFIs) such as the IDBI, NABARD, NHB and SIDBI, etc., with majority ownership of the Reserve Bank were set up to meet the long-term financing requirements of industry and agriculture. To

facilitate the growth of these institutions, a mechanism to provide concessional finance to these institutions was also put in place by the Reserve Bank.

The first development bank in India- IFCI- was incorporated immediately after Independence in 1948 under the Industrial Finance Corporation Act as a statutory corporation to pioneer institutional credit to medium and large-scale. Then after in regular intervals the government started new and different development financial institutions to attain the different objectives and helpful to five-year plans.

Government utilized these institutions for the achievements in planning and development of the nation as a whole. The all India financial institutions can be classified under four heads according to their economic importance that are:

- All-India Development Banks
- Specialized Financial Institutions(SIDBI)
- Investment Institutions (The Industrial Reconstruction Corporation of India Ltd., set up in 1971 for rehabilitation of sick industrial companies)
- State-level institutions(SFC)

S.H.Khan committee appointed by RBI(1997) recommended to transform the DFI (development finance institution) into universal banks that can provide a menu of financial services and leverage on their assets and talent.

Bank Nationalization

In 1969 and again in 1980, Government nationalized private commercial banking units for channelizing banking capital into rural sectors; checking misuse of banking capital for speculative purposes; to shift from `class banking' to `mass banking'(social banking); and to make banking into an integral part of the planning process of socio-economic development in the country. Today, no other developing country can boast of a banking system comparable to India's in terms of geographic coverage, operational capabilities, range of services and technological prowess.

Sector Priority lending

Commercial Banks

Today banks are broadly classified into two types - Scheduled Banks and Non-scheduled Banks

Scheduled banks are those banks which are included in the Second Schedule of the Reserve Bank Act, 1934. They satisfy two conditions under the Reserve Bank of India Act

- paid-up capital and reserves of an aggregate value of not less than Rs 5 lakh
- it must satisfy RBI that its affairs are not conducted in a manner detrimental to the depositors.

The scheduled banks enjoy certain privileges like approaching RBI for financial assistance, refinance etc and correspondingly, they have certain obligations like maintaining certain cash reserves as prescribed the RBI etc. The scheduled banks in India comprise of State Bank of India and its associates (8), the other nationalised banks (19), foreign banks, private sector banks,co-operative banks and regional rural banks. Today, there are about 300 scheduled banks in India having a total network of 79,000 branches among them.

Non-scheduled banks are those banks which are not included in the second schedule of the RBI Act as they do not comply with the above vriteria and so they do not enjoy the benefits either.

There are only 3 non-scheduled commercial banks operating in the country with a total of 9 branches.

In sum, all banks which are included in the Second Schedule to the Reserve Bank of India Act, 1934 are Scheduled Banks. These banks comprise Scheduled Commercial Banks and Scheduled Co-operative Banks.
Scheduled Commercial Banks in india are categorised into five different groups according to their ownership and / or nature of operation. These bank groups are (i) State Bank of India and its Associates, (ii) Nationalised Banks, (iii) Private Sector Banks, (iv)Foreign Banks, and (v) Regional Rural Banks. In the bank group-wise classification, IDBI Bank Ltd. has been included in Nationalised Banks.

Cooperative Banks

Co-operative Banks are organised and managed on the principle of co-operation, self-help, and mutual help. They function with the rule of "one member, one vote" and on "no profit, no loss" basis. Co-operative banks, as a principle, do not pursue the goal of profit maximisation.

Co-operative bank performs all the main banking functions of deposit mobilisation, supply of credit and provision of remittance facilities.

Co-operative Banks provide limited banking products and are functionally specialists in agriculture related products. However, co-operative banks are now provide housing loans also.

Urban Co-operative Banks (UCBs) are located in urban and semi-urban areas. These banks, till 1996, were allowed to lend money only for non-agricultural purposes. This distinction does not hold today. Earlier, they essentially lent to small borrowers and businesses. Today, their scope of operations has widened considerably. Urban CBs provide working capital, loans and term loan as well.

Co-operative banks are the first government sponsored, government-supported, and government-subsidised financial agency in India. They get financial and other help from the Reserve Bank of India, NABARD, central government and state governments. RBI provides financial resources in the form of contribution to the initial capital (through state government), working capital, refinance.

Co-operative Banks belong to the money market as well as to the capital market- they offer short term and long term loans.

Primary agricultural credit societies provide short term and medium term loans. State Cooperative Banks (SCBs) and CCBs (Central Cooperative Banks at the district level) provide both short term and term loans. Land Development Banks (LDBs) provide long-term loans.

Long term cooperative credit structure comprises of state cooperative agriculture and rural development bank (SCARDB) at the state level and primary PCARDBs or branches of SCARDB at the decentralised district or block level providing typically medium and long tem loans for making investments in agriculture, rural industries, and lately housing. The sources of their funds (resources) are ownership funds

- deposits or debenture issues.
- central and state government
- Reserve Bank of India
- NABARD
- other co-operative institutions

Some co-operative bank are scheduled banks, while others are non-scheduled banks. For instance, SCBs and some UCBs are scheduled banks (included in the Second Schedule of the Reserve Bank of India Act)

Co-operative Banks are subject to CRR and SLR requirements as other banks. However, their requirements are less than commercial banks.

Although the main aim of the co-operative bank is to provide cheaper credit to their members and not to maximize profits, they may access the money market to improve their income so as to remain viable.

Prakash Bakshi Committee

In August 2012, Reserve Bank of India constituted a committee to suggest ways to strengthen the rural co-operative credit structure.The panel, headed by Nabard Chairman Prakash Bakshi, will review the existing short-term co-operative credit structure (STCCS), focussing on structural constraints in the rural credit delivery system. It will also explore ways to strengthen the rural co-operative credit architecture. The seven-member panel will make an in-depth analysis of the STCCS, and examine various alternatives with a view to reducing the cost of credit.The STCCS targets the credit requirement of the small and marginal farmers in the country.It will mainly assess the role played by State and district cooperative banks in fulfilling the requirement of agriculture credit.

Commercial banks and their weaknesses by 1991

The major factors that contributed to deteriorating bank performance upto the end of eighties were

- high SLR and CRR locking up funds
- low interest rates charged on government bonds
- directed and concessional lending for populist reasons
- administered interest rates and
- lack of competition.

The reforms to set the above problems right were

- Floor and cap on SLR and CRR removed in 2006
- interest rates were deregulated to make banks respond dynamically to the market conditions. Even SB rates were deregulated in 2011
- near level playing field for public, private and foreign banks in entry

- adoption of prudential norms- Reserve Bank of India issued guidelines for income recognition, asset classification and provisioning to make banks safer
- Basel norms adopted for safe banking
- VRS for better work culture and productivity
- FDI upto 74% is permitted in private banks ← (Earlier 10% voting rights were given to FDI but now 24%)

One of the sectors that has been subjected to reforms as a part of the new economic policy since 1991 consistently is the banking sector. The **objectives of banking sector reforms** have been:

- to make them competitive and profitable
- to strengthen the sector to face global challenges
- sound and safe banking
- to help them technologically modernize for customer benefit
- make available global expertise and capital by relaxing FDI norms.

Narasimham Committee

Banking sector reforms in India were conducted on the basis of Narasimham Committee reports I and II (1991 and 1998 respectively). The recommendations of Narasimham committee 1991 are

No more nationalization

- create a level playing field between the public sector, private sector and foreign sector banks
- select few banks like SBI for global operations
- reduce Statutory Liquidity Ratio(SLR) as that will leave more resources with banks for lending
- reduce Cash Reserve Ratio(CRR) to increase lendable resources of banks
- rationalize and better target priority sector lending as a sizeable portion of it is wasted and also much of it turning into non-performing asset
- introduce prudential norms for better risk management and transparency in operations
- deregulate interest rates
- Set up Asset Reconstruction Company(ARC) that can take over some of the bad debts of the banks and financial institutions and collect them for a commission .

Targetted Priority sector - one who is not a priority should not avail the benefits

Most of these reforms are implemented except priority sector lending which is welfare-based and relates to agriculture. SLR is 23% today and CRR is 4.75%. Bank rate is aligned with MSF.(2012)

Divestment in public sector banks led to their listing on the stock exchanges and their performance has improved.

NPAs

Non-performing assets are those accounts of borrowers who have defaulted in payment of interest or installment of the principal or both for 90 days at least.

In 2003, NPAs stood at 9% and came down to 2.5% in 2008 but rose as economy slowed down since 2011.

Reflecting the stress in India Inc, net non-performing assets (NPAs) of banks at the aggregate level rose to Rs 60,100 crore at the end of March 2012.

One of the main reasons for this sharp jump in NPAs is the loans due to state electricity boards and also Air India. On the sectoral front, metals, textiles and infrastructure sectors were among the major ones to contribute to this slide.

The sharp rise in NPAs in the banking system, although was expected, has taken a toll on the stock prices of most of these banks.

PSU banks have seen their loans go bad at a faster rate than their private sector peers, the latter have been steadily improving their asset quality over the years.

RBI rules require that banks should set aside certain amount of money(provisioning) for the NPAs. Gross NPAs include the amount due along with the amount provisioned. Net NPAs include only the amount due.

NPAs are largely a fallout of banks' credit appraisal system, monitoring of end-usage of funds and recovery procedures. It also depends on the overall economic environment like the global recession since 2008, the business cycle and the legal environment for recovery of defaulted loans. Wilful default; priority sector problems among the poor etc are also responsible.

High levels of NPAs means: banks' profitability diminishes; precious capital is locked up; cost of borrowing will rise as lendable assets shrink; stock prices of banks will go down and investors will lose; investment suffers etc.

NPAs are classified as sub-standard; doubtful and loss making assets for provisioning requirements.

The following are the RBI guidelines for NPAs classification and provisioning:
Sub Standard Assets – These are those accounts which have been classified as NPAs for a period less than or equal to 18 months.

Doubtful Assets –These are those accounts which have remained as NPAs for a period of 12 months.

Loss Assets – Such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value. But a loss asset has not been written off, wholly or partly.

What is being done

- provisioning
- CAR norms
- norms
- one time settlement
- debt recovery tribunals
- securitization law
- foreclosure
- interest waiver
- writeoffs

Foreclosure means taking over by the lender of the mortgaged property if the borrower does not conform to the terms of mortgage.

Securitization is the process of pooling a group of assets, such as loans or mortgages, and selling securities backed by these assets.

SARFAESI Act 2002

To expedite recovery of loans and bring down the non-performing asset level of the Indian banking and financial sector, the government in 2002 made a new law that promises to make it much easier to recover bad loans from willful defaulters. Called the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002(SARFAESI) , the law has given unprecedented powers to banks, financial institutions and asset reconstruction/securitization companies to take over management control of a loan defaulter or even capture its assets.

Asset Reconstruction Company

Normally banks and FIs themselves recover the loans. But in the case of bad debts (sticky loans), it is outsourced to the ARCs who have built-in professional expertise in this task and who handle recovery as their core business. ARCs buy bad loans from banks and try to restructure them and collect them. Arcs were recommended by Narasimham committee II. ARCIL- the first asset reconstruction company was set up recently.

Prudential Norms

Prudential norms relate to

- income recognition
- asset classification
- provisioning for NPAs
- capital adequacy norms(capital to risk-weighted asset ratio, CRAR).

~~no~~ window dressing ↓ Paying defaulter to repay loans

A proper definition of income is essential in order to ensure that banks take into account income that is actually realized(received) . It helps in classifying an asset as NPA in certain cases. Once classified as NPA, funds must be set apart to balance the bank's operations so as to maintain safety of operations in case of non-recovery of NPAs.Thus, income recognition, asset classification and provisioning norms are inter-related.

No window dressing

Prudential norms make the operations transparent, accountable and safe.

Prudential norms serve two primary purposes: bring out the true position of a bank's loan portfolio and help in prevention of its deterioration.

Basel Norms

Banks lend to different types of borrowers and each carries its own risk. They lend the deposits of public as well as money raised from the market- equity and debt. The intermediation activity exposes the bank to a variety of risks. Cases of big banks collapsing due to their inability to sustain the risk exposures are readily available. Therefore, banks have to keep aside a certain percentage of capital as security against the risk of non-recovery. Basel committee provided the norms called Basel norms to tackle the risk.

If bank is lending to defaulter to pay his debt that will not be a realized income for banks.

Basel is a city in Switzerland. It is the headquarters of Bureau of International Settlement (BIS), which fosters co-operation among central banks with a common goal of financial stability and common standards of banking regulations. Every two months BIS hosts a meeting of the governor and senior officials of central banks of member countries. Currently there are 27 member nations in the committee. Basel guidelines refer to broad supervisory standards formulated by this group of central banks - called the Basel Committee on Banking Supervision (BCBS). The set of agreement by the BCBS, which mainly focuses on risks to banks and the financial system are called Basel accord. The purpose of the accord is to ensure that financial institutions have enough capital on account to meet obligations and absorb unexpected losses. India has accepted Basel accords for the banking system. In fact, on a few parameters the RBI has prescribed stringent norms as compared to the norms prescribed by BCBS.

In 1988, BCBS introduced capital measurement system called Basel capital accord, also called as Basel 1. It focused almost entirely on credit risk. It defined capital and structure of risk weights for banks. The minimum capital requirement was fixed at 8% of risk weighted assets (RWA). RWA means assets with different risk profiles. For example, an asset backed by collateral would carry lesser risks as compared to personal loans, which have no collateral. India adopted Basel 1 guidelines in 1999.

operational risk eg: Burglary, fire accident

In June '04, Basel II guidelines were published by BCBS, which were considered to be the refined and reformed versions of Basel I accord. The guidelines were based on three parameters, which the committee calls it as pillars. - Capital Adequacy Requirements: Banks should maintain a minimum capital adequacy requirement of 8% of risk assets - Supervisory Review: According to this, banks were needed to develop and use better risk management techniques in monitoring and managing all the three types of risks that a bank faces, viz. credit, market and operational risks - Market Discipline: This need increased disclosure requirements. Banks need to mandatorily disclose their CAR, risk exposure, etc to the central bank.

Basel III

In 2010, Basel III guidelines were released. These guidelines were introduced in response to the financial crisis of 2008. A need was felt to further strengthen the system as banks in the developed economies were under-capitalized, over-leveraged and had a greater reliance on short-term funding. Also the quantity and quality of capital under Basel II were deemed insufficient to contain any further risk.

→ More borrowing

deleverage - less borrowing

More

CRAR at 9 percent of the risk weighted assets is prescribed by Basel norms. It is the capital that is required to be set aside for absorbing risks. It is not to be provisioned from deposits raised but has to be additionally provided from debt, equity, reserves etc.

Presently the Basel II norms are being complied with by Indian banks as follows:

Basel 2 norms are 8% of CRAR.RBI made it 9% for greater security.

Basel-II aims to strengthen Basel I.

eg:- If 100 Rs are lent & it is expected (historically) that 90Rs are coming back. SO CRAR will be on Rs 10. i.e. 9% of 10

Not only credit risk but also market risk and operational risk are covered.

Credit risk
A bank always faces the risk that some of its borrowers may not repay loan, interest or both. This risk is called credit risk, which varies from borrower to borrower depending on their credit quality. Basel II requires banks to accurately measure credit risk to hold sufficient capital to cover it.

Market risk
As part of the statutory requirement, in the form of SLR (statutory liquidity ratio), banks are required to invest in liquid assets such as cash, gold, government and other approved securities. For instance, Indian banks are required to invest 24 per cent of their net demand and term liabilities in cash, gold, government securities and other eligible securities to comply with SLR requirements (2008-09).

Such investments are risky because of the change in their prices. This volatility in the value of a bank's investment portfolio in known as the market risk, as it is driven by the market.

Operational risk
Several events that are neither due to default by third party nor because of the vagaries of the market. These events are called operational risks and can be attributed to internal systems, processes, people and external factors.

Thus, Basel II uses a **"three pillars"** concept

Pillar 1 Specifies includes more types of risk- credit risk ,market risk and operational risk.

Pillar 2 Enlarges the role of banking supervisors.

Pillar 3 Defines the standards and requirements for higher disclosure by banks on capital adequacy, asset quality and other risk management processes.

Capital -Tier1 And Tier 2
Capital adequacy norms divide the capital into two categories. Tier one capital is used to absorb losses while the Tier 2 capital is meant to be used at the time of winding up.
Tier I Capital: Actual contributed equity plus retained earnings.
• Core capital

Tier II Capital: Preferred shares plus 50% of subordinated debt (junior debt)

Subordinated debt,figures between debt and equity – coming after the first in terms of eligibility for benefits like compensation.

Recapitalization is lending to the bank the resources needed to conform to the capital adequacy norms which stand at 8% today – minimum level.

One of the problems perceived in Basel 1 and 2 norms was that all sovereign debt, in general, was given a risk weight of zero, while all corporate debt was given similarly an equal weight irrespective of the difference in risk of the corporate concerned. The Eurozone sovereign debt crisis taught us lessons.

The risk weights led to some curious behaviour in lending. Banks started preferring to lend to governments, which required no capital addition, while even risk-free corporates, which had good rating, demanded additional capital provisioning under adequacy norms. Thus, one size fits all approach brought in distortions in lending.

Basel 3 norms: RBI Guidelines

The draft guideline norms announced by the RBI in mid-2012 will come into effect fully by 31 March 2018.

The key capital adequacy parameter has been stipulated at 9% higher than the international norm of 8%, and unchanged from what the regulator requires in India currently.

These guidelines mean that Indian banks would require a huge amount of capital in the next six years, about $30 billion to $40 billion. Some banks may find it difficult.

That would impose a heavy financial burden on the government, which will need to infuse capital in line with its holdings in the state-owned banks.

Countercycle
↓
cycle turns down

Under Basel III norms, a countercyclical capital buffer is prescribed: keep aside capital that can be used when the cycle turns down and the loans may turn bad.
Swap line for banks under the ECB route introduced by the RBI in mid-2013. (Discussed in the class)

BIS

The Bank for International Settlements (BIS) is an international organization of central banks which fosters international monetary and financial cooperation and serves as a bank for central banks." It also provides banking services, but only to central banks, or to international organizations. Based in Basel, Switzerland, the BIS was established by the Hague agreements of 1930.

As an organization of central banks, the BIS seeks to make monetary policy more predictable and transparent among its 55 member central banks. The BIS' main role is in setting capital adequacy requirements to safeguard bank's operations.

Shadow banks

NBFCs are largely refered to as shadow banking system or the shadow financial system. They have become the major financial intermediaries. As seen in the note on NBFCs elsewhere, shadow institutions do not accept demand deposits and therefore are not subject to the same regulations. Familiar examples of shadow institutions included Bear Stearns and Lehman Brothers. Hedge funds, pension funds, mutual funds and investment banks are some examples.

Shadow institutions are not as effectively regulated as banks and so carry higher risk of failure.

Universal Banking in India

Universal banking in India was recommended by the second Narasimham Committee (1998) and the Khan Committee (1998) reports. It aims at widening and integration of financial activities.

Universal Banking is a multi-purpose and multi-functional financial supermarket.' Universal banking' refers to those banks that offer a wide range of financial services, beyond the commercial banking functions like Mutual Funds, Merchant Banking, Factoring, Credit Cards, Retail loans, Housing Finance, Auto loans, Investment banking, Insurance etc. This is most common in European countries.

Benefits to banks from universal banking are that , since they have competence in the related areas, they can reduce average costs and thereby improve spreads(difference between cost of borrowing and the return on lending) by diversification. Many financial services are inter-linked activities, e.g. insurance, stock broking and lending. A bank can use its instruments in one activity to exploit the other, e.g., in the case of project lending to the same firm which has purchased insurance from the bank. To the customers, 'one-stop-shopping' saves transaction costs.

However, one drawback is that universal banking leads to a loss in specialisation. There is also the problem of the bank indulging in too many risky activities. ICICI(Industrial Credit and Investment Corporation of India) merged with its subsidiary-ICICI Bank in a reverse merger(parent merging with the subsidiary, the ICICI Bank). Other banks are also emerging as universal banks which are popular in Europe.

The compulsions for the DFIs like ICICI, IDBI, IFCI etc to become UBs is the following:
Earlier in the sixties and seventies, the DFIs specialized in project finance for the industries with long term capital needs. But the industries of late are mobilizing the finances from external sources or from the stock market and so the DFI business suffered. The cheap Government funds that were available in the earlier pre-liberalization era also are not available today.Banks and DFIs are having to compete for the same clients. Banks have an advantage in that they have a deposit base but the DFIs do not have same.

NBFCs

- Provide banking services (loans, credit..)
- Do not hold banking license
- Deposits ×
- Under banking regulations

- Administered price is govt determined price (001)
  - insulated economy (pre liberalization)

[800 import] → & returning loans.

From exports forex could be accumulated

- BOP crises 1991
  - India went to IMF for loans
    - Emergency financing facility ← cond'ns by IMF
    - Structure of economy was asked to be reformed
  - Devaluation (16min 001)
    Central bank is fixing rate when domestic currency's value lowers than other currency
  - Depreciation
    When exchange rate determined by market forces & value of currency deteriorate
  - Devaluation X Revaluation
- LERMS (D(002) (003)
  - Partial convertibility — 60 < 40 (market rate > govt rate)
  - Freedom to convertibility is market determined
- current account
  - trade: tourism
  - non trade: transfers, interest, dividends, profits

  From 1993 current account trade was made fully convertible
- Same time capital account was opened
  eg: Sony, LG came, FDI, FII
  ADR is also capital account convertibility
- 1999 ADR (10min)(003)
- Floating rupee (12min)
  - Rupee value decided by market forces
  - Symptom of developed economy
- Inelastic import (15min)
  - imports are ...

- Dirty float (005) ← a band is set beyond which value is changed. (5 – 60, 69)
  - when central bank intervenes
  - managed float / partial float
- Carry trade (1min)
- In order to reduce volatility when required RBI can intervene
  - so going by it rupee is floating (in context of rupee depreciation recently)
- Peg (006)
  - Fixed rate adopted by country engaged in international trade
  - To international hard currency (Buy dollar to cheapen ₹)
    - linking with hard international currency will bring stability
  - India cannot peg since India does not have $ to keep the value at pegged rate.
- Crawling Peg (9min)(006)
  (16min) Pegging ₹ at 8 it may get to 7 but slowly & eventually it will reach 8 ($ coming in country ₹ appreciates)
- Currency ~~vote~~ board (007)
  - money that is generated in India ~~can~~ is pegged with forex
  - Printing only when forex is there
  - To ~~control~~ protect purchasing power
  - Tight monetary discipline
  - India doesn't have currency board.

BANKING SYSTEM IN INDIA-II

Financial inclusion

Many people, particularly those living on low incomes, cannot access mainstream financial products such as bank accounts and low cost loans. This financial exclusion forces them to borrow from the moneylenders at high cost. Therefore, financial inclusion has been the goal of government's policy since late sixties.

Financial inclusion or taking banking services to the common man was the main driver of bank nationalization in 1969 and 1980 powered by three priority areas

- access to banking
- access to affordable credit, and
- access to free face-to-face money advice.

Thus, financial inclusion is the delivery of banking services at an affordable cost to the vast sections of disadvantaged and low-income groups. The Government of India's rationale for creating Regional Rural Banks (RRBs) in the years in 1975 following the nationalization of the country's banks was to ensure that banking services reached poor people.

The branches of commercial banks and the RRBs grew from 8,321 in 1969 to about 70,000.

Priority sector credit under which 40% of all bank advances should go to certain specified areas like agriculture is a form of directed credit that is aimed at financial inclusion.

Micro-finance (savings, insurance and lending in small quantities) and self-help groups are another innovation in financial inclusion.

Differential rate of interest; kisan credit cards; no-frills account (allowing opening of account with very little or no minimum balances) etc are examples of financial inclusion.

Scaling-up access to finance for India's rural poor, to meet their diverse financial needs (savings, credit, insurance, etc.) through flexible products at competitive prices is the goal of financial inclusion.

The total number of no-frill accounts opened over a two-year period (April 1, 2007 to May 30, 2009) stands at 25.1 million.

While it is beyond doubt that financial access of the people has significantly improved in the last three-and-a-half decades, and even more so in the last two years, the focus now should be on how to accelerate it as financial inclusion is important for economic growth, equity and poverty alleviation.

Unique identification number has some advantages for financial inclusion KYC (know your customer) bottlenecks will be dramatically reduced. Millions of new customers will become bankable. Growth will get a boost. Risk management will undergo a paradigm shift. Credit histories will be available on tap. Profitability will

improve and so will customer service. We could finally have a technology initiative to extend financial inclusion.

Bank consolidation

Merging public sector banks to form big and globally aspiring banks is bank consolidation. It is expected to bring about financial stability and was recommended by the Narasimham Committee-II (1997) on financial sector reform.

State Bank of Saurashtra's merger with SBI has been achieved and the remaining six are to be merged. Government says that bigger banks can take on competition; can raise more than smaller banks;

Rationalising the manpower and branch network after bank mergers is a challenge and the criticism also includes that the bigger banks will be so much more bureaucratized. Bigness also does not reduce chances of failure as seen in the west in the current meltdown.

India has more than 175 commercial banks, out of which 26 state-owned banks account for the majority of the banking sector's assets followed by private sector banks and foreign banks, which have a tiny share.

Financial stability

Financial stability is a situation where the financial system operates with no serious failures or undesirable impacts on development of the economy as a whole, while showing a high degree of resilience to shocks.

Financial stability may be disturbed both by processes inside the financial sector leading to the emergence of weak spots like excessive of leverage; dealing in doubtful products like collateralized debt options(CDS) etc. It can also be undermined through regulatory lapses and inadequate safeguards prescribed by law.

In India, the banking system was not impacted badly by the world financial crisis as Indian banks are well-regulated through proper supervision. They are also well capitalized through capital adequacy ratio according to the Bank of International Settlements (Basel, Switzerland).
Calibrated globalization also meant that we would open upon only on achieving the strength to compete successfully.

RBI and Financial Stability

Traditional role

Recent global financial crisis is largely attributed to the financial sector recklessness due to lack of quality regulation. The lesson to draw from the crisis is to provide for good regulation- need not be more regulation- by the Central bank so that there is financial stability. In India, RBI has performed the role by the following instruments

- Licensing of banks
- Deciding on who can set up a bank, expand etc
- SLR, CRR norms
- CAR rules
- Lender of last resort
- Laying down prudential norms

- Supervisory functions

RBI Governor heads the HLCC- High Level Coordination Committee of financial regulators of SEBI, PFRDA and IRDA.

RBI defines from time to time NPA norms; allows or limits or banks credit to certain sectors like real estate in order to make banking operations safe and stable. Interest rates are also changed through repo and reverse repo rates to caution the borrowers and consumers.

Post-Lehman

Maintaining and monitoring financial stability has always been a key objective of monetary policy. However, it was only from the middle of 2009(post-Lehman) that the government and the RBI sought to institutionalise the process, making financial stability "an integral driver of the policy framework."

RBI tracks the following parameters in its quest to maintain financial stability: excessive volatility in interest rates, exchange rates and asset prices; signs of excess leverage (borrowings) in the financial sector, companies and households; and the unregulated parts of the financial sector.

RBI set up a Financial Stability Unit in 2009 and started presenting periodical reports since March 2010. The first report found the banking system to be broadly healthy and well-capitalised, but noted that global economic shocks, inflation, the slow pace of fiscal consolidation and the unsettlingly large capital inflows posed significant risks to financial stability. According to the second FSR, many of the positive features are intact. Growth has rebounded strongly and the financial conditions are stable. Despite intermittent volatility in the foreign exchange and equity markets, the financial sector has been risk-free. New risk assessment measures are introduced by the RBI — such as the Financial Stress Indicator and the Banking Stability Index.

Risks to financial stability are: the widening current account deficit; volatile capital inflows and the persistently high inflation.

The asset quality of banks and their asset-liability mismatch need to be constantly monitored.

Recent developments in the microfinance institutional structure cause serious concern.

Given the increasing correlation between global economic growth and that in emerging markets, the possibility of certain exogenous risks materialising is strong.

Banking Stability Index

It has been devised by the RBI in 2009. This index is simple average of five sub indices chosen for banking stability map that RBI has constructed. Banking Stability Map has used five key risk dimensions like operational efficiency, asset-quality, liquidity and profitability. These are based on capital adequacy ratio, cost-to-income ratio, nonperforming loans to total loans ratio, liquid assets to total assets ratio and net profit to total assets ratio.

Words

PLR
Prime Lending Rate (PLR) is the rate at which banks lend to the best customers. About 15% today. (2009)

Basis point
Changes in interest rates and other variables are expressed in terms of basis points to magnify and express the importance of changes. One basis point is 1% of 1%.

Weak Bank – Narasimham Committe – II
A 'Weak Bank' has been defined by the committee as follows: Where total accumulated losses of the bank and net NPA amount exceed the net worth of the bank.

Narrow banking
Take deposits & put them in govt securities

For restoring weak banks to strength, restructuring is needed. Such restructuring is generally attempted by operating the bank(s) as narrow bank(s), among other things. Narrow banking would restrict banks to holding liquid and safe government bonds. It prevents bank run.

Bank run
A bank run is a type of financial crisis. It is a panic which occurs when a large number of customers of a bank fear it is insolvent and withdraw their deposits.

Subordinated debt
• Senior debt will be cleared first & then subordinate debt.
• Subordinate debt gives high rate of return than senior debt

It is also known as junior debt. It is a finance term to describe debt that is unsecured or has a lesser priority than that of other debt claim on the same asset. This means that if the party that issued the debt defaults on it, people holding subordinated debt get paid after the holders of the "senior debt". A subordinated debt therefore carries more risk than a normal debt. Subordinated debt has a higher expected rate of return than senior debt due to the increased inherent risk.

Core banking
Core Banking is normally defined as the business conducted by a banking institution with its retail and small business customers. Many banks treat the retail customers as their core banking customers, and have a separate line of business to manage small businesses. Larger businesses are managed via the Corporate Banking division of the institution. Core banking basically is depositing and lending of money.

World bank recapitalization
Government of India has made an assessment that the public sector banking system would need as much as Rs.35,000 crore worth of Tier-1 capital by 2012, given projections of how much their business needs to expand. Past divestment of equity has significantly reduced the government's shareholding in many public sector banks. Hence, it is argued, if 51 per cent government ownership has to be maintained to secure the public sector character of these banks, this recapitalisation has to be in the form of new government equity capital. Since the government is strapped for funds

eg: BANK A ← govt's share 51%
If govt want to raise money for recapitalisation it can float shares (sell shares) of BANK A. But by doing this the govt's share will reduced & so it will no more be a public bank.

for this purpose, it has decided to use this requirement as the basis for opting for a sector-specific $2 billion World Bank loan.

Banks stress tests

A **stress test** is an assessment or evaluation of a bank's balance sheet to determine if it is viable as a business or likely to go bankrupt when faced with certain recessionary and other stress situations- whether it has sufficient capital buffers to withstand the recession and financial crisis. European banks were recently subjected to such stress tests.

Financial sector reforms

Reforming the financial sector - banking, insurance, capital market, pensions- is crucial to make them generate resources; gain efficiencies; innovate new products and serve the economy and people well. It involves adoption of best practices in regulation and other areas like micro finance etc. The need is particularly felt in the wake of the global financial crisis brought about essentially by the financial sector that ruined the real economy related to production.

Some recent initiatives in this sector relate to introduction of private banks and foreign banks being given a level playing field with Government banks; deregulation of interest rates; reduction reserve requirements; pensions system being reformed ; base rate for banks; setting up of Financial Stability and Development Council; business correspondent model for financial inclusion.

There is a need however to improve the regulation of the NBFCs as they borrow from banks and lend which means if they are not properly regulated, the whole financial system is vulnerable.

Crr and slr have been freed from floor and cap to make banking more flexible.

Consolidation of banks is taking place so that benefits of scale can push Indian banks to global heights. State Bank of Saurashtra is merged with SBI and State Bank of Indore is also merged. Bank of Rajasthan has been acquired by ICICI Bank and merged with the latter.

However, in the insurance sector, reforms are still due. The Insurance Laws (Amendment) Bill provides for enhancement of share holdings by a foreign company from 26% to 49%. The Bill is not made into law as there ar differences among the political parties.

Pension Fund Regulatory and Development Authority (PFRDA) Bill that wants r FDI in this sector is also not approved.

The government was finding it difficult to manage its rising pension liability because of the defined-benefit system, under which the pension paid to employee was based on their last salary drawn.

In 2004, it shifted to a defined contribution system, which required employee to save for retirement from their earnings.

Towards this end, it set up a new pension system (NPS) for those joining government service after January 2004 and subsequently set up the Interim Pension Fund Regulatory and Development Authority to oversee the scheme that already managed the retirement savings of lakhs of state and central government employees.

The NPS was later extended to private individuals. The government now hopes to establish the NPS as the premier retirement savings scheme.

The pension bill seeks to give statutory or legal powers to the PFRDA, and set the framework for the regulation of pension fund schemes, including the ones being currently offered.

Debt market: The bond market in India remains limited in terms of nature of instruments, their maturity, investor participation and liquidity. Recent reforms include raising of the cap on investment by foreign institutional investors, or FIIs. Infrastructure debt fund etc.

Regulatory reforms- setting up of the FSDC is crucial for better supervision and clear demarcation of the jurisdiction.

The roadmap for financial sector reforms has been defined by the RH Patil, Percy Mistry & Raghuram Rajan reports.

The Banking Laws (Amendment) Act 2012

The Act would strengthen the regulatory powers of Reserve Bank of India (RBI) and to further develop the banking sector in India. It will also enable the nationalized banks to raise capital by issue of preference shares or rights issue or issue of bonus shares. It would pave the way for new bank licenses by RBI resulting in opening of new banks and branches. This would not only help in achieving the goal of financial inclusion by providing more banking facilities but would also provide extra employment opportunities to the people at large in the banking sector.

The salient features of the Bill are as follows:

- To enable banking companies to issue preference shares subject to regulatory guidelines by the RBI;
- To increase the cap on restrictions on voting rights; (From 10 → 24%)
- To create a Depositor Education and Awareness Fund by utilizing the inoperative deposit accounts;
- To provide prior approval of RBI for acquisition of 5% or more of shares or voting rights in a banking company by any person and empowering RBI to impose such conditions as it deems fit in this regard;
- To empower RBI to collect information and inspect associate enterprises of banking companies;
- To empower RBI to supersede the Board of Directors of banking company and appointment of administrator till alternate arrangements are made;
- To provide for primary cooperative societies to carry on the business of banking only after obtaining a license from RBI;
- To provide for special audit of cooperative banks at instance of RBI; and
- To enable the nationalized banks to raise capital through "bonus" and "rights" issue.

Bhartiya Mahila Bank (BMB)

It is an Indian financial services banking company based in New Delhi, India. Prime Minister Manmohan Singh inaugurated the bank on 19 November 2013 on the occasion of the 94th birth anniversary of former Indian Prime Minister Indira Gandhi.Although initially reported as a bank exclusively for women, the bank will allow deposits to flow from everyone, but lending will be predominantly for women. It has employees other than women too.

In India, only 26% of women have an account with a formal financial institution, compared with 46% of men. That means an account in either a bank, a co-operative, post office or a microfinance institution, according to a study by the World Bank. Also, for women, per capita credit is 80 per cent lower than males.

Furthermore, the results of a study using a global dataset covering 350 Microfinance Institutions (MFIs) in 70 countries indicates that more women clients is associated with lower portfolio-at-risk, lower write-offs, and lower credit-loss provisions.

The bank will place emphasis on funding for skills developments to help in economic activity. Moreover, the products will be designed in a manner to give a slight concession on loan rates to women.

The bank shall also aim to inspire people with entrepreneurial skills and, in conjunction with NGOs, plans to locally mobilize women to train them in vocations like toy-making or driving tractors or mobile repairs.

One of the other objectives of the bank is to promote asset ownership amongst women customers. Studies have shown that asset ownership amongst women reduces their risk of suffering from domestic violence.

The Bank's initial capital consists of Rs 1,000 crores. The government plans to have 25 branches by the end of March 2014 and 500 branches by 4th year of operation (2017).

Initially the bank will have a board of directors consisting of eight women.

How Indian banks survived the global crisis

Even though many banks failed and some survived on huge bailouts in the west due to the global financial crisis, Indian banking is almost unscathed for the following reasons

↳ W/o suffering any injury

- Public sector banks- 27- dominate
- FDI is 74% in private banks but voting rights are only 10%
- We adopted capital account convertibility in a measured manner
- RBI has been conservative and regulated the banks well. Banks were not allowed to invest in risky instruments like credit default swaps(CDS)
- Basel norms, SLR and CRR levels were well maintained
- Prudential norms also saved the Indian banks from recklessness.

Financial Inclusion

Access to finance by the poor and vulnerable groups is a prerequisite for poverty reduction and social cohesion. This has to become an integral part of our efforts to promote inclusive growth. Financial inclusion means delivery of financial services at an affordable cost to the vast sections of the disadvantaged and low-income groups. The various financial services include credit, savings, insurance and payments and remittance facilities. The objective of financial inclusion is to extend the scope of activities of the organized financial system to include within its ambit people with low incomes.

NSSO data reveal that 45.9 million farmer households in the country (51.4%), out of a total of 89.3 million households do not access credit, either from institutional or non-institutional sources. Further, despite the vast network of bank branches, only 27% of total farm households are indebted to formal sources (of which one-third also borrow from informal sources). The poorer the group, the greater is the exclusion.

Endow → Provide with a permanent income or property

While financial inclusion can be substantially enhanced by improving the supply side or the delivery systems, it is also important to note that many regions, segments of the population and sub-sectors of the economy have a limited or weak demand for financial services. In order to improve their level of inclusion, demand side efforts need to be undertaken including improving human and physical resource endowments, enhancing productivity, mitigating risk and strengthening market linkages.

JLBs are proposed by the Rangarajan committee on financial inclusion 2008.JLB is like the SHG but is confined to farming operations mainly. A Joint Liability Group (JLG) is an informal group comprising preferably of 4 to10 individuals coming together for the purposes of availing bank loan either singly or through the group mechanism against mutual guarantee. The JLG members are expected to engage in similar type of economic activities like crop production.

Micro Finance Institutions (MFIs) could play a significant role in facilitating inclusion, as they are uniquely positioned in reaching out to the rural poor. The committee feels that legislation to regulate the microfinance sector is essential.

Important additional data for financial inclusion

- The first major breakthrough in financial inclusion came through when MYRADA, an NGO working in Karnataka developed the self-help group (SHG) methodology to link the unbanked rural population to the formal financial system through the local bank branches. Thanks to the efforts of the Reserve Bank of India (RBI), Nabard, state governments and numerous civil society organisations , about 8.6 crore households now have access to banking through SHGs. There are 61 lakh saving-linked SHGs with Rs 5,545.6 crore aggregate savings and 42 lakh credit-linked SHGs with loan outstanding of Rs 22,679.8 crore as on March 31, 2009.
- The business correspondent (BC) model advocated by the RBI is another pertinent example of potential frugal innovation in the financial inclusion space. The use of BCs enables banks to extend banking services to the

Frugal - Sparing with money or food. Restraint - relevant

hinterland without setting up a brickand-mortar branch, which is often an unviable proposition. Banks use various types of hand-held devices, (aptly nicknamed microATMs) to authenticate micro-transactions at the BC location and to integrate the same with bank's main database.

- Unique Identification Authority of India (UIDAI

RBI as a regulator (Can be constructed from above)

Basics of Base Rate

What is the base rate (BR)?

It is the minimum rate of interest that a bank is allowed to charge from its customers. Unless mandated by the government, RBI rule stipulates that no bank can offer loans at a rate lower than BR to any of its customers.

How is the base rate calculated?

A host of factors, like the cost of deposits, administrative costs, a bank's profitability in the previous financial year and a few other parameters, with stipulated weights, are considered while calculating a lender's BR. The cost of deposits has the highest weight in calculating the new benchmark. Banks, however, have the leeway to take into account the cost of deposits of any tenure while calculating their BR. For example, SBI took costs of its 6-month deposits into account while calculating its BR, which it has fixed at 7.5%.

When did the base rate come into force?

It is effective from Thursday, July 1. However, all existing loans, including home loans and car loans, continue to be at the current rate. Only the new loans taken on or after July 1 and old loans being renewed after this date are be linked to BR.

How is it different from bank prime lending rate?

BR is a more objective reference number than the bank prime lending rate (BPLR) -- the current benchmark. BPLR is the rate at which a bank lends to lend to its most trustworthy, low-risk customer. However, often banks lend at rates below BPLR. For example, most home loan rates are at sub-BPLR levels. Some large corporates also get loans at rates substantially lower than BPLR. For all banks, BR will be much lower than their BPLR.

How often can a bank change its BR?

A bank can change its BR every quarter, and also during the quarter.

What does it mean for corporate borrowers?

Under the BPLR system, large corporates who enjoyed rates as low as 4-6% will be hit.

What are its benefits?

Makes the lending rates transparent. Monetary policy changes will find genuine transmission. Cross subsidation of the corporate at the expense of MSMEs will stop and MSMEs will get credit more affordably.

What are the exceptions?
Educational loans, export credit, credit to weaker sections can be given at sub-base rate.

Securities and Insurance Laws (Amendment) and Validation Act, 2010
United Linked Invest Plans(Ulips) are the insurance products in which payment is made partly for premium(insurance) and rest of it invested in the capital market like a Mutual Fund investment. It led to jurisdictional disputes between Sebi and Irda. Sebi says that a huge amount of Ulip is invested in stock market. Government promulgated an ordinance to set up a mechanism to regulate such jurisdictional disputes.

Financial sector is inter-related. Banks keep money that is invested in stock market. Insurance companies have stock market related products like Ulips.Pension funds are becoming popular in the stock market. These players can have mutual problems of jurisdiction as seen in the case of Ulips. Therefore, there is a need for a 'super regulator'.

Parliament passed a Bill- Securities and Insurance Laws (Amendment) and Validation Bill, 2010 -that provides a mechanism, headed by the finance minister, to resolve disputes between financial regulators as an ad-hoc arrangement. It has representations from the four financial sector regulators and the Finance Ministry- Sebi, Irda, Rbi and Pfrda.

The Act states that the Reserve Bank Governor will be the vice-chairman of the joint committee. The joint body can entertain only jurisdictional issues. Even here, forst the involved parties should settle it between them

However, there were apprehensions expressed by RBI over its autonomy.

The government is still working on a permanent body to settle the inter-regulator disputes such as the SEBI-IRDA turf war.
The criticism is that there is already a Hligh level Coordination Committee with Rbi Governor heading it and there is no need for the current mechanism. It has lead to politicization.

Swabhimaan 2011
The government has launched 'Swabhimaan' – a programme to ensure banking facilities in habitation with a population in excess of 2,000, by March 2012. The programme will use various models and technologies, including branchless banking through business correspondents. The government has decided to pay banks Rs 140 for every no frills account they open as part of the financial inclusion plan.

The initiative would enable small and marginal farmers obtain credit at lower rates from banks and other financial institutions. This would insulate them from exploitation of the money lenders

The government has actually decided to give Rs 500 million to banks fo helping them open no frills accounts in the fiscal year 2011-2012.

Once banking access increases, it is hoped that it enables government subsidies and social security benefits to be directly credited to the accounts of the beneficiaries, enabling them to draw the money from the business correspondents in their village itself.

Given the size of the un-banked population in the country, the ongoing project can be considered a "significant beginning". Only a little more than a third of India's population has access to banking services at present. Among the bank-supported initiatives, self-help groups (SHGs) also have a role to play, the government's FI project is reliant more on Banking Correspondent (BCs} and technology to reduce the capital-intensity of expanding the banking cover.

There should at the same time be focus on financial literacy so as to take full benefit for the inclusion. This is particularly true in a context of rapid development of branchless banking, with newly banked people being exposed to non-bank intermediaries, therefore with no possibility to directly interact with experienced bankers.

Financial inclusion should not only be about reaching high numbers of unbanked or underserved groups. It should equally be about the provision of quality financial services and products. This means that access to safe, adapted, accessible, affordable and usable financial services and products should be offered.

The Insurance Regulatory and Development Authority's (IRDA) latest Annual Report indicates life insurance penetration at just 4.6 per cent and general insurance penetration at 0.6 per cent. Majority of the people do not have bank accounts, and even though RBI mandates have ensured the opening of 50 million no-frills accounts, hardly 11 per cent are active.

Innovations in financial products and technology-based delivery methods can expand the reach of financial services and create new opportunities to provide essential services to the poor. Financial products targeting the poor, such as money transfer services, microloans, microinsurance, or weather and catastrophic risk insurance, micropensions, can all have an important transformative effect. Deepening the financial system and widening its reach is crucial for both accelerating growth and for equitable distribution, given the present stage of development of our country.

One of the key features of the National Rural Livelihoods Mission (NRLM) is to work towards achieving universal financial inclusion, beyond basic banking services to all the poor households, SHGs and their federations. The key lies in linking access to financial services with livelihood options and leveraging the same to achieve poverty eradication. The end purpose of financial inclusion is and must be poverty alleviation.

Priority sector: Nair Committee recommendations

The RBI committee under the current Union Bank Chairman MV Nair has come out with their recommendations on lending to priority sector. It has reviewed the existing guidelines on lending to priority sector categories including agriculture, MSME and export. Its recommendations are

- Priority sector targets for public sector and private sector banks could be retained at the current level of 40% of the net credit to the sector.
- It has recommended severe changes should be made to exposure of foreign banks. Foreign banks' priority sector target should be increased from 32% to 40%.
- Special treatment should be given to small and marginal farmers and housing loans below Rs 2 lakhs should be classified under priority sector.

RBI acted on these recommendations

The Reserve Bank of India (RBI) in July 2012 said that foreign banks having 20 or more branches in the country will be brought on par with domestic banks for priority sector targets in a phased manner over a maximum period of five years starting April 1, 2013.

Foreign banks with less than 20 branches will have no sub-targets within the overall priority sector lending target of 32 per cent. This is expected to allow them to lend as per their core competence to any priority sector category.

The RBI said that the revised guidelines aim at implementing the essence of recommendations of Nair Committee without dismantling the established and accepted structure of priority sector lending.

The overall target under priority sector lending is retained at 40 per cent as suggested by the Nair Committee. The targets under direct and indirect agriculture are retained at 13.5 per cent and 4.5 per cent, respectively while refocusing the direct agricultural lending to individuals, self help groups (SHGs) and joint liability groups (JLGs) directly by banks.

The RBI said that loans to micro and small service enterprises up to Rs.1 crore; all loans to micro and small manufacturing enterprises up to Rs.25 lakh and for housing in metropolitan centres above Rs.10 lakh and at other centres Rs.15 lakh would form part of priority sector lending as per the revised guidelines. Loans to food and agro processing units and individuals for educational purposes, including vocational courses up to Rs.10 lakh in India and Rs.20 lakh abroad would also be part of priority sector lending.

Loans for housing projects exclusively for economically weaker sections and low-income groups, provided the cost does not exceed Rs.5 lakh per dwelling unit, loans to distressed farmers indebted to non-institutional lenders, loans to state sponsored organisations for scheduled castes and scheduled tribes, loans to individuals for setting up of off-grid solar and other off-grid renewable energy solutions for households and loans to individuals other than farmers up to Rs.50,000 to prepay their debt to non- institutional lenders would also be part of priority sector lending.

Investments by banks in securitised assets, outright purchases of loans and assignments to be eligible for classification under priority sector provided the underlying assets qualify for priority sector treatment and the interest rate charged to the ultimate borrower by the originating entity does not exceed Base Rate of such bank plus 8 per cent per annum.

Savings bank rate deregulation

The Reserve Bank of India (RBI) in 2011 deregulated savings bank rates .
A savings deposit one where the depositor can earn interest like an FD and can withdraw from the account like a current account. The savings rate was fixed at 3.50% from 2003 to 2011 and waslater raised to 4%.

However, during the period, the RBI changed both repo and reverse repo rates many times but the same was not reflected in the interest rates that the normal household gets. There was a huge gap between savings and term deposit rates. Thus, the depositors in SB account suffered.

After deregulation, it is expected that savings rate would move in tandem with the RBI monetary policy, thus, making the policy more effective.

NBFC-MFI

RBI decided to create a separate category of NBFCs viz; Non Banking Financial Company-Micro Finance Institution (NBFC-MFI) and notified norms in 2012.

Foreign banks can set up their branch by -
· WOS
· Set up their branch directly

Foreign banks: WOS vs Branch

The global financial crisis of 2008 has shown that the growing complexity and interconnectedness of financial institutions have compromised the ability of home and host authorities to cope with the failure of too big to fail (TBTF) institutions. The lessons learnt during the crisis lean in favour of domestic incorporation of foreign banks as wholly owned subsidiaries (Wos)

In general, following are the main advantages of local incorporation:

- It creates separate legal entities, having their own capital base and local board of directors; (from their parent)
- It ensures that there is a clear delineation between the assets and liabilities of the domestic bank and those of its foreign parent and clearly provides for ring fenced capital and assets within the host country;
- It imparts clarity and certainty with respect to applicability of the laws of country of incorporation on the locally incorporated subsidiary;
- A locally incorporated bank has its own board of directors and these directors are required to act in the best interests of the bank, to prevent the bank from carrying on business in a manner likely to create a risk of serious □loss to the bank's creditors/depositors;
- Provides effective control to the regulator.

A number of jurisdictions, therefore, impose requirement of local incorporation for foreign banks mainly for (i) protecting local retail depositors and (ii) affording greater regulatory comfort.

Considering the capital required to fuel economic growth, foreign banks have to play a significant role along with new private sector banks to cater to growing credit demand.

In a bid to better regulate them and avoid 2008-type crisis, RBI in November 2013 said that foreign banks with complex structures which do not provide adequate disclosure would have to operate in India only through wholly-owned subsidiaries (WOS).

The guidelines incentivise foreign banks operating in the country with 'near national treatment' if they become WOS, enabling them to open branches anywhere at par with other public and private sector banks.

The regulator also allowed foreign banks to list their subsidiaries on the local stock exchanges.

They can also acquire local banks.

Proviso → A cond^n attached to an agreement

Corporate guidelines for the WOS include a proviso that not less than 50 per cent of the directors should be Indian nationals/NRIs/PIOs.
Further, not less than two-thirds of the directors should be non-executive directors and a minimum of one-third of the directors should be independent of the subsidiary.
There are 45 foreign banks in India with a network of 333 branches as of 2013, most of which are held by the top three -- StanChart (100 branches), HSBC (50) and Citi (40).

Their market share stood at 6.5 percent of total banking assets in FY13.

The initial minimum paid-up equity capital or networth for a WOS should be Rs 500 crore, RBI had said.

Differences between branch and Wos models: To set up a branch, it needsto get RBI approval. Tax rate is high (40% as against domestic companies rate which is 30%) Advantage: Repatriation of money back to foreign country is easier.
If it is a wholly owned subsidiary, it becomes an independent entity - less RBI intervention, less tax rate and the rest outlined above.
Both however are subject to priority sector norms as mentioned above.

CDR

There are occasions when corporates find themselves in financial difficulties because of factors beyond their control and also due to certain internal reasons. For example, the global financial crisis and the recession that followed since 2008 along with the infrastructural investments being stalled in India for a variety of reasons. For the revival of such corporates as well as for the safety of the money lent by the banks and financial institutions, timely support through restructuring of genuine cases is called for. In India, a Corporate Debt Restructuring System was evolved and detailed guidelines were issued by Reserve bank of India early 2001.

It may be emphasized here that, in no case, the requests of any corporate indulging in fraud or misfeasance, even in a single bank, can be considered for restructuring under CDR System.

In a growing sign of companies facing difficulties in meeting their financial obligations, banks were approached for debt restructuring in a record 126 cases during 2012 for a collective amount of Rs 84,000 crore.

Debt restructuring is a process that allows a private or public company – or a sovereign entity – facing cash flow problems and financial distress, to reduce and renegotiate its delinquent debts in order to improve or restore liquidity and rehabilitate so that it can continue its operations.

Replacement of old debt by new debt when not under financial distress is referred to as refinancing.

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NPAs 2013

Net non-performing assets (NPAs) or bad loans of 40 listed banks jumped by 38% or around Rs 35,424 crore in the first six months of financial year ended September 30, 2013.

As on March 31, 2013, net NPAs of 40 listed banks were Rs 93,109 crore, which rose to Rs 1,28,533 crore as on September 30, 2013.

Poverty and Inequality: Concepts, Data, Policy and Analysis

Poverty is deprivation of basic needs that determine the quality of life- food, clothing, shelter, safe drinking water etc. It also includes the deprivation of opportunities to health, education, skills, employment etc.

Many different factors have been cited to explain why poverty occurs. No single explanation has gained universal acceptance. The factors responsible for poverty include:

- Historical factors, for example imperialism and colonialism.
- Overpopulation.
- Growth is not fast enough to eradicate poverty
- Models of growth may be unsuitable for poverty alleviation. For example, capital-intense growth in a labour surplus country
- Poverty itself, preventing investment and development.
- Widespread reliance on traditional methods of agriculture. About 60% of the population depends on agriculture whereas the contribution of agriculture to the GDP is 20%.While services and industry have grown at double digit figures, agriculture growth rate has dropped from 4.8% to 2%
- Geographic factors, for example lack of fertile land and access to natural resources.
- Anti-poverty schemes not being effective due to institutional and other inadequacies
- War, including civil war, genocide
- Lack of education and skills.
- gender discrimination
- Matthew effect— the phenomenon, widely observed across advanced welfare states, that the middle classes tend to be the main beneficiaries of social benefits and services, even if these are primarily targeted at the poor. Matthew effect refers to those already having an asset base benefiting from it while those without it continue to be denied the same.

Eradication of poverty

The strategy of the Government includes the following elements

- The main plank of anti-poverty strategy is reducing poverty through the promotion of economic growth. In India, after reforms began in 1991 when growth rates increased , poverty levels fell quite steeply.(NSSO 2005)
- Socio economic planning
- Food security through the nation wide PDS- largest in the world
- Progressive taxation to garner fiscal resources for spending on poor
- Social safety net like the, National Social Assistance Programme (NSAP)
- Open society in which poverty is recognized as a national challenge and earnest efforts are made to tackle it(Amartya Sen)
- Anti-poverty programmes – NREGA 2005
- Massive social sector expenditure for skill building
- Decentralization through PRIs and Nagarapalikas for better delivery models

Poverty concepts

Types of Poverty

Human Poverty is the lack of essential human capabilities- literacy and nutrition.
Income Poverty: The lack of sufficient income to meet minimum consumption needs.
The World Bank defines extreme poverty as living on less than 1.25 US$ per day, and moderate poverty as less than $2 a day.

Poverty line

It is the level of income below which one cannot afford to purchase all the resources one requires to live. People who have an income below the poverty line have no disposable income.

When comparing poverty across countries, the purchasing power parity exchange rates are used. These are used because poverty levels otherwise would change with the normal exchange rates. Thus, 'living for under $1 a day' should be understood as having a daily total consumption of goods and services comparable to the amount of goods and services that can be bought in the U.S. for $1.

Poverty lines are defined as the per capita monetary requirements an individual needs, to afford the purchase of a basic bundle of goods- only food or food and other goods. The value of this basic basket of goods can be determined in many ways, for example: Absolute Poverty is a fixed measure in terms of a minimum calorific requirement plus essential non-food components, if any. It is used in India. Individuals are considered as poor if the per capita real income/consumption of the household to which they belong is below the benchmark poverty line. In India monetary requirement to consume 2100 calories in urban areas and 2400 calories in rural areas per day per person is the absolute poverty line.

Relative poverty lines set the line in relation to another variable: the average expenditure or income in a country, for example, the line is derived as 60 percent of the country's per capita income.
Headcount ratio

The most common standard indicator is the incidence of poverty (also called poverty rate or headcount rate). This describes the percentage of the population whose per capita incomes are below the poverty line, that is, the population that cannot afford to buy a basic basket of items. In many instances, a different poverty line--a much more austere one that generally only includes food items--is applied to derive the extreme poverty rate.

Poverty Gap (PG)

PG is a measure of the intensity of poverty among the poor: the difference between the mean income among the poor and the poverty line. This indicator measures the magnitude of poverty as well as its intensity- number of poor and how poor they are. The Poverty Gap Index is the combined measurement of incidence of poverty and depth of poverty. PG is also called the Foster-Greer-Thorbecke (FGT) index. It is the gap between the average poverty among the poor and the poverty line.

Misery index

The misery index was initiated by Chicago Economist Robert Barro in the 1970's. It is the unemployment rate added to the inflation rate. It is assumed that both a higher rate of unemployment and a worsening of inflation cause and intensify the misery. A combination of rising inflation and more people of out of work ("stagflation") implies a deterioration in economic performance and a rise in the misery index.

Agricultural wage earners, small and marginal farmers and casual workers engaged in non-agricultural activities, constitute the bulk of the rural poor. Small land holdings and their low productivity are the cause of poverty among households dependent on land-based activities for their livelihood. Poor educational base and lack of other vocational skills also perpetuate poverty. Due to the poor physical and social capital base, a large proportion of the people are forced to seek employment in vocations with extremely low levels of productivity and wages. The creation of employment opportunities for the unskilled workforce has been a major challenge for development planners and administrators.

Planning Commission and Poverty

The Planning Commission as the Nodal agency in the Government of India for estimation of poverty has been estimating the number and percentage of poor at national and state levels. Estimates of poverty are made from the large sample survey data on household consumer expenditure conducted by the National Sample Survey Organization (NSSO) of the Ministry of Statistics and Programme Implementation.

NSSO and Poverty Estimates

National Sample Survey Organisation (NSSO) collects household consumer expenditure data every five years on a large sample. Household consumer expenditure surveys are also conducted annually but the sample size is much smaller. Every five years full surveys on 1,20,000 households are carried out. In the intervening period, "thin" samples of around 20,000 households are surveyed. The "thin" samples do not indicate trends fully.

History and methodology of Poverty estimate in India

Planning commission initially gave poverty numbers and related data ratios since 1979 based on the Alagh Committee Report of that year. This procedure was subsequently modified by the Lakdawala Committee (1993).The commission in middle of last decade appointed an expert group led by Suresh Tendulkar to suggest a new poverty line for rural areas. It submitted its report in 2009. It used the latest data to construct a new poverty line basket. It moved away from the calorie intake as anchor for poverty estimation and included price indices for health and education. The all-India rural poverty line adopted by the Tendulkar Committee was 446.68 for 2004-05. Tendulkar committee did not deal with the urban poverty as the line was not controversial at that time.

New NSSO findings showed that poverty declined by 1.5 percentage points per annum between 2004-05 to 2009-10. It is the fastest decline of poverty compared to earlier periods. Both growth and public intervention have contributed. The poverty line in 2009-10 was 4,298 per month for a family in urban and 3,364 per month for a family in rural areas. There are questions on whether one can live with this money. 350 million lived below even this minimalist poverty line in 2009-10 in India. This is

a matter of concern and the need for increase in incomes for these people is obvious.(read ahead for 2013 data)

The purpose of these estimates at the macro level is to see progress over time (these are already delinked from entitlements). For example, one can examine whether poverty declined faster in the post-reform period as compared to pre-reform period or whether anti-poverty programmes have had an impact on poverty. Which regions/states and social groups benefited during the reform period?

The rate of reduction in Bihar, Chhattisgarh and Uttar Pradesh was low while poverty declined by 20 percentage points in Orissa. Some other findings are: Scheduled Tribes have high poverty ratio (47%) in rural areas while Muslims have the highest poverty (33.9%) in urban areas. Despite the MGNREGS and increase in agriculture wages, the poverty ratio among agricultural labourers was 50%. These are the concerns regarding poverty estimates and have immense policy implications.

The government has taken a decision to appoint a technical group to revise/revisit 'the methodology for estimating poverty in a manner that is consistent with current realities'. The government is also waiting for the socio-economic and caste census, 2011, based on Saxena and Hashim committees. It may be noted that the Planning Commission poverty estimates relate to income poverty estimates based on private consumer expenditure (PCE). The Saxena and Hashim Committee recommendations on deprivation may relate more to non-income indicators.(See ahead).

Exclusive calorie method for estimating poverty can be misleading . Some studies have shown that if we use direct method of calorie deprivation, two-thirds of the population would be poor. Equally, Orissa and Bihar would be richer states than Tamil Nadu and Kerala.

Arjun Sengupta Commission on unorganised enteprises estimated 77% of the population can be categorised poor and vulnerable.

Rangarajan committee has to review, from time to time, the methodologies for measuring poverty in keeping with changing needs of the population.

Rangarajan Committee

The government in mid-2012 announced the formation of a new expert committee under C Rangarajan, to revisit the methodology for estimation of poverty and identification of the poor, months after a poverty line cut-off, based on the method proposed by Suresh Tendulkar, had created a flutter. It will give the report I inn 2013-14 and has 4 members. The panel would also look into the issue of linking poverty estimates with providing benefits under the Centre's social welfare schemes. The panel would also assess whether poverty can be determined on any criteria other than the consumption basket. The panel will also assess if the two (consumption basket and other methods) can be effectively juxtaposed for estimating poverty in rural and urban areas.

The panel would examine the divergence between consumption estimates based on the National Sample Survey Organisation (NSSO)'s methodology and those emerging from the National Account aggregates. It would also suggest a method to update the

consumption poverty line, using the national, urban and rural consumer price index data being released since 2011.

The committee would study the various poverty estimation models used across the world and suggest the best alternative for India.

This committee has been appointed due to concern over estimating poverty using the Tendulkar committee's method. We need to look at how to define and measure poverty. So far, the level of consumption expenditure has been used as a way to estimate poverty. This is based on the basket of goods and services, and estimated using the least possible level to sustain someone. It is adjusted for price increases and consumption patterns every five years.

Tendulkar committee's approach is based on updating rural consumption data on prevailing prices, while not revising the urban consumption data simultaneously. Rangarajan committee has see if this is the right way to do it.

Poverty can be estimated in different ways. First, the absolute method, in which one considers how the economy has changed over time and the number of people living below a certain income level. The other is the relative method, in which you consider the current level of average income and the income distribution in the country. This has been widely used in India. So far, we have only looked at consumption expenditure. Now, we will also look at alternative ways—how to combine the current method with poverty estimation techniques used in other countries.

NC Saxena Committee

The rural development ministry in 2008 appointed a committee headed by NC Saxena to look at revising the parameters laid out by the earlier Sanjeeva Reddy committee to calculate the rural BPL figures in the states.

Officially, there are two sets of BPL estimates in India, one made by the Planning Commission using NSSO data on household consumption expenditure and the other by the rural development ministry through a state-level BPL house-to-house census . The mismatch between the two, with Planning Commission progressively lowering poverty estimates while the states push higher numbers, has been a source of controversy. The Centre allocates resources for BPL schemes based on the figures of the Planning Commission.

The committee chaired by NC Saxena recommended that 50% of India's population be given below-poverty-line cards. Thus, it suggests expansion of the social security net which means fiscal and administrative challenges.

While advocating exclusion of large number of families from the BPL lists, the committee has recommended that those families having double the land of the district average of the agricultural land or two wheeler or one running bore well or income tax payers would be deleted from the BPL lists.

While pointing out that the present poverty line which allows only 6.52 crore BPL cards is flawed, the committee has recommended a poverty line that would allow 50% of the country's population to get BPL cards as compared to the 28% at present. The

panel has recommended that some disadvantaged communities be given BPL cards automatically. These include chronically vulnerable groups, such as households with members having tuberculosis, leprosy, disability, mental illnesses or HIV/AIDS and others,designated 'primitive tribe', designated dalit groups, homeless household etc.

The Centre has notified 13 new parameters for defining Below Poverty Line (BPL) category of people in the country. It has done away with the earlier definition based on food calories or annual earnings.

The revised definition is based on landholding, type of dwelling, clothing, food security, hygiene, capacity for buying commodities, literacy, minimum wages earned by the household, means of livelihood, education of children, debt, migration and priority for assistance. The matter had been stayed by the Supreme Court and has only now been vacated.

Urban poverty

The Planning Commission had constituted an expert group under S.R. Hashim in 2010 to recommend detailed methodology for identification of BPL families in urban areas in the context of the 12th Five Year Plan.The expert group submitted an interim report recommending that poverty in urban areas be identified through identification of specific vulnerabilities in residential, occupational and social categories.

It said that those who are houseless, live in temporary houses where usage of dwelling space is susceptible to insecurity of tenure and is affected by lack of access to basic services should be considered residentially vulnerable.

Houses with people unemployed for a significant proportion of time or with irregular employment or whose work is subject to unsanitary or hazardous conditions or have no stability of payment for services should be regarded occupationally vulnerable.Households headed by women or minors or where the elderly are dependent on the head of household or where the level of literacy is low or members are disabled or chronically ill should be considered socially vulnerable, it said.

The expert group is yet to finalise the detailed methodology for an ordinal ranking of the poor on the basis of vulnerability.

BPL survey will be done by staff of municipalities or urban departments in 45 major cities.

In smaller towns, district magistrate will be the nodal officer.

Questionnaire prepared for urban BPL survey will obtain information on several parameters including income, number of members, type of house and availability of amenities.

The survey will also give us information about housing shortage and deficiency in services in urban areas.

It is for the first time that such a survey is being done. This is important in the context

of the proposed food security act and the Rajiv Awas Yojana (RAY) which aims to make cities free of slums besides better targeting of other schemes.An estimated 90 million of the 300 million living in India's roughly 45 cities and over 5,000 towns are poor.

JNNURM and RAY

The Jawaharlal Nehru National Urban Renewal Mission (JNNURM) was launched in 2005. Within JNNURM, we have urban infrastructure and governance (UIG), basic services to urban poor (BSUP), urban infrastructure and development scheme for small and medium towns (UIDSSMT) and integrated housing and slum development programme (IHSDP).

What's the difference between BSUP and IHSDP? BSUP suggests basic services that may extend to more than integrated housing and slum development. But it is also about housing and slum development. BSUP is restricted to 65 JNNURM mission cities and IHSDP is meant for non-mission cities and towns. That's the only difference.

Under both BSUP and IHSDP, there is provision for infrastructure (water, sanitation, sewerage, roads and street lights).

In 2009, Rajiv Awas Yojana (RAY) was announced, and launched in 2010 to provide housing to the urban poor. Under the ministry of housing and urban poverty alleviation, RAY aims to make the country free of slums by 2014.
States are required to prepare a plan of action based on geographic information system-enabled mapping for specific cities to be made slum-free.
Unlike previous schemes, RAY seeks to provide property rights to slum dwellers.
Tthe government is likely to use the public-private partnership (PPP) model to build infrastructure under the project.

The expenditure will be shared between the beneficiary and states and the central government.

The ministry has also decided to be more inclusive in defining slums and responded positively to the suggestion of an expert committee which said a contiguous area with 20-25 households having slum-like characteristics be considered as slums.

The States would be required to include all the mission cities of JNNURM, preferably cities with more than 3 lakh population as per 2001 Census; and other smaller cities, with due consideration to the pace of growth of the city, of slums, predominance of minority population, and areas where property rights are assigned.

Mortgage Risk Guarantee Fund

The government in 2011 proposed the creation of a Mortgage Risk Guarantee Fund under Rajiv Awas Yojana. This would guarantee housing loans taken by Economically Weaker Sections and Low Income Group households and enhance their credit worthiness.

Pronab Sen Committee

The Ministry of Housing and Urban Poverty Alleviation set up a committee to look into various aspects of Slum statistics /Census and issues regarding conduct of slum census 2011. The committee submitted its report to the Ministry of Housing and Urban Poverty Alleviation in 2010 . The salient finding / recommendations of the committee are: -

- The committee has estimated Slum population in the country in 2001 as 75.26 million and the projected slum population in the country for the year 2011 at 93.06 million.
- For the slum census 2011, the committee has recommended that for policy formulation purposes it is absolutely essential to count the slum population even in cities having less than 20,000 populations. For the purpose of planning for Rajiv Awas Yojana and slum free India it would be necessary to count the population of slums in all statutory towns in the country in 2011.
- The committee has suggested a different definition for slum than the definition adopted by the census of India 2001 and the states. The committee has recommended a normative definition of slum as: "A compact settlement of at least 20 households with a collection of poorly built tenements, mostly of temporary nature, crowed together usually with inadequate sanitary and drinking water facilities in unhygienic conditions."

The committee has suggested adoption of the following as slum-like characteristics for the purpose of identification of the slum areas: -

- Predominant roof material: any material other than concrete
- Availability of drinking water source: not with premises of the census house
- Drainage facility: no drainage or open drainage

The committee has recommended that a contiguous area with 20-25 house holds having slum like characteristics be counted as slum.

NSSO 69th round (ahead)
Poverty figures of 2013 (ahead)
Socio-economic caste census (ahead)

POVERTY AND INEQUALITY: II

Inequality

When discussing poverty, inequality often refers to the income gap between the rich and poor of society. The greater the gap, the greater the inequality. It essentially refers to disparities in the distribution of economic assets and income- among individuals and groups within a nation and among nations.

Disparate = very different in kind.

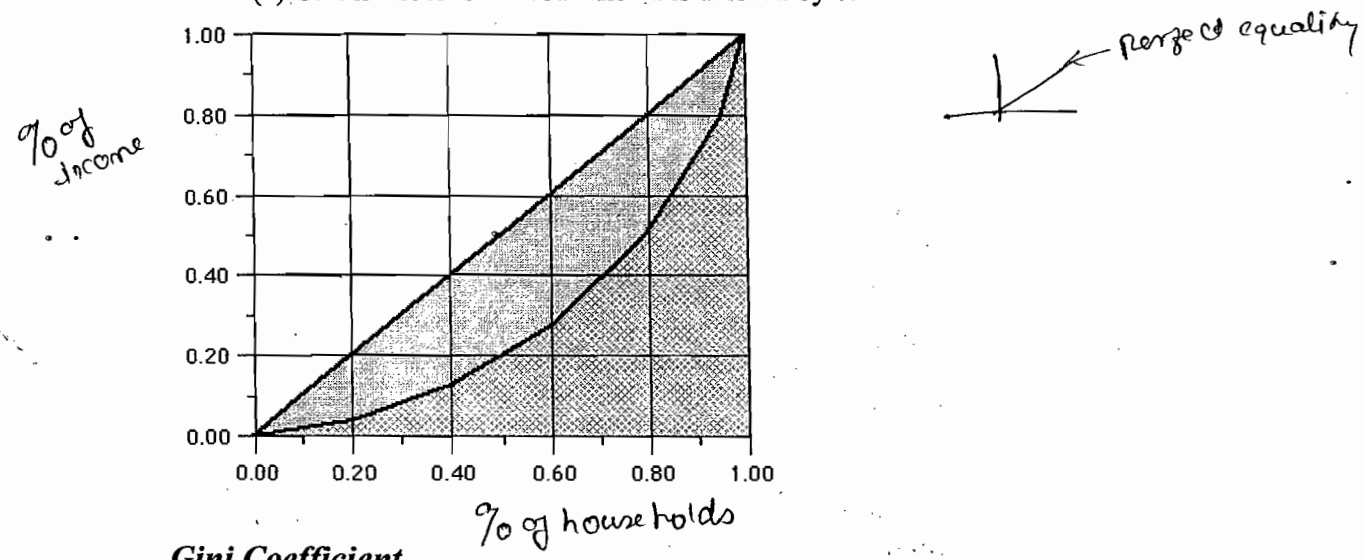
It may result from the operation of the economic system, access to assets, nature of laws, education and skills, social factors like caste and gender etc.

Lorenz Curve

The Lorenz curve was developed by Max O. Lorenz as a graphical representation of income inequality. It can also be used to measure inequality of income or assets or any other facility.

The Lorenz curve is used to calculate the Gini coefficient which is the numerical indicator of inequality in a country. Gini coefficient is derived by taking the following tow

- area between the line of perfect equality and the Lorenz curve(a)
- area between the line of perfect equality and the line of perfect inequality (b) Gini number is arrived when a is divided by b.



Gini Coefficient

To compute the Gini Coefficient, we first measure the area between the Lorenz Curve and the 45 degree equality line. This area is divided by the entire area below the 45 degree line (which is always exactly one half). The quotient is the Gini coefficient, a measure of inequality. The Gini index is the Gini coefficient expressed as a percentage, and is equal to the Gini coefficient multiplied by 100.

For a perfectly equal distribution, there would be no area between the 45 degree line and the Lorenz curve -- a Gini coefficient of zero. For complete inequality, in which only one person has any income (if that were possible) the Gini coefficient would be one. Real economies have some, but not complete inequality, so the Gini coefficients for real economic systems are between zero and one.

Gini coefficients : Sweden 0.250, Germany 0.283, India 0.325, France 0.327, Canada 0.331, Australia 0.352, UK 0.360, United States 0.408, China 0.447 and Russia 0.456.

Ahluwalia-Chenery Welfare Index

GDP may grow and the distribution of wealth may in fact worsen making the rich richer and the poor poorer. Thus, inclusive growth and not merely growth is required. An index that measures how all social groups are impacted by growth is necessary. This problem was recognized by Montek Singh Alhuwalia. Alhuwalia's solution, the Ahluwalia-Chenery Welfare Index, measures how each social group is impacted from the prosperity. It is an alternative measure of income growth, one that gave equal weight to growth of all sections of society.

Economic reforms, globalization and inequality

In India the LPG since 1991 contributed to prosperity but the rich have become richer faster than the poor improved. That is, even while poverty levels reduced impressively, inequality has grown too.

Liberalisation
Privatisation
Globalisation

When inequality is growing, economic growth will not achieve its potential in reducing poverty. Steep inequality damages the long-term prospects for economic growth. by creating conflict or instability, and it also limits growth by restricting the number of people who can participate in markets.

Prospect
↓
Possibility of something happening

To examine why growth is not reducing inequality: income growth is concentrated in certain urban centers, and those whose incomes increase are usually already above average in income and education. The reality is that those best positioned to gain from new economic opportunities are the educated urban-dwellers. On the other hand, the poor rely mainly on agriculture, and the agricultural sector has not been growing as fast as other sectors in most of Asia.

The current context of new technologies, market-oriented reforms and globalization has not favored the agricultural sector. Other causes of the agricultural sector's lackluster growth include: the decrease in transfers of new technology to farmers, and governments that invest little in agriculture and do little to encourage private investment in the sector.

Given that high levels of inequality are partly the result of government policy, government should address inequalities by introducing policies that ensure labour intensive growth; backward region development; social security; increased public investment in agriculture. Skills and training programs etc.

For millions of children, inequality means not having access to adequate nutrition, health, and basic education. Therefore, public policy has huge challenges in providing these services.

ICDS, SSA, NRHM, Mahatma Gandhi Backward Region Development Fund, Bharat Nirman etc are the initiatives in public policy by Government to bring down the divides.

In sum, main reasons for widening wealth gaps in recent years are:

- stagnation in agriculture while the economy is growing

Discrepancy
↓
A difference betn things Expected to be same

- discrepancy in investment between urban and rural areas which favoured better-educated, better-off urban populations.
- Improvements in rural infrastructure were being held back by government policies which deterred private investment.

Unevenness in growth in incomes across urban and rural areas, leading and lagging regions in the country, for example coastal and interior, and highly educated households and the less educated are important factors associated with increases in inequality.

Adverse impact of inequality

- Growing inequalities can dampen growth due to potential instability; weaken social cohesion.
- Urban-dominated growth in India has caused social friction as a result of the high levels of migration to cities and a shortage of foreign investment in more isolated areas.
- In societies where wealth is concentrated in the hands of a few, there is danger of policy levers being captured by the rich for their own benefit and a weakening of the institutional foundations of the growth process.

According to the ADB, absolute and relative inequality have widened. Although basic poverty levels have fallen as economy expanded, the living standards of the wealthiest in society have improved at a much faster rate compared to the poor.In a region as dynamic and vibrant as India, low growth in incomes of the poor is reflective of weakness in the pattern of growth. Incomes of the rich or top 20 percent have increased much more than those of the poor or the bottom 20 percent. That is, relative inequality is increasing.

Public Policy Challenge

ADB analyses the challenges to the government as follows:
Inequalities in life start early and they begin with extreme circumstances that deny millions the opportunity to have adequate nutrition, health and basic education. Governments must ensure their health and education programmes were "targeted" and implemented well. More spending is needed on education, training and healthcare to alleviate the situation .Government should implement complementary policies to counter negative impact of market-oriented reforms, such as social protection mechanism and skills and training programmes. There is a need to step up investment through PPPs to develop new economic activities and industries that generate employment opportunities that do not bypass the poor.

Public policy should also focus on radically improving the quality of basic health care and education.The key challenge to public policy here lies on not just increasing the quantum of public expenditures, but the outcomes are satisfactory- the target group is reached.

Summary

The growing wealth and wealth gap are a byproduct of globalization, which has brought higher incomes to urban, skilled, English-speaking workers in China, India and other countries, the bank's report said. The gap could slow the spread of prosperity, because the poorest people have less access to education, health care, bank

loans and other things needed to benefit from economic growth.We have to invest in creating opportunities, as well as investing in broadening access to opportunities. Relative inequality refers to proportionate differences in incomes, while absolute inequality refers to actual rupee differences in incomes.

Wealth distribution in India is uneven, with the top 10% of income groups earning 33% of the income. The 2007 report by the National Commission for Enterprises in the Unorganised Sector (NCEUS) found that 25% of Indians, or 236 million people, lived on less than 20 rupees per day.

Inequality in China and Nepal with Gini Coefficients of 47 are the highest in Asia, while India has a Coefficient of 36.

Social security

Certain social conditions need protection to prevent further distress- old age, poverty, unemployment, disability etc. Government provides social protection by way of wage employment, food grain either free or at affordable prices, old age pension etc. In some cases there is social insurance- disability etc.

In social insurance people receive benefits or services in recognition of contributions to an insurance scheme. These services include provision for retirement pensions, disability insurance, etc. Public distribution system in India is a social security example.

Social safety net is similar. It involves a collection of services provided by the state or other institutions including welfare, unemployment benefit, universal healthcare, homeless shelters etc to prevent individuals from falling into poverty beyond a certain level. For example, NREGA in India.

For many decades now, there have been laws in India that provided social security.

- **Workmen's compensation Act 1923 :** A beginning was made in social security with the passing of the Workmen's Compensation Act in 1923. The Act provides for payment of compensation to workmen and their dependents in case of injury and accident (including certain occupational disease) arising out of and in the course of employment and resulting in disablement or death.
- **Maternity benefit scheme:** The Maternity Benefit Act, 1961 regulates employment of women in certain establishments for a certain period before and after childbirth and provides for maternity and other benefits.
- **Gratuity scheme:** The Payment of Gratuity Act, 1972 provides for payment of gratuity at the rate of 15 days' wages for each completed year of service subject to certain maximum .
- **Employees state insurance scheme:** The Employees' State Insurance Act provides medical care in kind and cash benefits in the contingency of sickness, maternity and employment injury and pension for dependents in the event of the death of a worker because of employment injury.
- **Employees provident fund:** Retirement benefits in the form of provident fund, family pension and deposit-linked insurance are available to employees.
- Employees Pension scheme

- Aam Admi Bima Yojana
- Rashtriya Swasthya Bima Yojana
- Unorganised Workers Social Security Act 2008

MPI

Poverty is often defined by one-dimensional measures, such as income. But no one indicator alone can capture the multiple aspects that constitute poverty. Multidimensional poverty is made up of several factors that constitute poor people's experience of deprivation – such as poor health, lack of education, inadequate living standard, lack of income (as one of several factors considered), disempowerment, poor quality of work and threat from violence. A multidimensional measure can incorporate a range of indicators to capture the complexity of poverty and better inform policies to relieve it. Different indicators can be chosen appropriate to the society and situation.

Why multidimensional approach?

- **Income alone can miss a lot.** For example, economic growth has been strong in India in recent years. In contrast, the prevalence of child malnutrition has remained at nearly 50 per cent, which is among the highest rates worldwide. HUNGaMA report 2012. Multidimensional measures can complement income.
- **Poor people** describe ill-being to include poor health, nutrition, lack of adequate sanitation and clean water, social exclusion, low education, bad housing conditions, violence, shame, disempowerment and much more.
- **The more policy-relevant information available on poverty, the better-equipped policy makers will be to reduce it.** For example, an area in which most people are deprived in education is going to require a different poverty reduction strategy to an area where most people are deprived in housing conditions.

area specific

- **Some methods for multidimensional measurement, such as the OPHI-developed Alkire Foster method, can be used for additional purposes.** In addition to measuring poverty and wellbeing, OPHI's method can be adapted to target services and conditional cash transfers or to monitor the performance of programmes.
-

The **Multidimensional Poverty Index (MPI)** was developed in 2010 by Oxford Poverty & Human Development Initiative and the United Nations Development Programme and uses different factors to determine poverty beyond income-based lists. It replaced the previous Human Poverty Index.

The index uses the same three dimensions as the Human Development Index: health, education, and standard of living. These are measured using ten indicators.

Dimension	Indicators
Health	▪ Child Mortality ▪ Nutrition
Education	▪ Years of school ▪ Children enrolled
Living Standards	▪ Cooking fuel ▪ Toilet ▪ Water ▪ Electricity ▪ Floor ▪ Assets

Each dimension and each indicator within a dimension is equally weighted.
The MPI is an index of acute multidimensional poverty. It shows the number of people who are multidimensionally poor (suffering deprivations in 33% of weighted indicators) and the number of deprivations with which poor households typically contend.

GII

The **Gender Inequality Index (GII)** is a new index for measurement of gender disparity that was introduced in the 2010 Human Development Report 20th anniversary edition by the United Nations Development Programme (UNDP). According to the UNDP, this index is a composite measure which captures the loss of achievement, within a country, due to gender inequality, and uses three dimensions to do so: reproductive health, empowerment, and labor market participation. The new index was introduced as an experimental measure to remedy the shortcomings of the previous, and no longer used, indicators, the Gender Development Index (GDI) and the Gender Empowerment Measure (GEM), both of which were introduced in the 1995 Human Development Report.

There are three critical dimensions to the GII: reproductive health, empowerment, and labor market participation. The dimensions are captured in one single index.

Reproductive health

GII is a pioneering index, in that it is the first index to include reproductive health indicators as a measurement for gender inequality. The GII's dimension of reproductive health have two indicators: the Maternal Mortality Ratio (MMR),the data for which come from UNICEF's State of the World's Children, and the adolescent fertility rate (AFR), the data for which is obtained through the UN Department of Economic and Social Affairs, respectively. With a low MMR, it is implied that pregnant women have access to adequate health needs, therefore the MMR is a good measure of women's access to health care. The UNDP expresses that women's health during pregnancy and childbearing is a clear sign of women's status in society. A high AFR, which measures early childbearing, results in health risks for mothers and infants as well as a lack of higher education attainment. According to the

UNDP data, reproductive health accounts for the largest loss due to gender inequality, among all regions.

Empowerment

The empowerment dimension is measured by two indicators: the share of parliamentary seats held by each sex, which is obtained from the International Parliamentary Union, and higher education attainment levels, which is obtained through United Nations Educational, Scientific and Cultural Organization(UNESCO) and some other sources. The GII index of higher education evaluates women's attainment to secondary education and above. Access to higher education expands women's freedom by increasing their ability to question and increases their access to information which expands their public involvement. There is much literature that finds women's access to education may reduce the AFR and child mortality rates within a country. Although women's representation in parliament has been increasing women have been disadvantaged in representation of parliament with a global average of only 16%.

Labor market participation

The labor market dimension is measured by women's participation in the workforce. This dimension accounts for paid work, unpaid work, and actively looking for work. The data for this dimension is obtained through the International Labour Organization databases. Due to data limitations women's income and unpaid work are not represented in the labor market dimension of GII.

The metrics of the GII are similar in calculations to the Inequality-adjusted Human Development Index (IHDI), which was also introduced in the 2010 Human Development Report, and can be interpreted as a percentage loss of human development due to shortcomings in the included dimensions. The value of GII range between 0 to 1, with 0 being 0% inequality, indicating women fare equally in comparison to men and 1 being 100% inequality, indicating women fare poorly in comparison to men. There is a correlation between GII ranks and human development distribution, according to the UNDP countries that exhibit high gender inequality also show inequality in distribution of development, and vice versa. The GII a composite index used to rank the loss of development through gender inequality within a country. (Condensed in the class)

Poverty and recent achievements

The record in recent years of the anti-poverty strategies- the heart of inclusive growth- is encouraging. The percentage of the population below the official poverty line has been falling but even as that happens, the numbers below the poverty line remain large. According to the latest official estimates of poverty based on the Tendulkar Committee poverty line, as many as 29.8 per cent of the population, that is, 350 million people were below the poverty line in 2009–10. Questions have been raised about the appropriateness of the Tendulkar poverty line which corresponds to a family consumption level of `3,900 per month in rural areas and `4,800 per month in urban areas (in both cases for a family of five). There is no doubt that the Tendulkar Committee poverty line represents a very low level of consumption and the scale of poverty even on this basis is substantial. An Expert committee under Dr. C. Rangarajan has been set up to review all issues related to the poverty line keeping in

view international practices.(Read ahead for detailed examination of issues)

It is well established that the percentage of the population in poverty has been falling consistently but the rate of decline was too slow. The rate of decline in poverty in the period 2004–05 to 2009–10 was 1.5 percentage points per year, which is twice the rate of decline of 0.74 percentage points per year observed between 1993–94 and 2004–05. Normally, large sample surveys used for official estimates of poverty are conducted every five years, but because 2009–10 was a drought year, the National Sample Survey Office (NSSO) felt that it would tend to overstate poverty and it was therefore decided to advance the next large sample survey to 2011–12. The results of this survey – NSSO 68th Round details came out in 2013 June and are discussed ahead). NSSO 68th Round findings on poverty, consumption and inequality in consumption are: Poorest of poor in the country survive on barely Rs 17 per day in villages and Rs 23 a day in cities. According to the data, which relates to 2011-12 (July-June), five per cent population on the bottom rung had an average monthly per capita expenditure (MCPE) of Rs 521.44 in rural areas and Rs 700.50 in urban areas. On the other end of the spectrum, top five per cent of the population had an MPCE of Rs 4,481 in rural areas and Rs 10,282 in urban areas.

Rung → Horizontal Part of ladder

The National Sample Survey Office's (NSSO) 68th round of survey is based on samples consisting of 7,496 villages in rural India and 5,263 urban blocks except some remote areas, during July 2011-June 2012, the release said.On an average on the all-India basis, MPCE was around Rs 1,430 for rural India and about Rs 2,630 for urban India. Thus average urban MPCE was about 84 per cent higher than average rural MPCE for the country as a whole, though there were wide variations in this differential across states".

Inter-group Equality

Inclusiveness is not just about bringing those below an official fixed poverty line to a level above it. It is also about a growth process which is seen to be 'fair' by different socio-economic groups that constitute our society. The poor are certainly one target group, but inclusiveness must also embrace the concern of other groups such as the Scheduled Castes (SCs), Scheduled Tribes (STs), Other Back- ward Classes (OBCs), Minorities, the differently abled and other marginalised groups. Women can also be viewed as a disadvantaged group for this purpose. These distinct 'identity groups' are sometimes correlated with income slabs the SCs and STs, for example, are in the lower income category and all poverty alleviation strategies help them directly. Women on the other hand span the entire income spectrum, but there are gender-based issues of inclusiveness that are relevant all along the spectrum.

Inclusiveness from a group perspective goes beyond a poverty reduction perspective and includes consideration of the status of the group as a whole relative to the general population. For example, narrowing the gap between the SCs or STs and the general population must be part of any reasonable definition of inclusiveness, and this is quite distinct from the concern with poverty, or inequality, though the two are related.

Balance regional development (BRD) and Inclusive growth

Another aspect of inclusiveness relates to whether all States, and indeed all regions, are seen to benefit from the growth process. The regional dimension has grown in importance in recent years. On the positive side, as the PM mentioned in the 57th

NDC speech(See ahead), many of the erstwhile backward States have begun to show significant improvement in growth performance and the variation in growth rates across States has narrowed. However, both the better performing and other States are increasingly concerned about their backward regions, or districts, which may not share the general improvement in living standards experienced elsewhere. Many of these districts have unique characteristics including high concentration of tribal population in forested areas, or Minorities in urban areas. Some districts are also affected by left wing extremism, making the task of development much more difficult.

In the Twelfth Plan, govt aims pay special attention to the scope for accelerating growth in the States that are lagging behind. This will require strengthening of States' own capacities to plan, to implement and to bring greater synergies within their own administration and with the Central Government. As a first step, the Planning Commission is working with it's counterpart Planning Boards and Planning Departments in all State Governments to improve their capabilities. An important constraint on the growth of backward regions in the country is the poor state of infrastructure, especially road connectivity, schools and health facilities and the availability of electricity, all of which combine to hold back development. Improvement in infrastructure must therefore be an important component of any region- ally inclusive development strategy.

The efforts of the govt in this regard are

- FC criteria
- PC transfers
- special category states
- BRGF
- Green revolution in the eastern region
- North eastern region Vision 2020

Special focus on North east

Holding that infrastructure deficiency in North-East is a "major concern", Prime Minister Manmohan Singh in 2008 announced linking of all state capitals there by rail to ensure better connectivity and earmarking of Rs 31,000 crores to improve roads. Releasing 'Vision Document 2020 for the North-Eastern Region' he said besides developing rail and air connectivity, the government is also committed to improve road facilities in the Eleventh Plan. For improving air connectivity, he announced that a green-field airport will come up at Itanagar to connect the region with the rest of the country. He said all villages on the Arunachal Pradesh border will soon be electrified at a cost of Rs 550 crore. The Vision Document, approved by the North-East Council, also lays stress on promoting education in the region. Govt is to set up a NTFT and IIT at Shillong.

Green Revolution in Eastern India

The programme gets Rs 1,000 crore in his Budget for 2013-14.It was during Union Budget 2010-11 that for the first time, separate funds were allocated for the eastern parts of the country. The scheme, which comes under Rashtriya Krishi Vikas Yojana, includes Assam, Bihar, Jharkhand, eastern UP, Chhattisgarh, Odisha and West Bengal. Rice was a priority crop under the scheme. The other areas of focus were asset-building activities such as water management, construction of farm ponds and repair of irrigation channels. The main motive behind this project is to ensure food

security. The idea is to tap the eastern region for food grains and pulses. The Centre has also allocated Rs 500 crore for encouraging crop diversification to promote technological innovation. The original Green Revolution States face the problem of stagnating yields and over-exploitation of water resources. The answer lies in crop diversification.

BRGF

The Backward Regions Grant Fund Programme (BRGF), launched in 2007, signifies a new approach to addressing persistent regional imbalances in development. The programme subsumed the Rashtriya Sama Vikas Yojana (RSVY).The BRGF Programme covers 250 districts in 27 States, of which 232 districts fall under the purview of Parts IX and IX-A of the Constitution dealing with the Panchayats and the Municipalities, respectively. The remaining 18 districts are covered by other local government structures, such as Autonomous District and Regional Councils under the Sixth Schedule of the Constitution and state specific arrangements as in the case of Nagaland and the hill areas of Manipur.

so conc on regions of state.

Objectives

The Backward Regions Grant Fund is designed to redress regional imbalances in development by way of providing financial resources for supplementing and converging existing developmental inflows into the identified backward districts, so as to:

- Bridge critical gaps in local infrastructure and other development requirements that are not being adequately met through existing inflows,
- Strengthen, to this end, Panchayat and Municipality level governance with more appropriate capacity building, to facilitate participatory planning, decision making, implementation and monitoring, to reflect local felt needs,
- Provide professional support to local bodies for planning, implementation and monitoring their plans,
- Improve the performance and delivery of critical functions assigned to Panchayats, and counter possible efficiency and equity losses on account of inadequate local capacity.

The BRGF programme represents a major shift in approach from top-down plans to participative plans prepared from the grassroots level upwards. The guidelines of the Programme entrust the central role in planning and implementation of the programme to Panchayats in rural areas, municipalities in urban areas and District Planning Committees at the district level constituted in accordance with Article 243 ZD of the Constitution to consolidate the plans of the Panchayats and Municipalities into the draft district plan. Special provisions have been made in the guidelines for those districts in J&K, Assam, Manipur, Meghalaya, Mizoram, Nagaland and Tripura which do not have Panchayats, where village level bodies and institutions mandated under other frameworks such as the Sixth Schedule are to plan and implement the programme. The conviction that drives this new locally driven approach is that grassroots level democratic institutions know best the dimensions of poverty in their areas and are, therefore, best placed to undertake individually small, but overall, significant local interventions to sustainably tackle local poverty alleviation. There are three features of BRGF that make it truly unique among central initiatives to combat backwardness. First, the approach of putting the Panchayats and the Municipalities at the centre stage of planning and implementation. Second, no Central funding stream

is as 'untied' as the BRGF – the funds can be applied to any preference of the Panchayat/ Municipality, so long as it fills a development gap and the identification of the work is decided with people's participation. Third, no other programme spends as much funds, nearly 11 percent of the total allocation, for capacity building and staff provisioning.

Creation of capacity for effective planning at district and lower level is a key-pre-requisite to participative planning. Hence the BRGF contains a specific component for the capacity building of Panchayati Raj Institutions of Rs. 250 crore per year. A framework that looks upon capacity building in a very comprehensive fashion, encompassing training, handholding and providing ongoing support to Panchayat elected representatives has been developed for States to follow, while undertaking capacity building.

The planning process under BRGF is based on the guidelines for district planning issued by the Planning Commission. The process of integrated development commences with each district undertaking a diagnostic study of its backwardness and a baseline survey by enlisting professional planning support, to be followed by a well-conceived participatory district development perspective plan to address this backwardness during the period of the Eleventh Five Year Plan. Such plans would integrate multiple programmes that are in operation in the district concerned and, therefore, address backwardness through a combination of resources that flow to the district. District Plans received from the various States indicate that the untied fund allocated to the districts are generally being used for filling infrastructural gaps in drinking water, connectivity, health, education, social sectors, electrification, etc. The basket of works taken up includes construction of school buildings /class rooms, health sub-centres, drinking water facility, sanitation facilities, anganwadi buildings, Panchayat buildings, irrigation tanks/channels, street lights, link roads, culverts, soil and water conservation measures, etc. The BRGF has adopted the National Capability Building Framework (the NCBF) which envisages strengthening of institutional arrangements, including the infrastructure as well as software support for capacity building of elected representatives, the functionaries and other stakeholders of PRIs and thereby improving the vigour of grassroots level democracy.

The finance ministry in May 2013 set up an expert committee under the chairmanship of Chief Economic Adviser Raghuram Rajan to look into a composite development index of states for allocation of money under the Backward Region Grant Fund (BRGF). Rajan committee would consider criteria such as the state's positing in national per capita income and human development indicators to evolve a composite index. The panel would have five members but can invite experts as special invitees for deliberations. Finance Mnister Chidambaram in 2013-14 Budget speech said that the criteria for determining backwardness under BRGF are based on terrain, density of population and length of international borders. "It may be more relevant to use a measure like the distance of the state from the national average under criteria such as per capita income, literacy and other human development indicators."

PURA

Provision of Urban Amenities in Rural Areas (PURA) is a Central Sector scheme re-launched by Ministry of Rural Development (MoRD), Government of India during remaining period of the XI Plan with support from Department of Economic Affairs

and the technical assistance of Asian Development Bank. MoRD is implementing the PURA scheme under a Public Private Partnership (PPP) framework between Gram Panchayat(s) and private sector partners with active support of the state governments.

Amenity
A useful or desirable feature of a place

The scheme envisages development of rural infrastructure and is the first attempt at delivering a basket of infrastructure and amenities through PPP in the rural areas. The primary objectives of the scheme are the provision of livelihood opportunities and urban amenities in rural areas to bridge the rural – urban divide.

livelihood
A means of earning or obtaining necessities of life

Core funding shall be sourced from the Central Sector scheme of PURA and complemented by additional support through convergence of different Central Government schemes. The private sector shall also bring into the project its share of investment besides operational expertise. The scheme would be implemented and managed by the private sector on considerations of economic viability but designed in a manner whereby it is fully aligned with the overall objective of rural development.

Inclusiveness and Inequality

Inclusiveness also means greater attention to income inequality. The extent of inequality is measured by indices such as the Gini coefficient, which provide a measure of the inequality in the distribution on a whole, or by measures that focus on particular segments such as the ratio of consumption of the top 10 per cent or 20 per cent of the population to that of the bottom 10 per cent or 20 per cent of the population, or in terms of rural–urban, such as the ratio of mean consumption in urban versus rural areas. An aspect of inequality that has come sharply into focus in industrialised countries, in the wake of the financial crisis, is the problem of extreme concentration of income at the very top, that is, the top 1 per cent and this concern is also reflected in the public debate in India.

welfare state

Inequality must be kept within tolerable limits (Art.38, DPSP). Some increase in inequality in a developing country during a period of rapid growth and transformation may be unavoidable and it may even be tolerated if it is accompanied by sufficiently rapid improvement in the living standards of the poor. However, an increase in inequality with little or no improvement in the living standards of the poor is a recipe for social tensions. As a society, we therefore need to move as rapidly as possible to the ideal of giving every child in India a fair opportunity in life, which means assuring every child access to good health and quality education.

Inequality adjusted HDI

The HDI represents a national average of human development achievements in the three basic dimensions making up the HDI: health, education and income. Like all averages, it conceals disparities in human development across the population within the same country. Two countries with different distributions of achievements can have the same average HDI value. The IHDI takes into account not only the average achievements of a country on health, education and income, but also how those achievements are distributed among its citizens by "discounting" each dimension's average value according to its level of inequality.

The 2010 UNDP HDR focused on inequalities in human development attainments across countries. To quantify the potential loss because of such inequalities, the

Report introduced three new indices, viz., Inequality-adjusted Human Development Index (IHDI), Gender Inequality Index and Multi-dimensional Poverty Index.
According to the report, the IHDI is a "measure of the average level of human development of people in a society once inequality is taken into account. Under perfect equality, the HDI and IHDI are equal; the greater the difference between the two, the greater the inequality." In that sense, "the IHDI is the actual level of human development (taking into account inequality), while the HDI can be viewed as an index of the potential human development that could be achieved if there is no inequality."

The IHDI, estimated for 134 countries, captures the losses in human development due to inequality in health, education and income. Losses in the three dimensions vary across countries, ranging from 2.9% (Hong Kong) to 52.0% (Chad) in life expectancy, 1.3% (Czech Republic) to 49.7% (Yemen) in education and 4.5% (Azerbaijan) to 68.3% (Namibia) in income. Overall loss in all three dimensions ranges from 5.0% (Czech Republic) to 43.5% (Namibia).

India, HDI and IHDI: Human Development Report 2013

Over the past two decades, India has seen a big improvement in its human development index score, from 0.41 in 1990 to 0.554 in 2012, according to the latest report by the United Nations Development Program (2013). However, despite this improvement, India overtook only four of the countries positioned above it in 1990: Swaziland, Kenya, Cameroon and Congo. The rise in India's HDI score is partly thanks to it starting from a low base (countries with high HDI scores have limited room for improvement), and also a rapid increase in per capita gross national income.

Despite the improvement, India remains in the "medium development" category, 136th in a list of 186 countries that stretches from Norway at the top of the "very high human development" category to Niger at the bottom of the "low human development" group. In 2011, India was 134th in the list.
Since 2011, the UNDP report has included an inequality adjusted HDI, also known as IHDI, which aims to capture the effects of inequality on human development. If there is no inequality the IHDI equals the HDI, while a big difference between the readings means greater inequality. India's IHDI score was nearly 30% lower than its HDI reading.

The most glaring inequality in India is in education, the report says, even though it commends the introduction of the Right to Education Act.
Success stories, such as China, invariably show growth in investment in health and education, with a special focus on rural areas to "enable poor people to participate in growth," the UNDP report says.

India also fared poorly on life expectancy and gender equality.

NSSO 69th Round 2013

There were less numbers of slums in urban India in 2012 than three- years earlier. The number came down by 32.3 per cent to 33,150 in urban parts in 2012, compared with 49,000 in 2009, official data show. However, at least 12 per cent of the urban

population still lived in slums in 2012. The figures are based on the National Sample Survey Office (NSSO) report (69th) covering the period between July and December 2012. It was done in 3,832 urban blocks, spread over all states and Union Territories. At the all-India level, 881 slums were surveyed in urban blocks. The previous survey was based on the 65th round of NSSO, covering July 2008 to June 2009. A possible reason for the decline could be that at an all-India level, 24 per cent of slums had benefited from welfare schemes such as the Jawaharlal Nehru National Urban Renewal Mission, Rajiv Awas Yojana and others from state and local governments. Slums, according to the NSSO definition, are identified by the presence of certain undesirable living conditions — overcrowding, lack of hygiene and sanitation, inadequacy of drinking water and poor construction are some. "Any compact settlement with a collection of poorly built tenements, mostly of a temporary nature, crowded together, usually with inadequate sanitary and drinking water facilities in unhygienic conditions, provided at least 20 households lived there, was considered a slum for the survey," it said. About 41 per cent of these slums were notified and 59 per cent weren't. The former category refers to slums recognised by the municipalities or development authorities concerned. Those not notified were also covered in the survey. All-India, 44 per cent of slums — 48 per cent of the notified ones and 41 per cent of non-notified slums — were located on private land. Maharashtra, with an estimated 7,723 slums, accounted for 23 per cent of all slums in urban India, followed by Andhra Pradesh, with 13.5 per cent, and West Bengal with 12 per cent. The report says an estimated 8.8 million households lived in urban slums. Considering a household to be of five members, almost 44 million lived in slums in urban areas. This is 11.7 per cent of India's total urban population of 377 mn. The percentage could be actually more, since many households would have more persons.

Safe drinking water is not within the reach of half the rural households, according to a recent National Sample Survey Office (NSSO) study. According to the NSSO study, 54 per cent of rural households had no supply of drinking water at their homes in 2012. This was, however, a slight improvement compared to 2008-09 when 60 per cent did not have such amenities. The report was based on the 69th round of surveys, which covered a period of July-December, 2012 compared to the previous report based on the 65th round covering July 2008 to June 2009. As a result, large number of people in Chhattisgarh, Jharkhand, Madhya Pradesh, Rajasthan, Odisha and West Bengal had to walk at least half a kilometer to get drinking water.

Poverty levels down 2013

Poverty levels across India decreased by 15 percentage points — approximately 2 percentage year over year — between 2004-05 and 2011-12, as per the latest National Sample Survey Organisation (NSSO) figures. Many economists and government officials say the significant reductions in poverty levels can be correlated to high economic growth rates.

Between 2005 and 2010, the country's GDP grew at an average of 8.5 per cent and the poverty rate (the proportion of the population below the poverty line) registered an average annual decline of 1.48 per cent. The percentage of the country's population living below the poverty line declined from 37 per cent in 2004-05 to 22 per cent in 2011-12, according to NSSO data. The 11th Plan (2007-08 to 2011-12) had targeted reducing poverty by two percentage points by 2009-10, compared to 2004-05. Rural poverty has declined faster than urban poverty during this period.

India still counts nearly 26.89 crore poor among its citizens. According to the data, the total number of people below the poverty line in the country is 26.89 crore as against 40.73 crore in 2004-05. In rural areas, the number has reduced from 32.58 crore to 21.72 crore.

The data also indicate that the steepest decline in poverty was in India's poorer states. "While there has been a national reduction of poverty by two percentage points by 2009-10, compared to 2004-05, different states have performed differently. Bihar, Orissa, Rajasthan, Madhya Pradesh have witnessed a sharp decline. Bihar shows the biggest decline."

Bihar has experienced a substantive decline with the percentage of the population living below poverty line (BPL) coming down from 55 per cent in 2004-05 to some 35 per cent in 2011-12. The figures for Gujarat were 31 per cent in 2004-05 and 16 per cent in 2011-12. In Rajasthan, 0.6 crore were lifted out of poverty in the same period. Andhra Pradesh reveals a noteworthy decline in urban poverty from 23 per cent in 2004-05 to 6 per cent in 2011-12.

The Planning Commission has been estimating the number of people below the poverty line at both the state and national level based on consumer expenditure information collected as part of NSSO surveys since the Sixth Five Year Plan.

According to the Commission, in 2011-12 for rural areas, the national poverty line by using the Tendulkar methodology is estimated at Rs 816 per capita per month in villages and Rs 1,000 per capita per month in cities.

This would mean that the persons whose consumption of goods and services exceed Rs 33.33 in cities and Rs 27.20 per capita per day in villages are not poor.

PUBLIC SECTOR

Evolution, Reforms and Performance

Public sector units in India are wholly or partly owned and controlled by the government. In a public sector enterprise, the majority of equity shares is owned by the government directly or indirectly through governmental institutions and the government has decision making control .Public sector enterprise normally has forms of organisational structure like departmental undertakings(Railways etc);statutory corporations ;companies registered under the Companies Act 1956 mainly Departmental undertakings are not formed by or with the consent of the legislative authority. These are set up by the executive actions of government bodies and are charged with the duty of carrying out specially defined functions. These undertakings are not independent entities. They are subject to budgetary, audit and other controls of the government and are managed by civil servants. They are financed by annual budgets which also receives their revenues(CFI). A departmental undertaking is best suited where the main purpose of the enterprise is to collect revenue for the state and to provide public utilities and services at fair prices in larger public interest. Some examples of departmental undertakings are the Railway, Postal Department etc.

Statutory corporations are enterprises normally engaged in economic or manufacturing activities and are set up by act of legislature. These corporations are legal entities separate from the government and also the persons who conduct their affairs. ONGC , LIC are some examples. Shares of such corporations are in the name of the government and these are thus owned and controlled by the government. Statutory corporations enjoy extensive legal autonomy, and their rules, objectives, functions and duties are defined and specified in the act. Financing statutory corporations is not part of the Budget and therefore, they can retain their revenues, and also spend as per the rules laid down by the statute.

Control Boards are set up to manage government projects- for example, the river valley projects. Bhakra Management Board.

PSE can be in the form of cooperative society to support cooperative movement- Indian Farmers Fertilizer Cooperative Ltd(IFFCO) , Krishi Bharati Cooperative Ltd (KRIBHCO) etc. They are registered under Multi State Cooperative Societies Act. Over 65% of the capital of the units is held by the Central Government

Government Company is one where the government owns 51% or more of the paid up capital, according to Section 617 of the Companies Act 1956.

In India, we have all these types of PSEs.

Since the beginning of socio-economic planning after the Independence, public sector played a preeminent role in India. Commanding heights of the economy were to be in the hands of the public sector – basically infrastructure and basic industries like heavy engineering, power, metals etc. PSEs dominated the Industrial Policy Statement 1948 and IP Resolution 1956. They were opted for by the Government partly as the Government wanted to steer the economy towards planning goals rapidly and also because of pragmatic compulsions like the presence of the private sector in manufacturing was negligible and they were not willing to take up the unprofitable work of investing in infrastructure.

Govt is Promoter of PSUs.

The objectives of the PSUs are

- To build a self reliant economy
- To prevent/reduce concentration of private economic power
- Establish sound economic infrastructure
- Set up industries in the backward regions and thus help bring about balanced regional development
- Assist in ancillarization and thus spread the benefits of industrialization
- Create sufficient levels of employment and set standards in labour welfare
- Selling goods and services at reasonable prices so as to serve consumer , keep prices affordable and help non inflationary growth process .
- Invest in areas where the private sector would not invest like in roads , transport and so on .

Since planning began in 1951, the public sector has been the main engine of inclusive growth as can be seen below

- There are about 240 Central PSUs today (excluding insurance , finance and other companies) providing the country with infrastructure in steel , cement , transport , communication , power and so on .
- The record of the PSUs in supplying many goods and services like coal , ,transport ,power , irrigation and so on is commendable
- The PSUs are a model employer providing various facilities like education , housing and so on .
- Establishing industries in MP , Rajasthan , Bihar and so on , the efforts of the PSUs to reduce regional economic imbalances are not insignificant
- Non-inflationary growth process is facilitated because of the PSEs as prices of their goods and services can be administered.
-

While considering the performance of the PSUs it must be recognised that most of them had locational disadvantage ; sold the product at administered prices ; did not have access to the best of technology ; had excess of manpower ; operated in areas not meant for profit making like FCI ; were subject to multiple controls and excess of accountability and so on. Even while sick PSEs are reducing in number, the problems are compounded by : resource crunch, erosion of net-worth due to continuous losses incurred by the PSUs, reluctance of financial institutions to provide funds for revival of PSUs, heavy interest burden, old and obsolete plant and machinery, outdated technology, low capacity utilisation, excess manpower, weak marketing strategy, etc. Inadequate autonomy is one reason. Populism and the absence of rational pricing of goods and services is another reason for the low levels of efficiency in PSUs.

Public Sector and Economic reforms

Economic reforms were, made necessary to post higher growth rates for poverty alleviation on a war footing. Public sector was in need of competition to unlock its value. Therefore, domestic and foreign capital was invited to force the PSEs to compete and perform. Government recognized the need for PSE reform during the 7th FYP(1985-1990).

The New Industrial Policy 1991 made significant changes like dereserving many areas with only 3 areas being reserved today ; equity disinvestment ; managerial revamp with greater autonomy; refering a sick PSU to the Board of Industrial and Financial Reconstruction (BIFR) and so on.

Revamp → Alter something so as to improve it

(or areas)

List of industries reserved for the public sector

1. Atomic Energy
2. Minerals specified in the Schedule to the Atomic Energy (Control of Production and Use) Order, 1953
3. Railway passenger transport.

The period since 1991 when reforms were launched saw many reforms in the way PSEs should function

- Dereservation
- withdraw them from commercial and other areas like hotels, bakery, cycles etc
- disinvest a portion of the PSU equity for a variety of purposes
- strategic sale where a PSE is sold over to a strategic partner who buys majority equity and takes over management and may extend ownership further in course of time (eg: 3 5% Govt's share (of 100%) in NHPC given to Tata Power)
- Increasingly they are being subject to market discipline primarily by listing on the stock exchanges which is the direct outcome of divestment (Global rating ↑).
- Globalization - liberal FDI norms and import of capital goods , compel the PSUs to perform .
- The MOU system is being improved with greater weightage being given to the criterion of financial performance

MOU betn govt & PSU.

- Navaratnas (1997) are granted financial and managerial autonomy for global competitiveness (14 today, 2014).
- mini –ratnas were taken up for similar reforms (72 today, 2014)
- Maharatnas have been recognized since 2011(7 today, 2014)
- professionalization of boards

As mentioned above, the reforms have paid off and the performance is improved.

PSEs 2014

Public sector enterprises have been set up to serve the broad macro-economic objectives of higher economic growth, self-sufficiency in production of goods and services, long term equilibrium in balance of payments and low and stable prices. While there were only five Central Public Sector Enterprises (CPSEs) with a total investment of Rs. 29.00crore at the time of the First Five Year Plan, there are as many 248 CPSEs (excluding 7 Insurance Companies) with a total investment of Rs. 6,66,848 crore today(2012).

A large number of CPSEs have been set up as Greenfield projects consequent to the initiatives taken during the Five Year Plans. CPSEs such as National Textile Corporation, Coal India Ltd.(and its subsidiaries) have, however, been taken over from the private sector consequent to their 'nationalization'. Industrial companies such as Indian Petrochemicals Corporation Ltd., Modern Food Industries Ltd., Hindustan Zinc Ltd., Bharat Aluminium Company and Maruti Udyog Ltd., on the other hand, which were CPSEs earlier, ceased to be CPSEs after their 'privatization'.

Along with other public sector majors such as State Bank of India in the banking sector, Life Insurance Corporation in the insurance sector and Indian Railways in transportation, the CPSEs are leading companies of India with significant market-shares in sectors such as petroleum, (e.g. Coal India Ltd. and NMDC), power generation (e.g. NTPC and NHPC), power transmission (e.g. Power Grid Corporation of India Ltd.), heavy engineering (e.g. BHEL), aviation industry (eg. Hindustan Aeronautics Ltd. and Air India Ltd.) storage and public distribution system (eg. Food Corporation of India and Central Warehousing

Corporation), shipping and trading (eg. Shipping Corporation of India Ltd. and State Trading Corporation Ltd.) and telecommunication (eg. BSNL and MTNL).

With economic liberalization, post-1991, sectors that were exclusive preserve of the public sector enterprises were opened to the private sector. The CPSEs, therefore, are faced with competition from both domestic private sector companies (some of which have grown very fast) and the large multi-national corporation (MNCs).

Performance of CPSEs

The turnover of all 220 operating CPSEs stood at Rs. 14,73,319 crore as compared to Rs. 12,44,805 crore in the previous year. During the year 2010-11, the CPSEs earned foreign exchange equal to Rs. 97,004 crore as compared to Rs. 84,224crore in 2009-10. The foreign exchange outgo on imports and royalty, know-how, consultancy, interest and other expenditure, on the other hand, increased from Rs. 4,24,207crore in 2009-10 to Rs. 5,22,577 crore in 2010-11 showing an increase of 23.19%. The total employee strength in CPSEs was 14.44 lakh (excluding casual labours) in 2010-11 as compared to 14.90 lakh in 2009-10. The total strength of the employees in CPSEs has gone down by 45,981 persons due to superannuation, voluntary retirement etc. The salary and wages in all the CPSEs went up from Rs. 87,792 crore in 2009-10 to Rs. 96.210 crore in 2010-11, showing a growth of 9.58%.

Gross sales/turnover of CPSEs has been robust during 2010-11. The turnover of CPSEs (at the aggregate level) increased by 18.36 per cent in 2010-11 over 2009-10 against decline of 2.10 per cent in 2009-10 over 2008-09. There was, moreover, much variation from industry to industry. There was significant decline in turnover of CPSEs belonging to industries like medium & light engineering, transportation equipment and telecommunications services.

The profit of profit making CPSEs stood at Rs. 1,13,770 crore in 2010-11 compared to Rs. 1,08,434 crore in 2009-10. The loss of loss making CPSEs, on the other hand, was Rs. 21,693 crore in 2010-11 compared to Rs. 16,231 crore in 2009-10. At the aggregate level, the net profit of all CPSEs (aggregate net profit- aggregate net loss) stood at Rs. 92,077 crore in 2010-11 compared to Rs. 92,203 crore during 2009-10.
The best results were achieved by the 'mining' sector with 22.32 per cent growth in profit over the previous year. This was followed by 12.97 per cent growth in profits achieved by electricity sector. The 'services' sector suffered a loss of Rs. 7,639 crore during 2010-11, which was higher than the loss of Rs. 3,279 crore in 2009-10. This was mainly due to the loss suffered by Air India Ltd. in both these years. In the other industry groups, CPSEs belonging to transport services, telecommunication services and consumer goods were equally under stress, and their losses increased during 2010-11. Under the manufacturing sector, steel petroleum and textile showed a decline in profits. CPSEs belonging to medium and light engineering industries, suffered losses during the year in comparison to profit in the previous year. CPSEs in the chemicals & pharmaceuticals sectors, on the other hand, reduced their losses during 2010-11.

Oil & Natural Gas Corporation Ltd., NTPC Ltd., and Indian Oil Corporation Ltd have ranked first, second and third CPSEs respectively amongst the top ten profit making CPSEs. They are followed by NMDC Ltd., Bharat Heavy Electricals Ltd., Steel Authority of India Ltd., Coal India Ltd., GAIL(India) Ltd., Oil India Ltd. and Power Grid Corporation of India Ltd. All the top ten profit making companies are, more or less same in 2010-11 as in

ONGC 1st, NTPC 2nd
IOCL 3rd

2009-10 (with ranking slightly changed) except for Power Grid Corporation that has replaced the Power Finance Corporation.

Amongst the loss making companies, Air India Ltd., Bharat Sanchar Nigam Ltd. and Mahanagar Telephone Nigam Ltd. were the top three loss making enterprises during 2010-11. They are followed by Hindustan Photo Films Manufacturing Co. Ltd., Indian Drugs & Pharmaceuticals Ltd., Hindustan Cables Ltd., Fertilizer Corporation of India Ltd., Air India Charters Ltd., Hindustan Fertilizer Corporation Ltd. and ITI Ltd. The top ten loss making Companies covered nearly 92.55% of the total loss made by all the (62) CPSEs during the year. The top three CPSEs namely Air India Ltd., BSNL and MTNL alone have incurred a loss equal to 74% of the total loss of all CPSEs in 2010-11. Intense price war and cut-throat competition from new entrants, increase in salary & wages and increase in operating cost as well as increase in interest cost contributed to greater losses during the year. While the loss of Air India and MTNL have gone up by 24% and 54% respectively, the loss of BSNL increased by 145% in 2010-11 over 2009-10.

The share of 'gross value addition' in CPSEs (net value addition + depreciation) in Gross Domestic Product (at current market price) stood at 5.96 per cent in 2010-11 against a share of 6.44 per cent in 2009-10.

CPSEs contribute to the Central Exchequer by way of dividend payment, interest on government loans and payment of taxes and duties. There was, however, a significant increase in the total contribution of CPSEs to the central Exchequer during the year, which increased from Rs. 1,39,918 crore in 2009-10 to Rs. 1,56,124 crore in 2010-11. This was, furthermore, primarily due to increase in contribution towards 'customs duty' and 'excise duty' which increased from Rs. 6,896 crore and Rs. 52,627 crore in 2009-10 to Rs. 14,151crore and Rs. 62,713 crore respectively in 2010-11. There was a significant increase in contribution from corporate taxes as well, which went up from Rs. 38,134 crore in 2009-10 to Rs. 43,369 crore in 2010-11.

Disinvestment and Privatization

The New Industrial Policy 1991 , as mentioned above, talked of disinvestment and the Finance Minister's Budget Speech in 1999-2000 talked of privatization for the first time.

Definitions are important.

Disinvestment is the sale of shares of the Government to the retail public or employees or mutual funds or the FIIs. In other words, in disinvestment(divestment), there is no change in the management from public to private hands because either the government holds majority equity(51%) or even if the government holds less than 51% of equity, rest of it is sold to various individuals and institutions none of whom holds enough to take over management. It is essentially money-raising exercise with some accompanying benefits.

If the Government sells chunk of equity to a single buyer- 26% or 51% or more- to whom the management is also handed over, it is called strategic sale and the buyer is called strategic partner. It is a case of privatization. The buyer is one who has presence in the sector and can add value to the unit. For example, IPCL being sold to Reliance Industries Ltd(RIL) and Balco is sold to Sterlite.

Government may also sell off a unit to a strategic buyer- entire equity.

Strategic buyer is one who not only buys the chunk of entire equity- in one tranche or more- but also takes over management. That is the 'strategic' part of the sale. It is unlike disinvestment where sale of shares is unaccompanied by management control transfer. The strategic partner gives higher price for the shares as he gets management control along with it(management premium). Also, running of the unit improves.
Privatization and strategic sale are the same.

As mentioned above , disinvestment can be for less than 50% stake sale in which case the company remains a Government company.

The advantages with strategic sale (privatization) are that it gets investment; the strategic partner with management control will invest further for diversification and technological improvement; market perception will improve as it is no longer a government company; and shareholder value will increase. With the improvement of the functioning of the company , workers' protection will also be guaranteed.

Corporatization is a related term. It means: government units are reorganized along business lines. Typically they are required to pay taxes, raise capital from the market (with no government backing, explicit or implicit), and operate according to commercial principles. Government corporations focus on maximizing profits and achieving a favorable return on investment. They have to operate in a level playing field along with the private sector without any special advantages, more or less.

Advantages of Disinvestment/Privatization

- it raises finances for the government that can be spent on restructuring the PSEs
- makes additional finances available for the social sector priorities
- exposes the enterprises to market discipline, thereby forcing them to become more efficient and survive on their own financial and economic strength
- when units become more professionalized and profitable , budgetary support for them can be minimized freeing resources for social and infrastructural needs
- results in wider distribution of wealth through offering of shares to small investors and employees.
- beneficial effect on the capital market; the increase in floating stock would give the market more depth and liquidity and facilitate raising of funds by the PSEs for their projects or expansion, in future.
- Opening up the public sector to appropriate private investment would increase economic activity and benefits the economy, employment and tax revenues in the medium to long term.
- Reducing the public debt that is threatening to assume unmanageable proportions
- Releasing other tangible and intangible resources, such as, large government manpower currently locked up in managing the PSEs, and their time and energy, for redeployment in high priority social sectors that are short of such resources

In many areas, e.g., the telecom sector, the end of public sector monopoly brought relief to consumers by way of more choices, and cheaper and better quality of products and services. Competition made them perform better as outlined above.

Criticism of Divestment

While the advantages are convincing, the criticism is not to be dismissed wither.

- They constitute family silver and should not be liquidated

- PSEs check the private sector in the wider market place and so are crucial to economy. For example, if PSEs are not there, private enterprises may cartelise etc
- PSEs contribute by way of dividends and profits and thus are important sources of public finance
- The exercise is essentially meant to garner resources for filling the revenue deficit

A prudent middle path needs to be adopted by way of extent of divestment; unit chosen; pace of the process; method adopted – IPO, strategic sale etc; valuation debate etc.

By 2014, Rs.1.5 lakh crores were raised totally since 1992, approximately.

Divestment Policy

Elements of the policy since 2009 are

- List all unlisted public sector enterprises and sell a minimum of 10 percent of equity to the public, the survey stated.
- It also called for completing the process of offloading 5-10 percent equity in previously identified profit making non-Navratna companies.
- According to the survey, the targeted revenue generation from divestment should be Rs.25,000 crore annually.
- Auction all loss making PSUs that cannot be revived, it added
- Don't Privatise Profit making companies.

Valuation of shares

Fixing the price of shares for PSEs is done on the basis of the discounted cash flow (DCF) model. The DCF model is a method of valuing a business today based on the stream of its future profits or cash flows. It is said to be the best of the given methods.

Net asset valuation is not adopted as it applies only to the units that are being wound up and not for running businesses.

Details of the disinvestment proceeds till 2012are given at the end.

Government Policy on Disinvestment /Privatization

As a part of reforming the PSEs, Government's policy on disinvestment and privatization is evolving since the beginning of the reforms in 1991.

Its main elements are: -

- Divest to raise money and other advantages
- Profit-making PSUs will not be privatized
- List the unlisted companies
- Making shares available to a wider section of the public
- Restructure and revive potentially viable PSUs;
- Close down PSUs which cannot be revived;
- Fully protect the interests of workers.

Strategic & Non-strategic Classification

Government classified the Public Sector Enterprises into strategic and non-strategic areas for the purpose of disinvestment. It was decided that the Strategic Public Sector Enterprises would be those in the areas of:

- Arms and ammunitions and the allied items of defence equipment, defence aircrafts and warships;

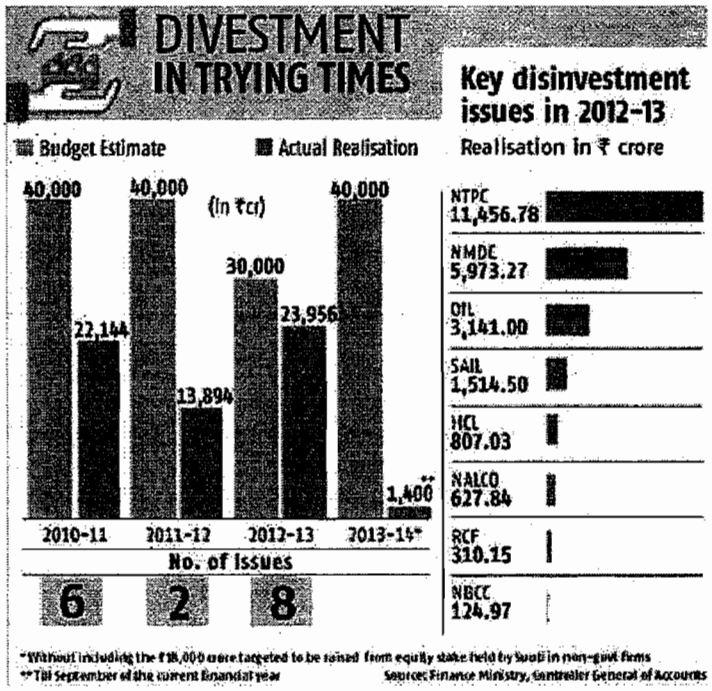
- Atomic energy (except in the areas related to the generation of nuclear power and applications of radiation and radio-isotopes to agriculture, medicine and non-strategic industries);
- Railway transport.
- All other Public Sector Enterprises were to be considered non-strategic.

Disinvestment 2013-14

Budget target of raising Rs 40,000 crore through disinvestment this year may be difficult .However, Indian Oil Corporation (IOC) and Coal India Ltd (CIL), Powergrid and others are being divested.

The government raised Rs 23,920 crore in 2012-13. All options — ETFs, offer for sale (OFS) etc — are available. Specified Undertaking of Unit Trust of India (Suuti), through which the government holds stakes in ITC, L&T and Axis Bank, was dismantled after a Cabinet decision in March 2013. It was decided that the Rs 40,000-crore assets would be transferred to an asset management company (AMC), which would leverage the assets to raise resources for the government.

Now, the government wants to revive Suuti so that it can sell stakes in these private companies because a Cabinet clearance is required each time shares held by the proposed AMC are to be sold.



Buyback and cross holdings

Cash rich companies buy back their own shares from the secondary market to help shareholders and share market. So far PSEs have not don buyback. But in 2012, GOI gave active consideration to the idea. Government in 2012 permitted public sector companies sitting on cash to buy back their own shares, a move that is expected to help the Centre raise more funds in the coming months. Public sector companies have the option of using their cash for investment and capex or buyback their own shares- in this case from the government, the promoter. The buyback route is useful for the government to meet its target for disinvestment.Under the buyback mode, the government can raise money by selling its equity in the company to the PSU itself.

To facilitate the disinvestment process, the Sebi Board in January 2012 had relaxed the norms for buyback of shares. It would help the companies to complete the process of selling shares within 1-1.5 months , as against the normal process which can take months.

Cross holdings

State-owned companies like Coal India, NTPC and NHPC, have significant cash on their balance sheets. It.can be used by them to buy shares of one another as the companies are

related and have synergies. Similarly, oil companies. When they buy shares of one another in bulk, the can guide each other and work with a common purpose. Government benefits as such purchase is done from the promoter.

ETF

GOI is also considering exchange traded fund (ETF) route for selling shares of state-owned firms as part of steps to meet the disinvestment target. Divested shares can make up an ETF that can be listed on the exchange and can be traded upon by those who have the shares related to the ETF.

Board for Reconstruction of Public Sector Enterprises (BRPSE)

Government is committed to a strong and effective public sector; undertake measures for strengthening, modernizing, reviving, and restructuring of public sector enterprises; and in pursuit of the above, decided to establish a Board for Reconstruction of Public Sector Enterprises (BRPSE) to address the above mentioned tasks and advise the Government on strategies, measures and schemes related to them.

The Board was set up in 2004

Following are the terms of reference to the Board:

- To advise the Government on ways and means for strengthening public sector enterprises in general and making them more autonomous and professional;
- To consider restructuring - financial, organizational and business (including diversification, joint ventures, seeking strategic partners, merger and acquisition) - of CPSEs and suggest ways and means for funding such schemes;
- To advise the Government on disinvestment/closure/sale, in full or part, in respect of chronically sick/loss making companies which cannot be revived. In respect of such unviable companies the Board would also advise the Government about sources of fund including sale of surplus
- assets of the enterprise for the payment of all legitimate dues and compensation to workers and other costs of closure;
- To monitor incipient sickness (incurring loss for two consecutive years) in CPSEs; and
- To make recommendations and advise the Government on such other matters as may be assigned to it from time to time.

All sick CPSEs will be referred to the Board for revival/ restructuring. The recommendations of the Board are advisory in nature. BRPSE which is an advisory body to advise the Government on the strategies, measures and schemes related to strengthening, modernizing, reviving and restructuring of public sector enterprises, comprises of a Chairman, three Non-official Members, three Official Members and three Permanent Invitees.Dr. Nitish Sengupta has been appointed as Chairman in the rank of Minister of State.

Navaratna and Miniratna Companies

Navaratnas

Economic reforms subject PSEs to market competition. Gloablization makes the competition more intense. To perform in such conditions, PSEs need a level playing field with the private players. Hence, the Navaratna package that gives autonomy to PSEs.

Government introduced the navaratna concept in 1997. It granted enhanced autonomy to nine selected PSEs referred to as "Navaratnas". These were IOC, IPCL, ONGC, BPCL,

HPCL, NTPC, SAIL, VSNL and BHEL. IPCL and VSNL were strategically sold to Reliance and Tatas respectively. Many more CPSEs were made navaratnas since then. Totally, there are 14 (2014)

1. Bharat Electronics Limited
2. Bharat Petroleum Corporation Limited
3. Hindustan Aeronautics Limited
4. Hindustan Petroleum Corporation Limited
5. Mahanagar Telephone Nigam Limited
6. National Aluminium Company Limited
7. National Mineral Development Corporation Limited
8. Neyveli Lignite Corporation Limited
9. Oil India Limited
10. Power Finance Corporation Limited
11. Power Grid Corporation of India Limited
12. Rashtriya Ispat Nigam Limited (Vizag Steel)
13. Rural Electrification Corporation Limited
14. Shipping Corporation of India Limited

The government is likely to accord the coveted status to Engineers India Limited, which is under consideration.

A new company Rashtriya lspat Nigam Limited (RINL) in Visakhapatnam was formed in 1982. Visakhapatnam Steel Plant was separated from SAIL and RINL was made the corporate entity of Visakhapatnam Steel Plant in April 1982.

The government has a quantitative system to confer the status of "Navarathna" on PSE. According to the system, every PSE is rated on the following 6 parameters:

- Net Profit to Net Worth
- Total Manpower Cost as a Percentage of Total cost of Production
- Profit before Depreciation ,Interest and Taxes (PBDIT) on Capital Employed
- PBDIT on turnover
- Earning per Share &
- Inter-sectoral performance

To gain Navarathna status, a PSE must score atleast 60 out of 100 based on these 6 parameters.

Additionally,a company must first be a miniratna and must have four independent directors on its board before it can be made a navaratna

These navaratnas , subject to certain guidelines, now have freedom to

- incur capital expenditure
- decide upon joint ventures
- set up subsidiaries/offices abroad
- enter into technological and strategic alliances
- raise funds from capital markets (international and domestic)
- enjoy substantial operational and managerial autonomy
- Boards of these PSEs have been broad-based with induction of nonofficial part-time professional directors.

For example, 'Navaratna' status empowers it to invest up to Rs. 1000 cr or 15% of their net worth on a single project without seeking government approval. The overall ceiling on such investment in all projects put together is 30% of the networth of the company.

Miniratna companies

There are two types of miniratna companies: Type 1 and 2.Together there are 72 such companies.

Miniratnas can also enter into joint ventures, set subsidiary companies and overseas offices but with certain conditions.

Category I Miniratna

- They are PSEs that have made profits continuously for the last three years and earned a net profit of Rs 30 crores or more in one of the three years. These miniratnas are granted certain autonomy like incurring capital expenditure without government approval up to Rs. 500 crores or equal to their net worth, whichever is lower. There are 48 miniratnas. Bridge & Roof Company (India) Limited was added late in 2010.

Category II Miniratna

This category include those PSEs which have made profits for the last three years continuously and should have a positive net worth. Category II miniratnas have autonomy to incurring the capital expenditure without government approval up to Rs. 300 crores or up to 50% of their net worth whichever is lower. There are 14 such miniratnas: Bharat Pumps & Compressors Limited was added late in 2010.

Maharatnas

The category of PSEs was created in 2011.

Maharatna CPSEs

1. Bharat Heavy Electricals Limited
2. Coal India Limited
3. GAIL (India) Limited
4. Indian Oil Corporation Limited
5. NTPC Limited
6. Oil & Natural Gas Corporation Limited
7. Steel Authority of India Limited

To be eligible for the grant of the Maharatna status, the company should have an average turnover of over Rs 25,000 crore, average annual net worth of more than Rs 15,000 crore and average annual net profit of over Rs 5,000 crore during the last three years.

Besides, it should be a Navratna firm, should be listed on the Indian Stock Exchange with minimum prescribed public shareholding under the SEBI regulations and have global presence.

Once a company gets the Maharatna status, its board would not be required to take the government's permission for investments up to Rs 5,000 crore in a joint venture project or wholly-owned subsidiary.For the Navratna companies, the limit is Rs 1,000 crore.

The main objective of the Maharatna scheme is to empower mega-Central public sector enterprises to expand their operations and emerge as global giants.

Ad-hoc Group of Experts (AGE) Report

The Report on Empowerment of Central Public Sector Enterprises, prepared by a group of experts headed by Arjun Sengupta, recommended

- greater autonomy for Public Sector Units
- central PSUs to have truly independent boards. It has recommended empowering the PSU boards to take decisions about mergers, joint ventures, pricing, exports, appointments, selection of dealers, promotion and transfer of employees, and so on. The ministry concerned should not review the PSU more than twice a year. Supervision should be done by sector specific supervisory boards.
- ministries should not interfere with the functioning of the PSUs under them. Their managements should be accountable to the board and not to the ministry
- government should be given flexibility to divest its stake in PSUs. As long as the government's stake remains above 51 per cent, it should not require Parliament's permission to divest its shares — even in navratnas, mininavatnas, and consistently profit-making PSUs. This can be done through a board decision..
- supplementary audit by the Comptroller and Auditor General of India of the PSEs should be an exception rather than rule, as it delays the publishing of audited accounts as required by SEBI.
- reworking of the accountability of the PSEs to Parliament so that the questions raised on their functioning do not compromise sensitive trade data and work as an impediment in functioning as commercial enterprises.

The Government accepted some of the recommendations of AGE relating to enhancement of financial powers of Navratna, Miniratna and other profit-making CPSEs. The remaining recommendations relating to ownership issues, audit of Government companies, Article 12 of the Constitution. Parliamentary accountability, vigilance, management in CPSEs, etc. are under examination.

MOU

The beginning of the policy of Memorandum of Understanding can be traced to the report of the Arjun Sengupta Committee in mid eighties. One of the recommendations of this committee was for the introduction of the system of MOU for measurement of performance of public enterprises. The MOU system was introduced on an experimental basis in 1987-88. It was based on the French system. From 1989-90 the signaling system was adopted and it remains in vogue till the present.

One of the most important differences between the French system and the signaling system relates to the possibility of making an overall judgement on the enterprise's performance in the latter system. In performance contracts belonging to the French system, it was possible to only point out whether a particular target was met or not. This created great difficulty for making an overall judgement regarding enterprise's performance. The signalling system overcomes this problem by adopting the system of "five point scale" and "criteria weight" which ultimately result in calculation of "composite score" or an index of the performance of the enterprise

The MOU system has been adopted as it was felt that PSEs are unable to perform at efficient levels because of multi-point accountability. Also, there was no clarity of objectives . Absence of functional autonomy also hampered their performance
MOU is a freely negotiated agreement between the public enterprise and the administrative ministry. Under the agreement, the enterprises undertake to achieve the targets set in the agreement at the beginning of the year. The MOU covers both financial performance as well as non-financial performance. Under this system performance of the company is categorized into five categories namely: excellent,very good, good, fair, and poor.

The objectives of the MOU system are to improve the performance of public enterprises by increasing autonomy and accountability of the management;remove the fuzziness in the goals and objectives the enterprise is to pursue through clearly laid down performance targets at the beginning of the year;enable the evaluation of managerial performance through objective criteria and provide a mechanism to reward good performance through performance incentives to stimulate improved performance.

Some recent initiatives in restructuring the PSEs

- BRPSE is set up as an advisory body
- National Investment Fund is set up
- more companies given navaratna and mini ratna status to improve their performance in the global competitive environment
- infusion of equity and debt capital in PSEs to turn them around and strengthen them

NIF

Original **Objectives of NIF are**

- The proceeds from disinvestment of CPSUs will be channelised into NIF, which is to be maintained outside the Consolidated Fund of India.
- NIF will be professionally managed to provide sustainable returns to the Government, without depleting the corpus. Selected Public Sector Mutual Funds will be entrusted with the management of the corpus of NIF.
- 75% of the annual income of NIF will be used to finance selected social sector schemes, which promote education, health and employment. The residual 25% of the annual income of the Fund will be used to meet the capital investment requirements of profitable and revivable CPSUs that yield adequate returns, in order to enlarge their capital base to finance expansion/diversification.

Use of Disinvestment Proceeds

The income from the Fund is to be used for the following broad investment objectives:

- 75% to finance selected social sector schemes, which promote education, health and employment
- 25% to meet the capital investment requirements of profitable and revivable CPSEs that yield adequate returns, in order to enlarge their capital base to finance expansion/diversification

However, in view of the difficult economic situation caused by the global slowdown of 2008-09 and a severe drought in 2009, GOI decided to give a one-time exemption to utilization of proceeds from disinvestment of CPSEs for a period of three years, till 2012 – i.e. disinvestment proceeds during this period would be available in full for meeting the capital expenditure requirements of selected social sector programmes decided by the Planning Commission/Department of Expenditure. It has been further extended to 2014.

Accordingly disinvestment proceeds are being routed through NIF to be used in full for funding capital expenditure under the following social sector programmes of the Government:-

- Mahatma Gandhi National Rural Employment Guarantee Scheme
- Indira Awas Yojana
- Rajiv Gandhi Gramin Vidyutikaran Yojana
- Jawaharlal Nehru National Urban Renewal Mission
- Accelerated Irrigation Benefits Programme
- Accelerated Power Development Reform Programme

NIF Chief Executive Officer (CEO), who is administratively attached to the Department of Disinvestment under the Finance Ministry, would formulate the investment strategy.

The Government in 2013 approved restructuring of the National Investment Fund (NIF) and decided that the disinvestment proceeds with effect from the fiscal year 2013-14 will be credited to the existing 'Public Account' under the head NIF and they would remain there until withdrawn/invested for the approved purpose. It was decided that the NIF would be utilized for the following purposes: investment in railways; uranium corporation , Equity infusion in various Metro projects etc.

Autonomy for PSEs

Managerial and financial autonomy is important for the PSEs to function well in a market economy where there is severe competition and the companies are also listed on the stock exchanges. Steps for rendering autonomy to the PSEs are essentially two

- Maharatnas
- Navaratna and miniratna status
- MOU

(Given above in detail)

Professionalisation of PSU Boards

- MOU
- outside professionals should be inducted in the boards of PSU in the form of non-official Directors whose number should be at least 1/3 of the Actual strength of the Board
- Under the Navratna/Miniratna package, the board of select PSUs have been professionalised by inducting a minimum of 4 non-official Directors in case of Navratnas and 3 in case of Miniratnas.
- number of Government Directors on the Board should not be more than two

Problems and Prospects of PSU restructuring

Tenure of the CEO and Board of Directors

The managerial problems in the PSU begin with the tenure of CEO and the Board of Directors. The selection, service conditions and the tenure of the Board of Directors is subject to the Government rules and regulations. Unlike the private sector where CEO have almost a decade to nurture the company, in PSU the rules with respect to superannuation tends to focus attention on short term strategies-co-terminus with CEO's tenure. There is, hence a need to provide continuity in the management by appointing CEO and other

Superannuation → Regular payment made by employee towards a pension

members in the Board of Directors for longer tenure with representation of shareholders other than GoI Shareholders.

Multiple-Audit

The business decision in PSUs gets influenced by presence of a number of controlling agencies, such as the Ministry, parliamentary committees, CAG, CVC etc. The end result of this is recourse to a risk- averse approach to business. For example, there is a decision related purchase of second hand equipment where on the spot decision is required and transparent processes such as global bid are not available. It helps the company to save if it can take quick decisions. In some cases there could be loss which needs to be out of the purview of CVC as otherwise it will dampen the decision making process in commercial matters.

Role of administrative Ministry

It needs to change. Like a shareholder of any other company, the Ministry's role should be limited to contributing as shareholder in AGM/EGM of the companies, and providing it the requisite support. The role of Ministry in day-to-day management through correspondence should be avoided.

Non Commercial Activities

PSUs are expected to function on commercial consideration but are burdened with takeover of some sick/potentially sick unit.

Investment in newer units is based on socio-political consideration. This results in non-flexibility of to the company to reorganise its own business. Regularisation of contract labour under article 12 of the Constitution forces PSUs to absorb extra labour without any consideration to the existing manpower strength. PSUs are unable to spin-of loss making units or close operations in those units, which have become operationally unviable.

Purchase Preference Policy

Government gives purchase preference in supply of goods and services to the Government Departments, Autonomous bodies and other PSEs if the price quoted by the supplying CPSE is within 10% of the lowest valid bid price, other things being equal. It helps support the PSEs.

CPSEs listed on the BSE/NSE(2014)

1. OIL & NATURAL GAS CORP.LTD.
2. COAL INDIA LTD.
3. NTPC LTD.
4. MMTC LTD.
5. BHARAT HEAVY ELECTRICALS LTD.
6. NMDC LTD.
7. INDIAN OIL CORP.LTD.
8. STEEL AUTHORITY OF INDIA LTD.
9. GAIL (INDIA) LTD.
10. POWER GRID CORP.OF INDIA LTD.
11. POWER FINANCE CORP.LTD.
12. NHPC LTD.
13. OIL INDIA LTD.
14. HINDUSTAN COPPER LTD.
15. RURAL ELECTRIFICATION CORP.LTD.

16.NATIONAL ALUMINIUM CO.LTD.
17.BHARAT PETROLEUM CORP.LTD.
18.NEYVELI LIGNITE CORP.LTD.
19.CONTAINER CORP.OF INDIA LTD.
20.BHARAT ELECTRONICS LTD.
21.HINDUSTAN PETROLEUM CORP.LTD.
22.MANGALORE REFINERY & PETROCHEMICALS LTD.
23.ENGINEERS INDIA LTD.
24.SJVN LTD.
25.MOIL LTD.
26.RASHTRIYA CHEMICALS & FERTILIZERS LTD.
27.NATIONAL FERTILIZERS LTD.
28.SHIPPING CORP.OF INDIA LTD.,THE
29.HMT LTD.
30.BEML LTD.
31.CHENNAI PETROLEUM CORP.LTD.
32.FERTILIZERS & CHEMICALS TRAVANCORE LTD.
33.MAHANAGAR TELEPHONE NIGAM LTD.
34.STATE TRADING CORP.OF INDIA LTD.,THE
35.DREDGING CORP.OF INDIA LTD.
36.ITI LTD.
37.ANDREW YULE & CO.LTD.
38.BALMER LAWRIE & CO.LTD.
39.INDIA TOURISM DEVELOPMENT CORP.LTD.
40.MAHARASHTRA ELEKTROSMELT LTD.
41.HINDUSTAN PHOTO FILMS MFG.CO.LTD.
42.BALMER LAWRIE INVESTMENTS LTD.
43.HINDUSTAN ORGANIC CHEMICALS LTD.
44.MADRAS FERTILIZERS LTD.
45.IRCON INTERNATIONAL LTD.
46.SCOOTERS INDIA LTD.
47.BHARAT IMMUNOLOGICALS & BIOLOGICALS CORP.LTD.
48.HINDUSTAN FLUOROCARBONS LTD.
49.KIOCL LTD.
50. HINDUSTAN CABLES LTD.

Q PSE does not exist in ?

CPSE-ETF

The Finance Ministry is expected to launch Central Public Sector Enterprises Exchange Traded Fund (CPSE ETF) .Cabinet Committee on Economic Affairs approved setting up of the fund.

This instrument will comprise listed CPSE stocks, each with a fixed weightage in the basket. The instrument aims to minimise market disruptions seen in public offerings of listed CPSEs. It will also increase the Government's ability to monetise partial stakes in listed CPSEs, some of which have low liquidity and free float. It will broad base retail participation of shares of CPSEs, and also help deepen the market for equity-based products. It is also considered beneficial to the Government from a pricing perspective, as part of the discounts could be back-ended. ETF is a trading instrument like shares on stock exchanges.

At present, there are 33 ETFs with assets under management of over Rs 11,500 crore, held by 6.2 lakh investors. Gold ETFs dominate the market in the country, as of now.

Bretton Woods Institutions & Others

The United Nations Monetary and Financial Conference, commonly known as Bretton Woods conference, was held in Bretton Woods, New Hampshire , USA to regulate the international monetary and financial order after the conclusion of World War II. The conference resulted in the agreements to set up the International Bank for Reconstruction and Development (IBRD)- popularly known as World Bank and the International Monetary Fund (IMF).The IMF was set up to foster monetary stability at global level. The IBRD was created to speed up post-war reconstruction. The two institutions are known as the Bretton Woods twins.

IMF

The International Monetary Fund, a UN specialised agency, was established under the Bretton Woods Agreement in 1944 along with the World Bank. It has 188 members (2014). It is headquartered in Washington and its Managing Director is Christine Lagarde. It started functioning in 1947.

Upon joining, each member of the IMF is assigned a quota, based broadly on its relative size in the world economy. A member's quota guides :

- Subscriptions: the amount the member is obliged to provide to the IMF.
- Voting power
- Access to financing: The amount of financing a member can obtain from the IMF

Upon joining the IMF, a country normally pays up to one-quarter of its quota in the form of widely accepted foreign currencies (such as the U.S. dollar, euro, yen, or pound sterling) or Special Drawing Rights (SDRs). The remaining three-quarters are paid in the country's own currency.

India's current quota in the IMF is SDR (Special Drawing Rights) 5821.50 million, giving it a shareholding of 2.44 %. Based on voting share, India (together with its constituency countries viz. Bangladesh, Bhutan and Sri Lanka) is ranked 17th in the list of 24 constituencies.

The IMF reviews members' quotas once in five years and the last such review took place in December, 2010. India has already consented to its quota increase under the 2010 review and after the 2010 quota review comes into effect, our quota share will increase from the current 2.44% to 2.75%, making India the eight largest quota holding country at the IMF up from its previous position of being the 11th largest. In absolute terms, India's quota will increase to SDR 13,114.4 million from SDR 5,821.5 million (an increase of approximately US$ 11.5 billion or INR 56,000 crore).

IMF Objectives

IMF objectives are

- To promote international monetary cooperation
- To facilitate balanced growth of international trade for the economic growth of all member countries

- To promote exchange rate stability ; maintain orderly exchange rate arrangements; and to avoid competitive exchange rate revaluation
- To help members in times of balance of payments crisis.

What the IMF Does

In order to achieve the above objectives, the following functions are performed:
The IMF monitors the world's economies, lends to members in economic difficulty and provides technical assistance.

To elaborate, the work of the IMF is of three main types.

Surveillance involves the monitoring of economic and financial developments, and the provision of policy advice, aimed especially at crisis-prevention.

The IMF also lends to countries with balance of payments difficulties, to provide temporary financing and to support policies aimed at correcting the underlying problems; loans to low-income countries are also aimed especially at poverty reduction.

Third, the IMF provides countries with technical assistance and training in its areas of expertise.

The IMF also plays an important role in the fight against money-laundering and terrorism

Surveillance is the process of appraisal of the exchange rate policies of member countries. In the absence of surveillance, the financial volatility in the world today can become worse.

Special Drawing Rights (SDRs)

The SDR is an international reserve asset, created by the IMF in 1969 to supplement its member countries' official reserves. Its value is based on a basket of four key international currencies- dollar, euro,yen and pound. SDRs can be exchanged for national currencies.

SDR is neither a currency, nor a claim on the IMF. Rather, it is a potential claim on the freely usable currencies of IMF members. Holders of SDRs can obtain these currencies in exchange for their SDRs.

The value of the SDR is set dynamically against a basket of currencies consisting of the euro, Japanese yen, pound sterling, and U.S. dollar. The basket composition is reviewed every five years to ensure that it reflects the relative importance of currencies in the world's trading and financial systems. China wants Yuan included.

IMF Borrowing Arrangements

While quota subscriptions of member countries are its main source of financing, the IMF can supplement its resources through borrowing if it believes that resources might fall short of members' needs. Through the General Arrangements to Borrow (GAB) and the New Arrangements to Borrow (NAB), a number of member countries and institutions lend additional funds to the IMF.

The GAB and NAB are credit arrangements between the IMF and a group of members and institutions to provide supplementary resources to the IMF to prevent or cope with problems of the international monetary system or to deal with an exceptional situation that poses a threat to international monetary stability.

India and NAB

India funded bailouts in financially-stricken Europe, marking a dramatic role reversal from 20 years ago when it went knocking on the doors of the International Monetary Fund (IMF) to avert a balance of payments crisis.

The government took parliamentary approval to provide loans to the multilateral agency's New Arrangements to Borrow (NAB), a fund whose corpus was raised to $580 billion when the debt crisis in Europe showed no signs of abating after the Greek sovereign debt crisis.

India participates in the Financial Transactions Plan of the International Monetary Fund since 2002.FTP is the mechanism through which the Fund finances its lending and repayment operations to its members.

India gave $10b in 2012 during the Mexico summit of the G-20 for the Eurozone crisis firewall.

How the IMF lends

A core responsibility of the IMF is to provide loans to member countries experiencing balance of payments problems. This financial assistance enables countries to rebuild their international reserves; stabilize their currencies; continue paying for imports; and restore conditions for strong economic growth while undertaking policies to correct the underlying problems. Unlike development banks, the IMF does not lend for specific projects.

IMF Facilities

Over the years, the IMF has developed various loan instruments, or facilities, that are tailored to address the specific circumstances of its diverse membership.

Low-income countries may borrow at a concessional interest rate through the Poverty Reduction and Growth Facility (PRGF) and the Exogenous Shocks Facility (ESF). The Exogenous Shocks Facility (ESF) provides policy support and financial assistance to low-income countries facing global shocks. For example, due to commodity prices falling etc.

Non-concessional loans are provided mainly through Stand-By Arrangements (SBA) for members with very strong policies and policy frameworks, and the Extended Fund Facility (which is useful primarily for low-income members).

The IMF also provides emergency assistance to support recovery from natural disasters and conflicts, in some cases at concessional interest rates.

Except for the PRGF and the ESF, all facilities are subject to the IMF's market-related interest rate.

The amount that a country can borrow from the Fund—its access limit—varies depending on the type of loan, but is typically a multiple of the country's IMF quota. This limit may be exceeded in exceptional circumstances.

Extended Fund Facility (EFF) is to help countries address longer-term balance of payments problems requiring fundamental economic reforms. Arrangements under the EFF are thus longer than SBAs.

The IMF's analysis of global economic developments, contained in its World Economic Outlook, provide finance ministers and central bank governors with a common framework for discussing the global economy. Twice a year, it publishes the Global Financial Stability Report. The IMF's performance is assessed on a regular basis by an Independent Evaluation Office.

IMF and the global financial crisis

As the world economy has become engulfed in the worst crisis since the Great Depression before the second world war, the IMF has mobilized on many fronts to support its member countries, increasing its lending, using its cross-country experience to advise on policy solutions, and introducing reforms to become more responsive to member countries' needs.

Stepping up crisis lending, including a sharp increase in concessional lending to the world's poorest nations.

Overhaul
↓
Examine & repair;
Overtake

Providing analysis and targeted advice.

Becoming more flexible. The IMF has overhauled its general lending framework to make it better suited to country needs.

Creating a financial safety net. The IMF created a broad financial safety net to limit the spread of the crisis.

Drawing lessons from the crisis. The IMF is contributing to the ongoing effort to draw lessons from the crisis for policy, regulation, and reform of the global financial architecture.

The financial crisis of 2008 called the fund into action, as it brokered rescue packages for countries like Pakistan, Iceland, Hungary and Ukraine that were swamped by the collapse.

But since the spring of 2010 the I.M.F. has focused largely on Europe after the outbreak of the sovereign debt crisis that has threatened the euro.

It was drawn into the crisis when France and Germany were unable to agree on a purely European solution to Greece's short-term debt needs. The fund pledged to provide up to 15 billion euros as part of a 45 billion euro aid package. But as the crisis deepened for

Greece and threatened to spread to Spain and Portugal, the fund promised to put up a share of a package that could total 120 billion euros, or $160 billion, over three years.

Christine Lagarde made herself into a blunt voice of dissent, criticizing Europe's handling of the debt crisis for an over-emphasis on austerity. She warned repeatedly that the bailout fund created by the European Union was inadequate to stop the spread of the crisis to larger countries like Spain and Italy, and called for measures to restore growth.

In April 2012, the I.M.F. announced that it had raised at least $430 billion in extra lending capacity to be used if the euro zone crisis worsens or global financial conditions deteriorate.

In June, Ms. Lagarde made her most forceful intervention in the European crisis, as the fund called for the euro area to move swiftly toward a fiscal union including issuance of joint euro zone debt and said the viability of the currency was being questioned.

The fund also said it would like euro zone bailout funds to be lent directly to struggling banks – rather than through national governments – and appealed to the European Central Bank to take more aggressive measures to quell volatile financial markets, such as increasing the money supply or resuming the purchase of the bonds of stressed sovereigns such as Spain.

IMF and Brics

In the wake of the ongoing Eurozone crisis, the IMF has proposed a new bilateral borrowing programme to augment its resources for crisis prevention and resolution and to meet the potential financing needs of all IMF members. At the Los Cabos Summit of the G20 held 2012, BRICS countries have announced their contributions, including US$ 10 billion by each of India, Brazil and Russia and US $ 43 billion by China.

The IMF has committed that these new resources will be drawn only if they are needed as a second line of defense after resources already available from quota and existing borrowing arrangements are substantially used. If drawn, they would be repaid with interest. It has been clarified that quota resources would remain the basic source of fund financing and that the role of borrowing is to temporarily supplement the quota resources.

IMF and Conditionalities

There has been a controversy about the IMF loans that the debtor countries are suggested economic reforms that are socially and in human terms damaging in return.. The conditionalities as they are called are justified by the IMF on grounds that they are the genuine reforms necessary for economic health to be restored. IMF further believes that if the recipient country follows the reforms it will be in a position to repay the loan. Debtor countries however hold that the reforms suggested are anti-poor and anti-development-like cutting subsidies; scrapping priority sector lending; opening up the country at a fast pace etc.

Some of the conditionalities are

/reduce fiscal deficit

/follow privatisation

/deregulate the rupee in external transactions
/downsize the government
/enact flexible labour sector reforms
/reduce subsidies etc.

It is clear that most countries can not follow these policies with popular support. At the same time it must be understood that these policies should be selectively followed for the best results by avoiding populism and adhering to genuine welfarism.

The Fund admitted that too many conditions were imposed on borrowers; it overstepped its mandate and expertise.

Another criticism about the conditionalities is that the reforms suggested are the same for all countries irrespective of the causes of the crisis.

India suggested that the IMF conditionalities must be more sensitive to the domestic realities of the member countries.

Reforming the IMF

Role of IMF was criticized for the following reasons

- One size fits all policy under which it gives the same recipe for all ills
- Conditionalities that go with the loans that it disburses demand that spending on poor be curtailed
- The private international flows are huge and in comparison, the IMF resource base is small and so is rendered ineffective
- IMF Managing Director is invariably from a European country(the current MD, Chritine Lagarde is from France) and India and other emerging markets are demanding that it should not be geographically confined and be merit – based
- India wants that its economic power ,as it is emerging, should be recognized and so is given greater voting rights
- IMF failed to predict the global recession in 2008-09, let alone prevent it with its surveillance role
-

Invariable
↓
never changing

Reforms have taken place after the global crisis in some of these matters.

India and the IMF

India and the IMF have had a friendly relationship, which has been beneficial for both. The IMF has provided India with loans over the years and this has helped the country in times of BOP pressure.

- India joined the IMF in 1945, as one of the IMF's original members.
- India accepted the obligations of Article VIII of the IMF Articles of Agreement on current account convertibility in 1994.
- India subscribes to the IMF's Special Data Dissemination Standard. Countries belonging to this group make a commitment to observe the standard and to provide information about their data and data dissemination practices.

While India has not been a frequent user of IMF resources, IMF credit has been instrumental in helping India respond to emerging balance of payments problems on two

occasions. In 1981-82, India borrowed SDR 3.9 billion. In 1991-93, India borrowed a total of SDR 2.2 billion under two stand by arrangements, and in 1991 it borrowed SDR 1.4 billion under the Compensatory Financing Facility.

The relationship between the IMF and India has grown strong over the years. In fact, the country has turned into a creditor to the IMF and has stopped taking loans from it. We lent $10b in 2012(Mexico G20 Summit) to the IMF to bail out the Eurozone countries.(See India and NAB above)

The Importance of IMF in the post-Lehman period

The IMF saw its international standing strengthened with the global financial crisis of 2008.The global financial crisis, which originated in the U.S. housing market, sparked a growing discussion among policy makers and academics that the world should no longer rely on a single, dominant currency, such as the dollar. Nobel Prize-winning economist Joseph Stiglitz even called for a new global reserve system based on the SDR's.

With the financial crisis intensifying and private capital drying up for credit, more and more countries are coming to the IMF for funds. Recently IMF bailed out Greece.

G20 has agreed that the IMF should triple its borrowing, to ensure that it has enough money to offer loans.

The money is pledged by other IMF countries.

The IMF wants to use this money to offer a new kind of loan that would be preventive. Rather than waiting for countries to get into financial difficulties, it would offer them a line of credit to help them defend their currencies in advance. – NAB- an additional $250bn. This would be done by creating more of its own currency, the SDR or special drawing right.

The IMF is also set to have a bigger role in preventing future crises, by developing an early warning system for financial problems, and taking a larger role in looking at the problems of the financial sector as a whole, in conjunction with a new global regulator, the Financial Stability Board.

But the biggest changes in the IMF involve giving greater voice to the developing countries.(Read ahead).

Another reform:It has already been agreed that in future, the convention that the World Bank and IMF must be headed by an American and a European respectively will be abandoned.

The changes to the resources and the role of the IMF are historic and perhaps the most important development in international monetary system that reflects changing realities.

But it is a move towards a more balanced global system of international finance.

Quotas, GAB and NAB

While quota subscriptions of member countries are the IMF's main source of financing, the Fund can supplement its resources through borrowing if it believes that resources might fall short of members' needs- through the General Arrangements to Borrow (GAB) and the New Arrangements to Borrow (NAB).

SDRs as an alternative to the US dollar as global reserve currency

The international monetary system needs fundamental reform. Dollar as a global reserve currency is neither viable nor desirable to the same degree as before. It has led to problems like the huge current account deficit and fiscal deficit of the USA. Global imbalances- counties like China make and export goods and have current account surpluses and USA import them and depend on them and thus have unmanageable CADs.

John Maynard Keynes once proposed a global currency, the Bancor, to be placed at the centre of the international monetary system. The idea never caught on. Instead, we now have a system dominated by holdings of US dollars. This has disadvantages. It creates tension due to the use of a national currency, the dollar, as the global currency. This can lead to global volatility as a result of growing US current account deficits. These deficits generate excessive indebtedness, both external and internal. So if the US were to shrink its deficit too quickly, a deficiency of supply of the global reserve currency could result.

Responses to global financial instability create the other problem, where developing countries have accumulated large reserves as "self-insurance" against a future balance of payments crisis. These protect them during crises, but also add to global imbalances.
In the late 1960s a more limited global currency was created: the SDRs, issued by the IMF when enough member countries agree. The largest such issue – equivalent to $250bn, and suggested by the G20 in April 2009 – was a response to the dramatic collapse in international private lending after the global financial crisis. It helped soften the negative impact of the crisis on growth.

Some experts argue that the global role of SDRs should be increased as it would avoid the need for countries like India and China to build reserves of dollars. US deficits can also be resolved. Global stability enhances as dollar worries recede. However, SDRs can only supplement the dolar and other global reserve currencies and gold as the SDR is the creation of US and the west within the IMF. If SDR becomes a rival to dollar and yen, it may not receive the support of these countries.

World Bank Group and World Bank

The World Bank Group (WBG) is a family of five international organizations that gives loans, generally to poor countries. The Bank came into existence in 1945 following international ratification of the Bretton Woods agreements, which emerged from the United Nations Monetary and Financial Conference (1944). It is responsible for the preparation of the World Development Report. Commencing operations in 1946, it began operations for post-war reconstruction. Its current role is different as it focus is to lend to and develop the poor countries and help fight poverty in all its facets.

The Group's headquarters are in Washington. It is an international organization owned by member governments; although it makes profits, these profits are used to support continued efforts in poverty escalation.

Technically the World Bank is part of the United Nations system, but its governance structure is different: each institution in the World Bank Group is owned by its member governments, which subscribe to its basic share capital, with votes proportional to shareholding. Membership gives certain voting rights that are the same for all countries but there are also additional votes which depend on financial contributions to the organization. The President of the World Bank is conventionally an American and currently is Jim Yong Kim whose ancestry is from South Korea. There are 188 countries in the WB today.

A country has to first join IMF before it can be a member of the WB.
Its five agencies are:

- International Bank for Reconstruction and Development (IBRD)
- International Development Association (IDA)
- International Finance Corporation (IFC)
- Multilateral Investment Guarantee Agency (MIGA)
- International Centre for Settlement of Investment Disputes (ICSID)

The term "World Bank" generally refers to the IBRD and IDA, whereas the World Bank Group is used to refer to the institutions collectively.

The World Bank's (i.e. the IBRD and IDA's) activities are focused on developing countries, in fields such as human development (e.g. education, health), agriculture and rural development (e.g. irrigation, rural services), environmental protection (e.g. pollution reduction, establishing and enforcing regulations), infrastructure (e.g. roads, urban regeneration, electricity), and governance (e.g. anti-corruption, legal institutions development).

The IBRD and IDA provide loans at soft rates to member countries, as well as grants to the poorest countries. Loans or grants for specific projects are often linked to wider policy changes in the sector or the economy. For example, a loan to improve coastal environmental management may be linked to development of new environmental institutions at national and local levels and the implementation of new regulations to limit pollution.

The activities of the IFC and MIGA include investment in the private sector and providing insurance respectively.

Difference between WB and WB Group

The World Bank differs from the World Bank Group, in that the World Bank comprises only two institutions:

- International Bank for Reconstruction and Development (IBRD)
- International Development Association (IDA)

The IBRD focuses on middle income and creditworthy poor countries, while IDA focuses on the poorest countries in the world.
Whereas the latter incorporates these two in addition to three more:[3]

- International Finance Corporation (IFC)
- Multilateral Investment Guarantee Agency (MIGA)
- International Centre for Settlement of Investment Disputes (ICSID)

IBRD

The International Bank for Reconstruction and Development (IBRD) is one of five institutions that comprise the World Bank Group. The IBRD is an international organization whose original mission was to finance the reconstruction of nations devastated by World War II. Now, its mission has expanded to fight poverty by means of financing states.

IDA

The International Development Association (IDA) , is the part of the World Bank that helps the world's poorest countries. It complements the World Bank's other lending arm — the International Bank for Reconstruction and Development (IBRD) — which serves middle-income countries with capital investment and advisory services.
IDA was created in 1960 and is responsible for providing long-term, interest-free loans to the world's 80 poorest countries. IDA provides grants and credits with repayment periods of 35 to 40 years.

While the IBRD raises most of its funds on the world's financial markets, IDA is funded largely by contributions from the governments of its richer member countries. Additional funds come from IBRD's and IFC's income and from borrowers' repayments of earlier IDA credits.

Donors meet every three years to replenish IDA funds. IDA 15 (IDA 15th Replenishment) projects over the three-year period ending June , 2011.

IDA15 replenishment provided US$ 41.6 billion. IDA15 supports low-income countries by increasing its activities in combating climate change, facilitating regional integration and cooperation, boosting infrastructure investment and providing greater support to post-conflict countries, notably in Africa.A total of 45 countries made pledges to IDA's 15th replenishment

IDA loans address primary education, basic health services, clean water supply and sanitation, environmental safeguards, business-climate improvements, infrastructure and

institutional reforms. These projects are intended to pave the way toward economic growth, job creation, higher incomes and better living conditions.

IDA 16

Donors agreed to contribute nearly $50 billion over three years(2011-14) to the World Bank fund dedicated to the globe's poorest countries.

It supports health, education, food security and building programmes through grants and long-term, interest-free loans to the world's 79 least-developed countries. The fund is replenished every three years at a donors conference. This year it marked a record for giving, with 51 countries agreeing to contribute.
IDA has 172 members.

IFC

The International Finance Corporation (IFC) promotes private sector investment in its member countries, particularly developing countries as a way to reduce poverty and improve people's lives.

IFC is a member of the World Bank Group and is headquartered in Washington. It shares the primary objective of all World Bank Group institutions: to improve the quality of the lives of people in its developing member countries.

Established in 1956, IFC is the largest multilateral source of loan and equity financing for private sector projects in the developing world.

India is one of the founder members of the IFC. IFC finances investments with its own resources and by mobilizing capital in the International financial markets.India has been a member of IFC since 1956. As of June 2012, India held 81,342 shares of IFC, representing 3.43% of IFC's subscribed share capital and 81,592 votes, representing 3.38% of the voting power. Over the past few years, in line with a strong strategic focus on India, IFC has augmented its program and portfolio in India by investing in high impact projects.India represents IFC's single-largest country exposure. As of May 31, 2012, IFC's portfolio of committed investments in India was approximately US$4 billion.In IFC's Fiscal Year 2012, total commitments in India reached US$960 million in 45 projects, distributed across infrastructure, manufacturing, financial markets, agribusiness and renewable energy. The above figures include commitments for IFC's own account and mobilized financing.IFC is scaling up its presence and activities in the Low Income States and NE States (LIS) in India. A new office in Kolkata was set up to focus on the LIS; approximately US$400-500 million has been invested in the LIS over the past three fiscal years. Further, IFC Advisory Services is working in the LIS in the following areas by promoting:

- investment climate for private sector development and inclusive growth;
- financial inclusion by working on financial services and initiatives related to the sustainability of the MFI sector including micro-credit bureau, risk mitigation initiatives, code of conduct setting etc;
- renewable energy (solar and biomass) and cleaner production as well as key subsectors like agribusiness; and

- developing PPP transactions with focus on social services (health and education) and climate change impact projects.
- Infrastructure has been stepped up to 30-40% of IFC's portfolio in India in the last few years and currently accounts for about US$1.3 billion of current committed portfolio.

IFC floated a rupee bond in the global credit market to raise a billion dollars that could be used to assist the Indian companies in 2014.

MIGA

The Multilateral Investment Guarantee Agency (MIGA) is a member of the World Bank group. It was established to promote foreign direct investment into developing countries. MIGA was founded in 1988 and is headquartered in Washington.

MIGA promotes foreign direct investment into developing countries by insuring investors against political risk, advising governments on attracting investment etc.

MIGA can cover only new investments. These include:

- new, greenfield investments;
- new investment contributions associated with the expansion, modernization, or financial restructuring of existing projects; and
- acquisitions involving privatization of state enterprises.

ICSID

The International Centre for Settlement of Investment Disputes (ICSID) is an institution of the World Bank group based in Washington. It was established in 1966 . ICSID has an Administrative Council, chaired by the World Bank's President, and a Secretariat. It provides facilities for the conciliation and arbitration of investment disputes between member countries and individual investors.

India and the World Bank

The advantage of borrowing from the World Bank is the low cost and stable financing it provides with longer maturity periods that better match India's investment needs.

Financing through the International Development Association (IDA), the Bank's concessional lending arm, is provided for as low as 0.75% p.a., repayable over a period of 35 years, inclusive of a 10 year grace period.

India benefited from the WB funds in education(Sarva Shiksha Abhiyan); health care;health care; power; agriculture; irrigation; natural gas , roads and other sectors.

India has been borrowing from the World Bank (through IBRD and IDA) for various development projects in areas of poverty alleviation, infrastructure, rural development, human resource development, etc. IDA funds are one of the most concessional external loans for GOI and are used largely in social sector projects that contribute to the achievement of MDGs. IBRD funds are semi - concessional and of a longer maturity and therefore, cheaper than commercial external borrowings. GOI utilizes IBRD loans primarily for infrastructure projects.

Since 1949 when India took the first assistance from World Bank, the Bank's cumulative commitment to India stands at US$ 91.91 billion {US$ 48.28 billion under IBRD and US$43.63 billion under IDA (up to July, 2012)}.

The support would be for transformative projects, including the Kosi flood recovery project in Bihar state and cleaning up the River Ganga. As part of the overall lending, the Bank also has earmarked USD $3 billion to support the country's domestic response to the global financial crisis.

This includes a USD $2-billion package for the federal government to provide capital to some of the public sector banks so that they could maintain their credit expansion and prevent a shortfall of capital from affecting the economy in the wake of the global economic crisis.

India's enhanced voice

In the recent Capital Increase in IBRD (2010), India has been allocated additional shares. As a result India will become the 7th largest shareholder in IBRD with voting power of 2.91%. Before this revision, India's voting power was 2.77% with 11th position among shareholders. As a constituency (comprising of four countries - India, Bangladesh, Sri Lanka and Bhutan), India's voting power will increase to 3.26% from the present 3.14%. India along with developing countries like China, Brazil, Indonesia, Mexico and Turkey, with greater voting power, would now have more say in the affairs of the World Bank and how its funds are disbursed.China has overtaken Germany, France and the UK to become the third largest shareholder in the Bank with 4.42% voting rights. There is an overall shift of 3% voting share in favour of developing countries, bringing their total vote share to 47%. The change will give emerging nations more say in how the bank is run and how its funds are disbursed.

These changes "are transformative in nature and will reposition the World Bank Group in the international financial architecture".They will strengthen the role the World Bank Group in being an effective multilateral instrument for eradicating poverty, achieving the MDGs (millennium development goals), supporting international efforts to manage global public goods, and most importantly, keeping it relevant in a dynamic world.

Membership of the financial institution gives certain voting rights, which are the same for all countries. But additional votes are granted depending on a country's financial contribution to the organisation.

The International Monetary Fund and the World Bank at a Glance	
International Monetary Fund	**World Bank**
oversees the international monetary system	seeks to promote the economic development of the world's poorer countries
promotes exchange stability and orderly exchange relations among its member countries	assists developing countries through long-term financing of development projects and programs
assists all members--both industrial and developing countries--that find themselves in temporary balance of payments difficulties by providing short- to medium-term credits	provides to the poorest developing countries whose per capita GNP is less than $865 a year special financial assistance through the International Development Association (IDA)
supplements the currency reserves of its members through the allocation of SDRs (special drawing rights)	encourages private enterprises in developing countries through its affiliate, the International Finance Corporation (IFC)
draws its financial resources principally from the quota subscriptions of its member countries	acquires most of its financial resources by borrowing on the international bond market
has at its disposal fully paid-in quotas now totaling SDR 145 billion (about $215 billion)	has an authorized capital of $184 billion, of which members pay in about 10 percent

Financial Stability Board

The Financial Stability Board (FSB), successor to the Financial Stability Forum, was established in 2009 following the G-20 London summit, and includes all G-20 major economies, including India.

The FSB has been established to address vulnerabilities and to develop and implement strong regulatory, supervisory and other policies in the interest of financial stability. It comprises senior representatives of national financial authorities (central banks, regulatory and supervisory authorities and ministries of finance), international financial institutions etc. G20 gave the FSB more power in surveillance role.

FSB is based in Basel, Switzerland.

Financial action task force

In 2010, India has become a member of the Financial Action Task Force (FATF), an inter-governmental body responsible for setting global standards for anti-money-laundering and combating financing of terrorism.

The membership of FATF comes nearly four years after the country became an observer (in 2006) to this elite global body. India is now the thirty-fourth country member of FATF. There are 36 countries in it.

FATF membership is very important for India in its quest to become a major player in international finance, an official release said.

It will help India build the capacity to fight terrorism and trace terrorist money and help to successfully investigate and prosecute money laundering and terrorist financing offences.

India will benefit in securing a more transparent and stable financial system by ensuring that financial institutions are not vulnerable to infiltration or abuse by organised crime groups.

The FATF process will also help in co-ordination of international efforts in anti-money laundering and combating the financing of terrorism, the release added.

The FATF Secretariat is housed at the headquarters of the OECD in Paris.Its President is Mr.Corral.

Asian Clearing Union

The Asian Clearing Union (ACU) was established with its head quarters at Tehran, Iran in 1974 at the initiative of the United Nations Economic and Social Commission for Asia and Pacific (ESCAP), for promoting regional co-operation. The main objectives of a clearing union are to facilitate payments among member countries for eligible transactions on a multilateral basis, thereby economizing on the use of foreign exchange reserves and transfer costs, as well as promoting trade among the participating countries. The Central Banks and the Monetary Authorities of Iran, India, Bangladesh, Bhutan, Nepal, Pakistan, Sri Lanka, Myanmar and Maldives are currently the members of the ACU.

The Asian Monetary Units (AMUs) is the common unit of account of ACU and is denominated as 'ACU Dollar' and 'ACU Euro', which is equivalent in value to one US Dollar and one Euro, respectively. All instruments of payment under ACU have to be denominated in AMUs.

Reserve Bank receives and pays US Dollars / Euros.
All permitted current account transactions including export / import transactions between ACU member countries are eligible to be settled through the ACU.
India- Iran oil payments

In 2010, Reserve Bank of India has barred Indian companies from using the Asian Clearing Union (ACU) to process current account transactions for oil and gas . India makes $12 billion worth of oil imports annually from the Islamic Republic. In 2009, Iran asked Indian companies such as ONGC to use the ACU to avoid being targeted by U.S. extra-territorial sanctions. But since the U.S. Treasury, which enforces those sanctions, is unable to monitor ACU transactions, Washington had been pressuring Delhi to shut down this route. ACU transactions are made by the central banks and the individual companies and their identities are not known. Thus, USA can not punish them for dealing with Iran.

Under the ACU mechanism, imports by the nine nations are settled every two months with every member paying for imports after netting out its exports among the union. Till 2008, payment under the ACU mechanism was done in US dollars, but after the United States imposed sanctions on Iran over its suspected nuclear programme, the currency was shifted to Euro.

Companies can't deal with the U.S. and EU companies if they have invested over $20 million in Iran.This led to Reliance abandoning plans to invest in an oil refinery in Iran as it saw diminished chances of participating in shale gas exploitation after having bought a stake in a U.S. company.

Without mentioning Iran, the RBI cited unspecified "difficulties being experienced by importers and exporters" while asking companies to stop using the ACU.

In a solution under discussion, banks and oil companies would put in place an alternative means of settlement for India's oil purchases from Iran.

South Korea pays for Iranian crude using the Won.We can explore to do our business in other currencies like (Emirate) dirham.

Trade in each other's currency (rupee and Rial) is not feasible as India's imports are many times more than exports. (← means ∵ imports are more rupee will be weaker compared to rial)

ADB

ADB is an international development finance institution whose mission is to help its developing member countries reduce poverty and improve the quality of life of their people.

Headquartered in Manila, and established in 1966, ADB is owned and financed by its 67 members, of which 48 are from the region and 19 are from other parts of the globe.
ADB's main partners are governments, the private sector, nongovernment organizations, development agencies, community-based organizations, and foundations.
Under Strategy 2020, a long-term strategic framework adopted in 2008, ADB will follow three complementary strategic agendas: inclusive growth, environmentally sustainable growth, and regional integration.In pursuing its vision, ADB's main instruments comprise loans, technical assistance, grants, advice, and knowledge.ADB President is Haruhiko Kuroda.

G-20

The Group of Twenty (G-20) Finance Ministers and Central Bank Governors was established in 1999 to bring together systemically important industrialized and developing economies to discuss key issues in the global economy. The inaugural meeting of the G-20 took place in Berlin in 1999, hosted by German and Canadian finance ministers.

Mandate

The G-20 is the premier forum for our international economic development that promotes open and constructive discussion between industrial and emerging-market countries on

key issues related to global economic stability. By contributing to the strengthening of the international financial architecture and providing opportunities for dialogue on national policies, international co-operation, and international financial institutions, the G-20 helps to support growth and development across the globe.

Origins

The G-20 was created as a response both to the financial crises of the late 1990s and to a growing recognition that key emerging-market countries were not adequately included in the core of global economic discussion and governance.

Membership

The G-20 is made up of the finance ministers and central bank governors of 19 countries:

- Argentina
- Australia
- Brazil
- Canada
- China
- France
- Germany
- India
- Indonesia
- Italy
- Japan
- Mexico
- Russia
- Saudi Arabia
- South Africa
- Republic of Korea
- Turkey
- United Kingdom
- United States of America

The European Union, who is represented by the rotating Council presidency and the European Central Bank, is the 20th member of the G-20. To ensure global economic fora and institutions work together, the Managing Director of the International Monetary Fund (IMF) and the President of the World Bank, plus the chairs of the International Monetary and Financial Committee and Development Committee of the IMF and World Bank, also participate in G-20 meetings on an ex-officio basis. The G-20 thus brings together important industrial and emerging-market countries from all regions of the world. Together, member countries represent around 90 per cent of global gross national product, 80 per cent of world trade (including EU intra-trade) as well as two-thirds of the world's population. The G-20's economic weight and broad membership gives it a high degree of legitimacy and influence over the management of the global economy and financial system.

Achievements

To tackle the financial and economic crisis that spread across the globe in 2008, the G20 members were called upon to further strengthen international cooperation. Accordingly, the G20 Summits have been held in Washington in 2008, in London and Pittsburgh in 2009, and in Toronto and Seoul in 2010.

The concerted and decisive actions of the G20, with its balanced membership of developed and developing countries helped the world deal effectively with the financial and economic crisis, and the **G20 has already delivered a number of significant and concrete outcomes:**

First, the scope of financial regulation has been largely broadened, and prudential regulation and supervision have been strengthened. There was also great progress in policy coordination. Finally, global governance has dramatically improved to better take into consideration the role and the needs of emerging of developing countries, especially through the ambitious reforms of the governance of the IMF and the World Bank.

Chair

G-20 (like the G-7) has no permanent staff of its own. The G-20 chair rotates among members, and is selected from a different regional grouping of countries each year. In 2014 the G-20 chair is Russia

Meetings and activities

It is normal practice for the G-20 finance ministers and central bank governors to meet once a year.

Interaction with other international organizations

The G-20 cooperates closely with various other major international organizations and fora- World Bank and IMF. The G-20 also works with, and encourages, other international groups and organizations, such as the Financial Stability Board and the Basel Committee on Banking Supervision.

8 members

How does the G-20 differ from the G-7?

The G-7 was established in 1976 as an informal forum of seven major industrial economies: Canada, France, Germany, Italy, Japan, the United Kingdom and the United States of America. Russia joined later.The G-7 conducts dialogue and seeks agreement on current economic issues on the basis of the comparable interests of those countries. The G-20 was established in 1999 and reflects the diverse interests of the systemically significant industrial and emerging-market economies. It has a high degree of representativeness and legitimacy on account of its geographical composition (members are drawn from all continents) and its large share of global population (two-thirds) and world GNP (around 90 per cent). The G-20's broad representation of countries at different stages of development gives its consensus outcomes greater impact than those of the G-7.

Miscellany

Every G-20 member has one 'voice' with which it can take an active part in G-20 activity. To this extent the influence a country can exert is shaped decisively by its commitment. There are no formal criteria for G-20 membership and the composition of the group has remained unchanged since it was established. In view of the objectives of the G-20, it was considered important that countries and regions of systemic significance for the international financial system be included. Aspects such as geographical balance and population representation also played a major part.

The G-20 Finance Ministers were tasked from the Pittsburg Summit to take forward work in the following areas;

- Framework for Strong, Sustainable, and Balanced Growth
- Strengthening the International Financial Regulatory System
- Modernizing our Global Institutions to Reflect Today's Global Economy
- Reforming the Mandate, Mission, and Governance of the IMF
- Reforming the Mission, Mandate, and Governance of Our Development Banks
- Energy Security and Climate Change
- Strengthening Support for the Most Vulnerable
- Putting Quality Jobs at the Heart of the Recovery
- An Open Global Economy

Summits

The G-20 Summit was created as a response both to the financial crisis of 2007–2010 and to a growing recognition that key emerging countries were not adequately included in the core of global economic discussion and governance. The G-20 Summits of heads of state or government were held in addition to the G-20 Meetings of Finance Ministers and Central Bank Governors who continued to meet to prepare the leaders' summit and implement their decisions. After the debut summit in Washington, D.C. during 2008, G-20 leaders held 8 summits, the last being in Russia. 2014 and 2015 will be held in Australia and Turkey respectively.

G20 meeting → FM & governor
G20 summit → Heads of state

OECD

The Organisation for Economic Co-operation and Development (OECD) is an international economic organisation of 34 countries founded in 1961 to stimulate economic progress and world trade. It defines itself as a forum of countries committed to democracy and the market economy, providing a platform to compare policy experiences, seeking answers to common problems, identifying good practices, and co-ordinating domestic and international policies of its members.

The OECD originated in 1948. Later, its membership was extended to non-European states. The OECD's headquarters are in Paris.

ECB

The European Central Bank (ECB) is the institution of the European Union (EU) which administers the monetary policy of the 17 EU Eurozone member states. It is thus one of the world's most important central banks. The bank was established by the Treaty of Amsterdam in 1998, and is headquartered in Frankfurt, Germany. The current President of the ECB is Jean-Claude Trichet, former president of the Banque de France.

International financial stability architecture for the 21st century

The institutions involved are:

IMF

- G-20 and G20 Summit since 2008
- FSB: In response to the global financial crisis, the international financial community established the Financial Stability Board (FSB). The FSB aims to address vulnerabilities and develop and implement strong regulatory, supervisory and other policies in the interest of financial stability.
- BIS, Basel.

Summit → Head of govt

- WB and ADB provide economic assistance so that the long term economic underpinings of global economy are strengthened.

Bretton Woods 2.0

The original Bretton Woods conference purpose was post –WWII reconstruction. The arrangements need redefinition and refocus in the post-recession world since 2008. The broad mandate should be

- we need to restructure global finance, based on an expanded system of capital adequacy standards, financial reporting, system-wide risk management etc. FSB and BIS can have a larger role in this matter.
- IMF should have an expanded role and be the lender of last resort. SDRs should be more central to global monetary system
- World Bank should be refocused with clear goals, and accountability for their success. Specifically, the bank should have one overarching assignment: helping the poorest countries achieve the millennium development goals to reduce poverty, hunger and disease.
- global trade agenda should be reoriented A trade agreement worthy of the effort would do two main things. Importantly, it would help the poorest countries to be more productive ;global trade would promote environmental sustainability, to help enforce compliance with reduced carbon emissions and protection of endangered biodiversity
- the new global financial structure should help to rescue the world from human-induced climate change. A tax on the carbon content of fossil fuels, levied by all countries, would do the job.
- G20 summit should be the policy guidance platform.

Brics Fund and bank

The BRICS emerging economies will set up a $100 billion fund to steady currency markets. China, holder of the world's largest foreign exchange reserves, will contribute the bulk of the currency pool. The initiative to establish a BRICS currency reserve pool is at its final stage. China committed $41 billion; Brazil, India and Russia $18 billion each; and South Africa $5 billion.

A joint BRICS development bank, with capital of up to $50 billion is also on the anvil It is called New development bank.

WTO and GATT-I

The General Agreement on Tariffs and Trade (GATT) is an agreement that was arrived at in 1947 by 23 countries to establish an free and fair international trading regime among member countries based on dismantling of trade barriers -tariffs or non-tariff restrictions like quotas . It came into existence in 1948. India was a founding member. GATT progressed- expanded its scope in terms of areas covered - by a series of "trade rounds"- negotiations centered around a specific set of issues over a period of a few years leading to agreement among members are called a round. GATT GATT was headquartered in Geneva, Switzerland. Eight rounds of such negotiations were held under GATT:

For ~~zero~~ volume of a good the tariff is x & for increased volume (y+) tariff ↑

- Havana Round (1947) with 23 countries brought into being the. GATT.
- Annecy (France) Round (1949) (France)
- Torquay Round(England) (1950) (England)
- Geneva Fourth Round (1956)
- Dillon Round (1960-1961) was held in Geneva and were named after Under Secretary of State, Douglas Dillon, who first proposed the talks
- Kennedy Round (1962-1967) was also held in Geneva but was named after the US President John F Kennedy, in his memory.
- Tokyo Round (1973-1979)
- Uruguay Round (1986-94)

WTO was set up as a result of the Uruguay Round. WTO came into existence in 1995. Doha Round is the first round under the WTO (2001-). It is yet to complete.

As can be seen from the above, the Uruguay round lasted the longest (doha round is taking longer) as it took place in a radically different set of circumstances- communism was collapsing; the model of western industrial democracies was becoming more acceptable to the developing countries; USSR disintegrated leaving the third world so much weaker in world diplomacy. New areas were brought into the agenda- intellectual property rights; agriculture; services; foreign direct investment and so on. Initially, the developing countries were reluctant and resisted the expansion of the agenda. But partly due to western force; lack of unity; and partly due to seeing benefits for themselves, they agreed. There was no agreement after protracted negotiations. The Director General of the GATT was asked to draft an agreement for the consideration of the members. It was called Dunkel Draft, named after the Director General Arthur Dunkel. After attaining consensus, it was made into the Marrakesh Treaty and was signed in Marrakesh (Morocco) in 1994 and paved the way for the establishment of World Trade Organization (WTO)at the beginning of 1995.

Protracted ↓ lasting longer than usual or expected

GATT and WTO

GATT is different from WTO in two essential respects- GATT is a treaty while WTO is an organization. GATT had no dispute settlement process while WTO has. The GATT was essentially concerned with traditional trade issues such as tariffs and quotas in international trade. It had only a relatively small secretariat with no institutional foundation to implement these rules.

The World Trade Organization that came into existence at the beginning of 1995 replaces the General Agreement on Tariffs and Trade(GATT). Like its predecessor, it is headquartered in Geneva, Switzerland. It has 159 members. Roberto Azevedo from Brazil is the current Director-General of the World Trade Organization.GD term is 4 years.

The WTO states that its aims are to increase international trade by slashing trade barriers and providing a platform for the negotiation of trade and related issues . Basically, it sets up a rule based multilateral trading system to liberalise the regime and boost world trade.
Principles guiding the WTO are

- non-discriminatory and rule-based trading system where foreign goods and services should receive the same treatment as domestically sourced ones
- trade barriers (tariffs and non-tariff barriers) should be dismantled and international trade should be free
- less developed countries should receive preferential terms of trade

Unlike other organizations like World bank and the International Monetary Fund(IMF) where there is weighted voting- a country has as much voting power as it contributes financially-, WTO has a 'one country one vote' system making it relatively democratic. Decisions are taken by consensus.

WTO is not part of the United Nations and acts autonomously at the behest of its membership. A global arrangement exists between the two, based on the relationship that had existed between the UN and the WTO's predecessor, the General Agreement on Tariffs and Trade (GATT). This includes provision and exchange of information, representation at each other's meetings and cooperation between the secretariats.

Structure of WTO

Highest level decision-making body of the WTO is the Ministerial Conference, which usually meets once every two years with each member country represented by the commerce minister. Next in authority is the General Council which carries out the decisions of the Ministerial Conferences. It is seated in Geneva. It has representatives (usually ambassadors or equivalent) from all member governments and has the authority to act on behalf of the ministerial conference

There are two other bodies apart from the General Council. They are the Dispute Settlement Body composed of all members, usually represented by ambassadors or equivalent; and Trade Policy Review Body (TPRB) - the WTO General Council meets as the Trade Policy Review Body to undertake trade policy reviews of Members.
Below the above three bodies, at the third level, there are Councils for Trade.The Councils for Trade work under the General Council. There are three councils - Council for Trade in Goods, Council for Trade-Related Aspects of Intellectual Property Rights, and Council for Trade in Services.. Apart from these three councils, six other bodies report to the General Council on issues such as trade and development, the environment, regional trading arrangements and administrative issues.

At the fourth level from the top, there are subsidiary bodies- various committees and working groups related to various fields.

Dispute Settlement

World Trade Organization (WTO) has a dispute settlement body (DSB) that settles trade disputes among members. Disputes can arise from trade policies of members that are violative of the WTO rules.

WTO procedures require sixty days of 'consultations' among the disputants to resolve the dispute failing which a disputes panel is set up.

There is no separate DSB but the General Council which is the second highest body in the organization works as the DSB while giving verdict on the trade dispute. DSB conclusion can be challenged in an appellate body.

After the ruling, the erring nation is directed to make changes in its laws to make them WTO-compliant within a reasonable time. If the 'losing country' does not correct its laws, the complainant country is allowed to take cross retaliatory measures.

On the face of it, it gives all member countries a level playing field as the process is multilateral. But the fact is that there is no punishment for the erring country and ; poor countries can not retaliate against rich countries.

WTO members and observers.

There are 159 members in the WTO. 25 countries enjoy observer status at the WTO. In addition to states, the European Union is a member. WTO members do not have to be full sovereign nation-members. Instead, they must be a customs territory with full autonomy in the conduct of their external commercial relations. Thus Hong Kong (as "Hong Kong, China" since 1997) became a GATT contracting party, and the Republic of China (Taiwan) acceded to the WTO in 2002 as "Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu" (Chinese Taipei) despite its disputed status. Iran is the biggest economy outside the WTO.

Chronology

- 1986-1994 - Uruguay Round of GATT negotiations were deadlocked. Dunkel Draft was the basis for the resolution. It led to the Marrakesh Agreement(Morocco) that resulted in the WTO coming into force.
- January 1, 1995 - The WTO came into existence.
- 1996 - The first ministerial conference in Singapore. Birth of "Singapore issues".
- 1998 – Second ministerial conference in Geneva, Switzerland.
- 1999 – Thi rd ministerial conference in Seattle, Washington, USA
- 2001 - Fourth ministerial conference in Doha, capital of Qatar. A new Round of trade talks begin called Doha Development Round.
- 2001 - The People's Republic of China joined the WTO after 15 years of negotiations (the longest in GATT history).
- 2002 - Taiwan joined under the name "Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu".
- 2003 – Fifth ministerial conference in Cancún, Mexico . Formation of G20 . Rejection of the 'overloading' of the Doha agenda with Singapore issues though trade facilitation which is one of the Singapore issues was accepted by all
- 2005 – Sixth Ministerial at Hong Kong once again failed to deliver results
- Seventh Ministerial 2009 in Geneva and 8th in 2011 in Geneva
- 9th Ministerial in Bali 2013 December

WTO Agreements

The WTO oversees about 60 different agreements which have the status of international legal texts. Member countries must sign and ratify all WTO agreements on accession. Important among the agreements are the following.

Agreement on Agriculture (AoA)

One of the most contentious issues that the Uruguay Round addressed was agriculture. When the Marrakesh Treaty was signed in 1994, AoA was resisted by the developing countries. They were won over with some concessional features and flexibilities. Its three pillars are

- domestic support
- export subsidies
- market access

Domestic support

It refers to the subsidies that governments give to the farmers like food, fertilizer, power, water etc . The domestic subsidies are grouped into three classes called "boxes": Green Box, Amber Box and Blue Box- the first two being borrowed from the traffic light colours.

Green box

Agriculture-related subsidies that fit in WTO's green box are policies that are not restricted by the trade agreement because they are not considered trade distorting.

Related to agri only

To qualify for the green box, WTO says a subsidy must not distort trade, or at most cause minimal distortion.

These green box subsidies must be government-funded — not by charging consumers higher prices, and they must not involve price support. They tend to be programs that are not directed at particular products, and they may include direct income supports for farmers that are decoupled from current production levels and/or prices.Examples: environmental and conservation programs, research funding, extension services, domestic food aid including food stamps, and disaster relief.

Amber box

Agriculture's amber box, according to the WTO, is used for all domestic support measures considered to distort production and trade.

Domestic subsidy eg: Food security bill

WTO members are required to maintain their amber box supports to within five to 10 percent of their value of production.

Any support payments that are considered to be trade distorting and are subject to limitations and disciplines fall into the amber box.

Blue box

Not subject to reduction commitments under Uruguay Round.

Included in the blue box are any support payments that are not subject to the amber box reduction agreement because they are direct payments under a production limiting program.

Subsidies given by USA and Europe make agricultural goods so cheap that their markets are virtually inaccessible to exports from developing countries. The earlier gains expected by the developing countries from an genuinely free international trade in agricultural goods have not come about as the advanced countries are least inclined to reduce the subsidies to the statutory levels. It is one of the 'implementational concerns' in WTO being discussed in the Doha round.

In the Bali ministerial in 2013 December, it was a contentious issue.(Details ahead)

G33

The **G33** is a group of developing countries that coordinate on agricultural trade and economic issues. It was created in order to help a group of countries that were all facing similar problems.

The G33 has proposed special rules for developing countries at WTO negotiations, like allowing them to continue to restrict access to their agricultural markets. **The Group of 33 developing countries that operates in the WTO's agriculture negotiations have similar position on designation of special products where they want to have higher tariffs on imports.**

so the consumers should not import those Products & domestic small producer is protected

The G-33, led by Indonesia, has been insisting on a change in WTO rules on agriculture that bring food procurement from poor farmers to feed the poor under a subsidy cap fixed at 10 per cent of farm produce. It has also been demanding a change in the methodology for subsidy calculation that is still based on a price index of 1986-88 and does not factor in inflation.

Export subsidies

"Export subsidies" are to be limited by the developed countries either in value or volume terms so that international prices are not lowered below a point and exports of the developing countries are not priced out..

Market Access

Market access means all member countries should throw open their domestic market to agricultural imports by reduction of tariffs and removal of or non-tariff barriers. Countries should undertake

- 'Tariffication'- to convert non–tariff barriers(like quotas) to tariffs and
- "bind" their tariffs- to agree to a limit that is the 'bounded rate' and not increase the rates beyond them. The bounded rates are usually high

AoA can be expected to, in the long run, benefit the developing countries that have cost advantages in production. However, any such benefits are conditional on the developed countries reducing their subsidies.

TRIPS

Intellectual property (IP) is the work of intellect or mind to create products that have commercial uses- products like drugs, literature, paintings etc. It is protected like the physical property with trade marks, patents etc. Holders of the patents etc are entitled to the commercial proceeds for a specified time period, exclusively

Types of intellectual property rights:

- A patent may be granted for a new, useful, and non-obvious invention, and gives the patent holder an exclusive right to commercially exploit the invention for a certain period of time (typically 20 years from the filing date of a patent application).
- Copyright is given for creative and artistic works (e.g. books, movies, music, paintings, photographs, and software) and give a copyright holder the exclusive right to control reproduction or adaptation of such works for a certain period of time.
- A trademark is a distinctive sign which is used to distinguish the products or services of different businesses.

- An industrial design right protects the form of appearance, style or design of an industrial object (e.g. spare parts, furniture, or textiles).

The need for agreement on TRIPS arises from the fact that the commercial proceeds from international trade in intellectual property are growing in worth.

Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs)
Agreement on TRIPS lays down legal standards for the member countries to protect intellectual property by way of copyright rights; geographical indications, industrial designs; integrated circuit layout-designs; patents; monopolies for the developers of new plant varieties; trademarks. TRIPs regulates dispute resolution procedures and enforcement procedures.

TRIPS and patents
A patent is an exclusionary right. It grants the right to exclude others from making use of the patented invention for the given period of 20 years from the filing date. In return for the patent, the inventor offers the knowledge with commercial use to be put in public domain after the expiry of the patent. Patent is an incentive to innovate and invent. It sustains research and development (R and D)

Product and process patents
Under WTO, patents can be granted for the process or product. Product patents provide for absolute protection of the product exhausting all the process that may lead to the product, whereas process patents provide protection in respect of the technology and the process or method of manufacture. Protection for process patents would not prevent the manufacture of patented products by a process of reverse engineering, where a different process or method from that which has been invented (and patented) is used. For example, national legislation requiring only process patent protection has enabled manufacturers in certain countries to make generic versions of patented medicines. RE (Reverse engineering) made it possible in developing countries to sell medicines cheap. India is a prime example.

TRIPS agreement allows both process and product patents , though only product patents must be awarded for food, pharmaceuticals and chemicals. Patents should be valid for 20 years. Developing countries have 10 years to adopt the TRIPS agreement standards while the advanced countries adopted them by 1995 itself.

TRIPS agreement is an integrated package . Developing countries that had apprehensions about the product patents agreed to it because they benefited under other agreements- for example, services etc. They agreed also because they received concessional terms under TRIPS- grace period of 10 years to adopt product patents in food, pharmaceutical and chemical fields.

Geographical Indications
There are world famous goods that owe their origin to the region in which they originate and are nurtured. The climate, soil and the native efforts of the region account for their fame, utility and qualities. **Some Indian examples are:** Basmati Rice, Darjeeling Tea, Kanchipuram Silk Saree, Alphanso Mango, Nagpur Orange, Kolhapuri Chappal, Bikaneri Bhujia, Agra Petha , Mysore silk, Nilgiri tea, Coorg coffee, Mysore sandal products, Malabar pepper etc.

GI is granted to a community or group or an institution that represents the interests of the product. It is generally not granted to an individual. It is given to a product for a specific period of time (10 years in India).The product can be an agricultural, natural or manufactured one. The manufactured goods should be produced or processed or prepared in that territory. It should have a special quality or reputation or other characteristics

If these products and processes are given geographical indication registration, commercial proceeds can accrue to the holder of the GI. GIs prevent spurious goods from entering the market It helps maintain quality . There is greater accountability, too. It boosts exports

Spurious → false/fake

In 1999, the Parliament passed the Geographical Indications of Goods (Registration and Protection) Act, 1999. This Act seeks to provide for the registration and protection of geographical indications relating to goods in India. The Act is administered by the Controller General of Patents, Designs and Trade Marks- who is the Registrar of Geographical Indications. The Geographical Indications Registry is located at Chennai.

The Geographical Indications of Goods (Registration and Protection) Act, 1999 came into force in 2003. This is a sui generic legislation intended to give better protection to GIs of India.

→ of its own kind

As per the Geographical Indications Act, 1999 "Any association of persons or producers or any organization or authority established by or under any law for the time being in force representing the interest of the producers of the concerned goods" may file an application for registration of a GI. This is in keeping with the overall objective of the G.I. Act, which is to protect the identity of a particular good that has properties which are attributable to a particular region or which are manufactured in a particular region.

Oranges of Nagpur, paintings of Kangra, Moradabad metal craft and Kolhapur jaggery are among 14 items waiting for Geographical Indications (GI) tag.

Once conferred, the uniqueness of these products will be statutorily insulated from false claimants trying to exploit their regional exclusivity. Already 195 items including Kancheepuram silk and Darjeeling tea from various states enjoy the protection.

The products about to get the protection are: Nagpur orange, Kangra painting, Moradabad Metal Craft, Firozabad Glass, Kannauj Perfume, Kanpur saddlery, Saharanpur wood craft, Dharmavaram handloom pattu sarees and paavadas, Warli painting, Kolhapur jaggery, Thewa art work and three Manipur-based knit works Moirang phee, Wangkhei phee and Shaphee lanphee.

Maharashtra government's Akola-based Dr Panjabrao Deshmukh Kirshi Vidyapeeth has applied for Nagpur orange under horticultural product category, saying the oranges differed from others in growth habit, physical-chemical properties and taste. "Its pulp is tender, saffron or orange coloured with excellent blend of sugar-acid," the application said. It said the fruit is cultivated in Nagpur and Vidharbha region of Maharashtra and some parts in adjoining regions of Madhya Pradesh.

Himachal Pradesh's Kangra Arts Promotion Society has sought GI saying the art form was invogue in the foothills of western Himalayas and pigments used in Kangra paintings are

derived from organic and inorganic sources. The central theme of Kangra paintings is love and the recurring themes are six seasons or music or Krishna-Radha or Shiva-Parvati.

Manipur government's department of commerce has sought GI for Moirang phee, Wangkhei phee and Shaphee lanphee, which are shawls/fabric with unique needle work, to be worn as special recognition of honour.

Kolhapur jaggery seeks unique recognition for its white and golden chemical-free product having no added colour, chemicals, additives and flavours. Its application said the jiggery had natural sweetener and contained glucose, vitamins, calcium and minerals.

As of April 2013, Karnataka with 32 GI products topped the national list followed by Tamil Nadu (24), Andhra Pradesh (22) and Kerala (20).

French champagne and cognac, the USA's Napa Valley, the UK's Scotch whisky and Mexican Tequila are among foreign products that have acquired GI tag in India.

Patents (Amendment) Act 2005

Indian Parliament passed the Patents (Amendment) Bill 2005. It introduced product patent regime for food, chemicals and pharmaceuticals. India was required to introduce product patent protection in these sectors from 1.1.2005 in accordance with the obligation under the TRIPS Agreement of the WTO. 10yrs from 1995

Highlights of the Act

- Product patent protection to drugs, foods and chemicals
- availability of Pre-grant and Post-grant challenge
- discovery of a new form of a known substance does not qualify for a patent; nor mere discovery of any new property or new use for a known substance
- Introduction of a provision for enabling grant of compulsory license and parallel imports to meet public health crises

Prior to 1970, 85 per cent of medicines available in India were produced and distributed by multinational corporations (MNCs) and the prices of drugs in the country were among the highest in the world. The 1970 Patents Act of India provided for process patents for pharmaceuticals and agro-chemical products. This enabled the growth of a strong local generic drug industry, which produced the same drugs as the MNCs at relatively low prices. When Indian generic manufacturers such as Cipla, Ranbaxy etc began manufacturing drugs, especially for Human Immunodeficiency Virus/Acquired Immune Deficiency Syndrome (HIV/AIDS), at much lower prices, it served a public health cause .The demand for these drugs grew in countries that could not afford to buy these drugs from MNCs.

Indian government accepted TRIPS and product patents because Indian pharma industry is going global and trips help R and D; also, TRIPS is a part of the larger WTO package.

There is a fear that prices of medicines will spiral due to product patents as it can lead to monopoly pricing. Some experts say the fear is unfounded because 97 per cent of all drugs manufactured in India are off-patent and will remain unaffected.

On the positive side, the Act modernizes the law. It helps Indian pharma companies to grow into MNCs. Indian companies can take up contract research. FDI will flow in with all the technological benefits.Safeguard provisions help meet public health concerns. Drug price Control order (DPCO) gives government the power to regulate the prices and make them affordable. Generic manufacturers can continue in India for product patented drugs by paying a reasonable fees. (Generic medicines are unbranded drugs . They can be produced for drugs for which either there is a process patent or the product patent expired. Once product patents are introduced for drugs, generic manufacturers can not continue in India except when they pay a fee if the patent holder agrees)

Another criticism is that it acts as a roadblock to cheap drugs. Indian generic companies brought down the prices of antiretroviral therapy for HIV/AIDS from $12,000 to $140 a year. Two-thirds of the world' s population will be systematically deprived of life-saving drugs when the Indian law comes into effect. Countries in Africa are dependent on Indian generic products and the WHO [World Health Organisation] expressed apprehensions about the Act.

The other criticism is that patents being given for 20 years will stunt technological development in India.

However, supporters argue that that product patents provide an opportunity for greater investment in R and D and exploitation of global markets. Prices also may not rise much as there is bound to be competition and also government regulation. DPCO- Drug Price Control Order of the Government ensures that essential drugs are sold cheap.Another reassurance about whether TRIPS can cripple public health concerns relates to compulsory licensing and parallel imports.

IPRs 2013

The Intellectual Property Appellate Board (IPAB) recently revoked GlaxoSmithKline's patent in India for its breast cancer drug Tykerb, a decision that took its cue from a recent landmark Supreme Court court ruling disallowing "repetitive patents" on the same drug.
The board has, however, upheld the patent for lapatinib, the original compound, citing innovative merit. IPAB ordered that the claimed invention, the salt version of the original drug, is "obvious" and, therefore, has been revoked.

Revoke → make law/order not valid anymore

This bears out India's policy stance that incremental inventions lacking "enhanced therapeutic efficacy" as assessed by the patenting authorities under Section 3(d) of the Patents Act won't qualify for patents. In April 2013, the Supreme Court in a landmark ruling rejected Swiss drug-maker Novartis' plea for a patent for its anti-cancer drug Glivec — beta crystalline of a known molecule called imatinib mesylate — saying it lacked novelty and failed to meet the country's patenting standards.

In 2012 , India revoked three patents on grounds that included lack of novelty/inventive step. These were for Pfizer's cancer drug Sutent, Roche Holding's hepatitis C drug Pegasys, and Merck's asthma treatment aerosol suspension formulation.

Compulsory licensing

The Intellectual Property Appellate Board (IPAB) in 2013 upheld the grant of compulsory licence (CL) to the Hyderabad-based Natco Pharma Limited, a generic drug maker, to produce and market Nexavar, a patented cancer drug of multinational pharma major Bayer

Corporation. The order will pave the way for reduction in the prices of costly life saving drugs.

Various international conventions and Indian laws allowed the member countries to grant such compulsory licence in order to make medicine cheaply available to the public.

IPAB directed Natco to pay seven percent royalty.

Bayer obtained a patent in India in 2008 for Nexavar which cost Rs. 2.8 lakh for a pack of 120 tablets, equivalent to a month's dosage. Controller of Patents, Mumbai, granted the first-ever compulsory licence to Natco to make 'sorofenib tosylate', a generic version of Bayer's high-priced anti-cancer drug Nexavar. Natco was told to sell the pack at Rs. 8,800.

Bayer appealed against the Controller's order before the IPAB. Upholding the compulsory licence, the IPAB pointed out that even after obtaining patent, Bayer had not made the drug available on a large scale and at an affordable price within the stipulated time.

Counterfeit
↓
Not genuine
or forged

The **Anti-Counterfeiting Trade Agreement (ACTA)**

It is a multinational treaty for the purpose of establishing international standards for intellectual property rights enforcement. The agreement aims to establish an international legal framework for targeting counterfeit goods, genericmedicines and copyright infringement on the Internet, and would create a new governing body outside existing forums, such as the World Trade Organization, the World Intellectual Property Organization, or the United Nations.

The agreement was signed in October 2011 by Australia, Canada, Japan, Morocco, New Zealand, Singapore, South Korea, and the United States. In 2012, Mexico, the European Union and 22 countries which are member states of the European Union signed as well. Supporters have described the agreement as a response to "the increase in global trade of counterfeit goods and pirated copyright protected works". Opponents say the convention adversely affects fundamental rights including freedom of expression and privacy. ACTA has also been criticised by Doctors Without Borders for endangering access to medicines in developing countries. It is not Trips Plus but is Trips minus.

In a huge boost to makers of generic medicines, the European Union (EU) parliament in 2012 rejected ACTA.

Public Health Concerns :TRIPS Agreement and Safeguards

Safeguards in the TRIPS Agreement include provisions that allow "parallel imports" and "compulsory licensing."

Parallel importation is the importation of drugs from another country where they are sold at a lower price to meet a public health crisis. It can take place if there are no manufacturers in the country facing the public health crisis and the pharma company that holds the patent for the drug is unwilling to price it affordably for the sake of the ailing public.

Compulsory licensing(read along with material given above) allows a government to temporarily override a patent. Government may issue a compulsory license to a company to produce generics when faced with a public health problem. This allows generic copies of a patented product to be produced domestically, with compensation paid to the patent holder.

Generic copies of patented drugs are much cheaper than the branded drugs. By introducing generics, governments can bring down the price of a certain medicine, thereby ensuring an adequate, affordable stock of the essential drugs. (Generic drugs are unbranded drugs with the same chemical ingredients of a the branded drug)

The compulsory licensing provision arms the government with the power to ensure that medicines are available to patients at affordable rates and has so far been used in Brazil, Thailand and South Africa.

It gives the government the right to allow a generic drug maker to sell cheap but safe versions of patented drugs under certain conditions, without the consent of the patent owner. Multinational drug companies had demanded strong safeguards against the liberal use of the provision when India's patent law was being framed, but the final legislation had kept the grounds for invoking this provision open-ended.

One important positive consequence of the order may be that MNCs may adopt multiple/dual pricing- selling drugs cheap relatively in developing countries.

In his order, the patent controller said Natco's application met three key conditions for granting compulsory licences. First, the German firm was able to supply its drugs to only 2% of the country's patient population and did not meet the 'reasonable public criteria' requirement. That is, it did not make sufficient efforts to make the drug available to public. Second, its price was not "reasonably affordable", and third, it was imported and not manufactured in the country.

Health experts and NGOs have welcomed the order saying it would deter innovator companies from selling their drugs at exorbitant prices.

Sui generis system

TRIPS agreement provides sui generis option regarding patent laws. Sui generis means generating by itself or of itself. It is a choice given to members in the place of patents. That is, they can protect inventions either on the basis of patents or any other indigenous system (sui generis).

GATS

The General Agreement on Trade in Services (GATS) is the set of regulations that governs trade in services among the WTO countries. GATS, which is one of the three agreements along with AoA and agreement on TRIPS was adopted in 1995 and details are being worked out since then .. GATS rules cover a broad range of economic activity such as health care, education, telecommunications, banking, insurance, business process offshoring (BPO), tourism and so on. India is interested in these fields due to its core competence.
With GATS, multilateral trading system extends to services for the first time. GATT, its predecessor did not cover services.

In services, members of the WTO offer one another most favoured nation (MFN) status as they do for physical goods. MFN means grant of non-discriminatory trade- normal trade.
GATS includes direct foreign investment in services. Liberalisation means national treatment to foreign investor; ending public monopolies, as well as deregulation whenever a regulation is considered restrictive for foreign investors and service providers.

GATS negotiations are conducted among members bilaterally on the basis of requests and offers.Requests can be made by any WTO member in any service sector to any member. Each member makes bilateral requests to its major trading partners covering sectors with export interest. These requests ask for full market access and national treatment commitments. National treatment requires that foreign investor should be offered the same terms as the local one.

The GATS agreement covers four modes of supply for the delivery of services in international trade:

	Criteria	Supplier Presence
Mode 1: Cross-border supply	Service delivered within the territory of the Member, from the territory of another Member	Service supplier not present within the territory of the member
Mode 2: Consumption abroad	Service delivered outside the territory of the Member, in the territory of another Member, to a service consumer of the Member eg:-Tourism	
Mode 3: Commercial presence	Service delivered within the territory of the Member, through the commercial presence of the supplier	Service supplier present within the territory of the Member
Mode 4: Presence of a natural person	Service delivered within the territory of the Member, with supplier present as a natural person	
	→Professionals. (like IT engg of India in Qatar) • A not migrants	

Trade negotiations

While WB and IMF operate on weighted voting basis, WTO decisions, such as adopting agreements (and revisions to them) are officially determined by consensus of all members. The advantage of consensus decision-making is that it encourages efforts to find the most widely acceptable decision. Small countries and low income countries also weigh for as much as rich countries.

In reality, WTO negotiations proceed not by consensus of all members, but by a process of informal negotiations between small groups of countries. Such negotiations are often called "Green Room" negotiations (after the colour of the WTO Director-General's Office in Geneva), or "Mini-Ministerials", when they occur in other countries.

Doha Round

Doha Round of Trade talks under the WTO began in 2001 in Doha, the capital of Qatar. Doha was the fourth ministerial after the WTO came into force- Singapore, Geneva, Seattle and Doha. It is called Doha Round because the talks were started in Doha. It is called Doha Development Round as it promised to address the issues that were important to the developing countries like India. It has lasted the longest and is yet to complete(2014).

The criticism is that since the developing countries believed that they received a raw deal under the Marrakesh Treaty in matters related to agriculture, patents and so on, they needed additional inducements to agree to the new round of talks..Thus, naming the Round as a Development Round was to pacify the developing countries.

Inducement → A thing that persuade someone to do something

Doha Round aims at further liberalizing international trade for agriculture, industry and services. The need for expeditious completion of the round is because trade as an engine of growth is needed ever more in the present world when global recession has reduced incomes of hundreds of millions of people due to collapse of demand. Also, protectionism is being chosen as a politically convenient strategy by countries including USA. It is a threat to globalization of trade and hurts all members.

Bali package (ahead)

Q: Trade as an engine of growth. What steps govt has taken?

Q: Integration of Europe is political project. Examine critically

Q Protectionism.

Q competition policy

WTO and GATT-II

Bali package

The **Bali Package** is a trade agreement resulting from the Ninth Ministerial Conference of the World Trade Organization in Bali, Indonesia on 3–7 December 2013. It is aimed at lowering global trade barriers. The package forms part of the Doha Development Round, which started in 2001.

The package includes provisions for lowering import tariffs and agricultural subsidies, with the intention of making it easier for developing countries to trade with the developed world in global markets. Another important target is reforming customs bureaucracies and formalities to facilitate trade.

The Bali package consists of ten separate decisions by the Ministerial Conference, covering four areas as follow:

Trade Facilitation

Agreement on Trade Facilitation will reduce red-tape and streamline customs. It will be legally binding, require some expense and a certain level of technology. LDCs will be supported in building capacities to implement the changes. Although, some critics worry governments may have to prioritize funds for trade facilitation over other important areas such as public health or education.

Agriculture: Covers food security in developing countries.

Development and LDC issues: Covers measures Least developed countries (LDCs) and developing countries, including preferential treatment and market access.

Before the agreement, the negotiations repeatedly came close to collapsing. India's demand that it should be allowed to extend its domestic agricultural subsidies indefinitely was met by opposition from the U.S. Eventually, India and the U.S. reached a compromise where a permanent solution to the Indian subsidies will be decided in separate future negotiations within four years.

This was the first global agreement by the WTO.

India and the Bali Package

India had not yielded on the food security issue in the WTO Bali ministerial and, in fact, secured some concessions on the trade facilitation agreement (TFA).

The Bali draft says that till a permanent solution is reached (on the question of issues of asymmetry in the Agreement on Agriculture), members would refrain from approaching the dispute-settlement body against breach of the 10% cap on price-support based food subsidy: peace clause till 2015.

India has also been able to extract a transition period for implementation of certain trade facilitation provisions.

As per the trade facilitation pact, India and developing countries had agreed to improve infrastructure at ports, put in place systems to facilitate faster custom clearances and invest in automation, computerisation and homogenous documentation to facilitate faster movement of goods.

India needs better trade facilitation to increase its share to a more respectable level. But developed countries controlling more than 80% of world trade needed this agreement more than us.

India's objections to amber box provisions and the way they are counted are the following

a. India is not a sizeable global trader in grain and so can not distort market ← Not a major exporter/importer of grains
b. 86-88 as the base year for external reference price is unfair

Trade facilitation

Trade facilitation looks at how procedures and controls governing the movement of goods across national borders can be improved to reduce associated cost burdens and maximise efficiency while safeguarding legitimate regulatory objectives. Trade facilitation as "the simplification, standardization and harmonisation of procedures and associated information flows required to move goods from seller to buyer and to make payment".

Occasionally, the term trade facilitation is extended to address a wider agenda in economic development and trade to include: the improvement of transport infrastructure, the modernization of customs administration etc.
Some examples:

Fiscal: Collection of customs duties, excise duties and other indirect taxes; payment mechanisms

Safety and security: vehicle checks; immigration and visa formalities

Environment and health: Phytosanitary, veterinary and hygiene controls; health and safety measures;

Consumer protection: Product testing; labelling; conformity checks with marketing standards (e.g. fruit and vegetables)

Trade policy: Administration of quota restrictions
Some organisations promoting trade facilitation emphasis the cutting of red tape in international trade as their main objective. Propagated ideas and concepts to reforming trade and customs procedures generally resonate around the following themes:

- Simple rules and procedures
- Avoidance of duplication
- Alignment of procedures and adherence to international conventions
- Transparent rules and procedures
- Mechanisms for corrections and appeals
- Fair and consistent enforcement
- Time-release measures
- Standardisation of documents and electronic data requirements
- Automation
- International electronic exchange of trade data
- Single Window System

Nama and India

Non-Agricultural Market Access

Introduction:

Non Agricultural Market Access (NAMA) relates to trade negotiations on non-agricultural or industrial products. In the NAMA negotiations, WTO Members discuss the terms or modalities for reducing or eliminating customs tariff and non tariff barriers on trade in industrial products.

The product coverage under NAMA includes marine products, chemicals, rubber products, wood products, textiles and clothing, leather, ceramics, glassware, engineering products, electronics, automobiles, instruments, sports goods and toys.

On tariffs, the negotiations take place on the bound tariff which are the bindings taken during the negotiations at the WTO. The bound tariffs are the upper limit of the applied customs tariff which are the tariffs actually applied by the Customs authorities on imports into any country. They can not be breached.

In the NAMA negotiations there are tariffs on which no bindings have been taken and these are known as the unbound tariff lines.

Elements of NAMA Negotiations:

The main elements of the NAMA negotiations are:

(i) Coefficient for the tariff reduction formula: how should the tariffs be reduced by the poor and the rich countries.
(ii) Flexibilities for protecting sensitive NAMA products
(iii) Sectoral initiatives for elimination of customs tariff in specific sectors
(iv) Non Tariff Barrier (NTB)

The deadlock on NAMA negotiations centres around how much tariff cut should be made; what formula should be sued; and whether north and south countries should be treated alike. However, here too the developed and developing countries are divided

Swiss formula and India

Tariff cut formulae are either linear or non-linear. In a linear formula, tariffs are reduced by the same percentage, irrespective of how high the initial tariff is. As opposed to a linear formula, in a non-linear formula, tariff cuts are directly or inversely proportional to the initial tariff rate,

Swiss formula is a non-linear formula. In the Swiss formula, tariff cuts are proportionally higher for tariffs which are initially higher. For instance, a country which has an initial tariff of 30% on a product will have to undertake proportionally higher cuts than a country which has an initial tariff of 20% on the same product.

India's average tariffs are much higher than those existing in the developed countries. If a linear formula for tariff reduction was used, then its reduction burden would have been proportional to that of developed countries. However, using a Swiss formula could lead to India taking on a greater reduction commitment than its developed counterparts with lower initial tariffs.

Nama 11 is a coalition of strong developing countries (including Argentina, Brazil, Egypt, Venezuela and the Philippines). They are fighting to get a fair deal from the north countries. India is a member.

Developing countries' demands and concerns

Developing countries like India, Brazil, South Africa etc want the US to slash its agricultural export and domestic subsidies and the EU to reduce tariffs on agricultural goods so that international market is relatively free of distortion and allows fair competition.

Developed countries demands

The rich countries(North) want the developing countries to open up the domestic markets for the manufactured goods- called Non-Agricultural Goods Market Access(NAMA) which the poor countries are resisting partly because it hurts the domestic industry at this stage and partly to use it as a bargaining lever for reforms expected of the rich countries in agriculture. Agriculture is associated with food security, livelihood security and holds key to self-reliance in these countries.

Rich countries also want liberalization of the services sector in the fields of education, legal advice and insurance.

US and EU consider access to rapidly developing economies as vital to their own growth. The negotiations are not yielding results as the poor countries are not responding to the demands on NAMA positively till their concerns on agricultural subsidy and tariff cut were met. Both the Cancun and Hong Kong Ministerial Meets broke down on this issue.

MFN

The principle of the MFN treatment means that the tariff policy that one country receives in an organization should be extended to all others. Some members may form a preferential trading block within the larger body but all others should atleast receive normal treatment. Contrary to the popular view, the MFN does not mean giving special treatment to imports from another country. It only means normal trading relation- neither positive nor negative discrimination. MFN treatment is not limited to tariffs. It extends on all matters like quotas and other rules related foreign trade.

The members of the World Trade Organization, which also include all developed nations, accord MFN status to each other.

What are the benefits

- It provides level playing field among countries which is the essence of multilateralism
- A country can import from the most efficient source. This may not be the case if tariffs differ by country.
- Same tariffs being given to all countries will lead to customs rule simplification
- Domestic companies can not lobby for protectionist measures as the government is committed to MFN tariffs with all countries.

WTO allows departures from the MFN principle.

- imports from poor countries are allowed at lower/zero tariffs(Generalised System of Preferences (GSP)
- preferential and free trade arrangement among countries of a region and others are allowed- at concessional and free rates respectively
- Article XXIV of the GATT allows Pakistan and India to depart from particular provisions of the Agreement in their bilateral relations pending the establishment of trade ties between them on a definitive basis. It is under this clause that Pakistan has not given MFN status to India, though the latter has extended such status to the former.

Regional Trading Arrangement (RTA) and Multilateralism under WTO

Conceptually, PTA/FTAs should be understood in the context of economic integration among countries- usually in a geographical region.

Preferential Trade Arrangement is the first step towards integration wherein the members agree to trade with one another at a concessional tariff. The same concessional tariff is denied to non-members.

The next step is duty-free trade and elimination of quotas. It is called FTA.

The customs union is a form of economic integration involving two or more sovereign states that stipulates that there be free trade between the member states and a common tariff policy on trade with non-member states.

A common external tariff is the agreement between the parties of the customs union that stipulates that all member states maintain the same tariffs, import quotas, non-tariff trade barriers and preferential policies towards non-member states. This prevents the practice of re-exportation within the customs union, which occurs if one member charges lower tariffs to attract foreign imports, and then re-exports those products to other members of the customs union for a profit under the internal free trade policy. The common external tariff is also useful in that it allows the members of the customs union to combine their economic power in enacting punitive or favorable tariffs towards non-member states.

The most important advantage to forming a customs union is that it represents an important step in the process of economic integration. In today's globalized economy, economic integration is more important than ever, as advancements in transportation technology have made international trade increasingly viable, and economic interdependency has emerged as a tool to facilitate cooperation and conflict resolution.

Later comes common market where there is a free movement of labour, capital, goods and services.

If the common market has the same currency, it is called a monetary union.
The last stage is the economic union in which members have a common currency and fiscal and monetary policies. Presently, the EU is the only example of an monetary and economic union.

As mentioned above, RTAs are allowed under the WTO. Some countries grant themselves concessions in regional and extra-regional trade that other members of the WTO are denied and given only MFN. Benefits are many

- tariffs being a barrier to trade, reducing and removing them boosts trade
- complementarities are established among the regional members
- trade creation is another argument- that is, due to free trade among members more trade is created
- higher production and greater efficiency due to enhanced competition
- free trade within a region is a beginning towards globalization as it prepares the countries to face global competition and secure benefits
- in fact. FTAs catalyse globalization as the benefits at the regional level will accelerate the pace towards a larger scale

- non-economic factors are another major incentive as more peaceful relations among the regional countries will have a a virtuous effect.

The following are the problems

- Trade diversion takes place. It means trade is not created but is merely diverted. Imports are made from the FTA member due to price advantage ,even if a non-member is more efficient
- Also, these arrangements have other undesirable fallout like loss of revenue due to tariff reduction or removal and

Regional economic integration without prejudicing globalization and multilateralism is carried forward with `open regionalism'."Open regionalism" is defined as external liberalization by trade blocs(PTAs and FTAs) that is, the reduction in barriers on imports from non-member countries that is undertaken when member countries liberalize the trade among themselves. Even as tariffs are reduced for the non-member countries, the level of reduction need not be the same as it is among the member countries.

Regionalism and Multilateralism

While the regional trade blocs erode the MFN principle , the following arguments are advanced to show that they promote globalization

- regional free trade is easier to implement in comparison to globalization as the latter is difficult to accept by the people of the country
- domestic lobbies for protectionism can be resisted more successfully by the government at the regional level initially and later at the global level
- scope for deeper integration at the regional level- not only trade but also comprehensive economic cooperation(investment, collaborations etc)
- open regionalism is a step towards making regional trade blocs global.

Some regional trading arrangements in force and in negotiations :

- The **Transatlantic Trade and Investment Partnership** (also known as the Transatlantic Free Trade Area) is a proposed free-trade agreementbetween the European Union and the United States. The deal is estimated to boost the EU's economy by €120 billion, the US economy by €90 billion and the rest of the world by €100 billion. Talks began in July 2013 and may be finalized by the end of 2014.
- **Regional Comprehensive Economic Partnership (RCEP)** is a Free Trade Agreement (FTA) scheme of the 10 ASEAN Member States and its FTA Partners (Australia, China, India, Japan, Korea and New Zealand) to be concluded by the end of 2015 includes more than 3 billion people, has a combined GDP of about $17 trillion, and accounts for about 40 percent of world trade. First mooted during the 2011 ASEAN Summit in Indonesia, the RCEP negotiation process was formally launched during the 2012 ASEAN Summit in Cambodia.
- **Trans-Pacific Partnership(TPP)** is a proposed trade agreement under negotiation Australia, Brunei,Chile, Canada, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, and Vietnam. The TPP is intended to be a "high-standard" agreement aimed at emerging trade issues in the 21st century.
- ASEAN Free Trade Area (AFTA) with Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand, Cambodia, Laos, Myanmar, Vietnam.
- European Free Trade Association (EFTA) between Iceland, Norway, Switzerland and Liechtenstein
- North American Free Trade Agreement (NAFTA) between Canada, U.S. and Mexico

- South Asia Free Trade Agreement (SAFTA) between India, Pakistan, Nepal, Sri Lanka, Bangladesh, Bhutan and the Maldives
- Mercosur is a Regional Trade Agreement (RTA) between Brazil, Argentina, Uruguay and Paraguay, founded in 1991 by the Treaty of Asunción, which was later amended and updated by the 1994 Treaty of Ouro Preto. Its purpose is to promote free trade and the fluid movement of goods, peoples, and currency
- The Andean Community of Nations (CAN) is a trade bloc comprising the South American countries like of Bolivia, Colombia, Ecuador and Peru. Its headquarters are located in Lima, Peru.
- The Economic Community of West African States (ECOWAS) is a regional group initially of sixteen countries, founded in 1975 on the basis of Treaty of Lagos.
- The Southern African Development Community (SADC) seeks to further socio-economic cooperation and integration as well as political and security cooperation among 14 southern African countries.

Groups

G-4 -- the United States, the European Union, Brazil and India. It has developing and the developed world.

G-10 are major food-importing economies like Japan, South Korea, Taiwan, Norway, Switzerland Israel etc. It has rich and poor representatives (Bulgaria etc)

Group of 20 (also called **G20+**) is a bloc of developing nations established in the 5th Ministerial WTO conference, held in Cancun. It stands for drastic reduction in agricultural subsidies by industrialized nations and opposed liberalization like Singapore issues and NAMA. The G-20 accounts for 60% of the world population, 70% of its farmers and 26% of world's agricultural exports

G-33 comprises developing countries like India, Indonesia etc with defensive farm interests that involves protecting farmers from imports. It is an alliance of developing countries on Special Products (SP) and Special Safeguard Mechanism (SSM) in the ongoing agriculture negotiations. It has 42 members including India , Indonesia etc .They are net-food importing developing countries.

While G-20 consists of developing countries with exporting interests as well as defensive interests, the G-33 includes only those developing countries with defensive interest in agriculture.

G-90 is the group of Least developed countries (LDCs) along with other countries from Africa, the Caribbean and Pacific formed G-90 during the Cancun conference in 2003.

WTO Words

- ACP countries - About 70 African, Caribbean and Pacific (developing) countries that have preferential access to the EU market.
- AMS – Aggregate Measurement of Support shows the extent of support- provided by governments to the agricultural sector, including direct payments to farmers and intervention in the market, e.g. through setting minimum prices. There are limits set on AMS under the AOA of WTO.
- Agreement on Agriculture - the first multilateral framework for the long-term reform of agricultural trade, through the creation of specific rules and commitments

for international and domestic agricultural activities, e.g. tariffs, export subsidies and domestic support.

- Amber box - trade and production-distorting policies. They are subject to reduction commitments (AMS).
- Anti-dumping duties – special import duties imposed when a firm, following an enquiry, is assessed as having sold a product in the importing market at a price below the one it charges in the home market or below the cost of production or at less than fair value; and it damages the producers in the importing country
- Blue box – Trade-distorting direct payments to farmers combined with production-limiting programmes, e.g. programmes requiring land to be "set-aside" from production. Blue box support is not subject to reduction commitments in the Uruguay Round. .
- Cairns Group – A group formed in 1986, comprising 17 WTO members dedicated to the fundamental reform of the agricultural trading system. The Chair is Australia. Other members are New Zealand, Argentina, All but three – New Zealand, Australia and Canada – are developing countries.
- Common Agricultural Policy (CAP) - the EU's internal agricultural policy, intended to provide stable agricultural markets and incomes for European farmers and food for European consumers through a system of domestic support, market access protection and export subsidies.
- Countervailing duties - special duties imposed on imports to offset the actual or potential injurious effects (i.e. price undercutting) of subsidies to producers or exporters in the country of export.
- Dumping - exporting goods at a price lower than the price a company normally charges on the domestic market. Governments in the importing country may levy anti-dumping duties, designed to offset the actual or potential injurious effects of dumping practices.
- Export Subsidies – government payments or other financial contributions provided to domestic producers or exporters if they export their goods and services (i.e. contingent on export performance).
- Government procurement – purchases by central and local governments.
- LDCs – Least Developed Countries, group defined by the United Nations on the basis of certain economic indicators. Includes 49 countries .
- Market Access - a negotiated commitment to guarantee a certain level of access in specified sectors.
- Most-Favoured Nation (MFN) – A core principle of the multilateral trading system which requires that normal trade be conducted among all members.
- Multilateral – among many parties, e.g. the WTO is a multilateral organisation involving 148 economies.
- National treatment - In services trade, a WTO member agrees in certain "committed" sectors to treat a foreign supplier no less favourably than a domestic supplier.
- Natural persons - People, as distinct from juridical persons such as companies and organisations. 'Movement of natural persons' concerns the ease of travel through and ability to live and work in other countries.
- Non-discrimination – a core principle of the multilateral trading system under the WTO. It includes most favoured nation (MFN) treatment and national treatment.

- Non-tariff barriers – government measures others than tariffs that restrict trade flows. Examples include quantitative restrictions, import licensing, standards and conformance regulations.
- Plurilateral – among several parties, e.g. the FTAA
- Round – the process of multilateral trade negotiations. Each of the eight sets of negotiations prior to the Doha Development Agenda (DDA) has been called a Round, e.g. the Uruguay Round, the Tokyo Round.
- Rules of origin – the production and content criteria defining where a good comes from. For example, among the FTA countries, any country can import from non-member countries but has to add a minimum value of about 30% or so before it can be traded within the FTA region.
- Safeguard action - temporary measures to allow countries to adjust to heightened competition from foreign suppliers, even where the competition is not a result of dumped or subsidised product.
- S&D – the "special and differential treatment", i.e. flexibility, given to developing countries in implementing WTO commitments, allowing longer phase-in times and addressing concerns such as food security and rural development.
- SPS – Sanitary and Phytosanitary agreement within the WTO dealing with trade affecting human, animal and plant health and life.
- Tariff escalation - tariff rates that increase with each additional level of processing, thus penalising value-added products, as is often the case with our wood exports.
- Tariff peaks – tariffs on particular products that are significantly higher that the typical tariff that the country in question levies on the full range of imports.
- Tariff rate quotas - allow a certain volume of product access at a lower tariff level. A higher tariff is charged on products imported outside the tariff quota.
- Three pillars - Market access, export competition and domestic support are the three pillars of the Agreement on Agriculture.

G33 and SP and SSM

G-33 is an alliance of developing countries on Special Products (SP) and Special Safeguard Mechanism (SSM) in the ongoing agriculture negotiations in the World Trade Organisation (WTO).

The WTO Framework Agreement of 2004 – also known as the July Framework – which laid down the parameters for further negotiations in the Doha Round, contained two major elements of interest to developing countries in the area of agricultural market access

It provided that developing countries would be eligible to designate an appropriate number of products as Special Products, based on their food and livelihood security or rural development needs; and

It also provided for the use of a Special Safeguard Mechanism against surge in imports so as to safeguard domestic producers of agricultural products in developing countries.

WTO and safeguard duty

In the technical language of the World Trade Organization (WTO) system, a **safeguard** is used to restrain international trade in order to protect a certain home industry from foreign competition. A member may take a "safeguard" action (i.e., restrict importation of a product temporarily) to protect a specific domestic industry from an increase in imports of any

product which is causing, or which is threatening to cause, serious injury to the domestic industry that produces like or directly-competitive products.
Safeguards are usually seen as responses to fair trade behaviour, as opposed to unfair trade practices such as

- Dumping
- Subsidy that attracts countervailing duty

As such they are supposed to be used only in very specific circumstances, with compensation, and on a universal basis, i.e., a member restricting imports for safeguard purposes will have to restrict imports from all other countries.

Special Products and Special Safeguard Mechanisms
Special Products (SP) and Special Safeguard Mechanisms (SSM) are key concerns of developing nations involved in WTO negotiations. By using SP and SSM, these nations hope to ensure food security and protect small farmers and the rest of the poor from the vagaries and pressures of international trade in agriculture commodities.

Special Products (SPs)
Special Products (SPs) are agricultural products of particular importance to farming communities in developing countries for reasons of food security, livelihood security and rural development.

It was decided at the Doha Development Round of WTO negotiations that SPs would attract lower levels of tariff reduction commitment than other agricultural products. The rationale is that higher levels of protection on SP will allow developing countries to sustain and develop domestic production of these products, thereby allowing them to protect and enhance livelihoods and food security in their domestic agriculture.

SP is a component of the WTO's Special and Differential (S&D) provision and is available only to developing country members of the WTO.

The Doha Ministerial Declaration recognised the non-trade concerns of developing countries and explicitly mentioned that the Doha Development Round of trade talks would include concessions that will "enable developing countries to effectively take account of their development needs, including food security and rural development".

Since the introduction of the concept of SP, discussions are going on about their selection and treatment. Essentially, the discussion centres on two issues:

- The number of products to be given SP status.
- The modalities to select SPs.

Special Safeguard Mechanisms (SSMs)
Special Safeguard Mechanisms or SSMs are a set of provisions through which a WTO member country can temporarily impose higher than bound tariff rates on the import of a particular agricultural product if there is a sudden surge in imports of that product into the country. The SSM provisions will be available to all developing and least developed country members of the WTO.

SSM is a trade defence mechanism to essentially counter the volatility of international commodity prices. Sudden and sharp declines in the international price of an agricultural commodity could lead to an import surge which, in turn, could damage the viability of

domestic production. Even with the available headroom between bound and applied tariff rates, countries may find it difficult to check these surges. In these cases, a temporary measure like SSM will allow developing countries to tide over crises. SSM will allow countries to raise tariffs above their bound levels for a limited duration.

The Hong Kong Ministerial text allows developing countries the right to impose SSMs based on both price and volume triggers. This means that developing countries will have the option of temporarily imposing higher tariff rates on the import of an agricultural product if there is either a surge in its import volume or a sharp dip in its import price. However, the exact mechanisms of the implementation of SSMs have not been spelt out.

To conclude, Special Products and Special Safeguards Mechanisms together can provide a reasonable level of protection to the agriculture sector of developing countries.

Safeguard Duty (For non agricultural products also) (compensation)
When imports of a particular product, as a result of tariff concessions or other WTO obligations undertaken by the importing country, increase unexpectedly to a point that they cause or threaten to cause serious injury to domestic producers of like or directly competitive products, a safeguard which is a form of temporary relief is used. Safeguards give domestic producers a period of grace to become more competitive vis-à-vis imports.

If this happens, the government of the importing country may suspend the concession or obligation, but will be expected to provide compensation by offering some other concession. Otherwise, the affected WTO member(s) can retaliate by withdrawing equivalent concessions. Safeguards usually take the form of increased duties to higher than bound rate or standard rates or quantitative restrictions on imports.

Safeguard duty in India
The Central Government after conducting an enquiry is satisfied that any article is imported into the country in such increased quantities and under such conditions so as to cause or threatening to cause serious injury to domestic industry, then it may by notification impose a safeguard duty on that article.

Faced with complaints from domestic manufacturers of a surge in import of caustic soda, a chemical used as a base for making products such as paper, textiles, soap and detergents, India has initiated investigations for imposing a safeguard duty on it.

The investigation has been initiated by the directorate general of safeguards (DGS following a complaint. The imports have come mostly from China, Qatar, Thailand and Saudi Arabia.

Special safeguard mechanism and safe guard duty: differences
Safeguards are contingency restrictions on imports taken temporarily to deal with special circumstances such as a sudden surge in imports or depressed prices. The special safeguards provisions for agriculture differ from normal safeguards. In agriculture, unlike with normal safeguards:

- higher safeguards duties can be triggered automatically when import volumes rise above a certain level, or if prices fall below a certain level; and
- it is not necessary to demonstrate that serious injury is being caused to the domestic producer.

Contingency – A possible but unpredectible future event

Special and differential treatment

The principle of special and differential treatment for addressing the concerns of developing countries is incorporated through a number of provisions in the area of market access including, proportionately lower tariff reductions and longer implementation periods, working out a tariff reduction formula after taking into account the different tariff structures of developed and developing countries as well as the new instruments of SP and SSM.

The Ministers are expected to discuss suggestions on SP and SSM in the WTO so that the sensitivities of various members of G-33 could be factored in the first approximation expected in July and also later in the Ministerial Declaration in Hong Kong.

What has India gained from the WTO?

- MFN status in the 159 member body
- Rule based trading system
- Impartial trade dispute settlement process unlike earlier when there was bilateral pressures and threats to fall in line(Super and Special 301 of the USA)
- Definitive schedule for trade liberalization with special protection so as to calibrate alignment with global economy
- Opportunity to throw up MNCs in the pharma sector
- Opportunity to step up agri exports as Indian agricultural reforms yield results and USA and EU reduce their subsidies

The adverse effect is in the from of uncertainties in the age of globalization; drug prices of some products going up due to product patents; farmers feeling the pressure of open trade etc.

WTO: Boon or bane

WTO liberalises International trade and steps up the total output which in turn promotes standards of living for all participants sooner or later. However, the exact impact differs from country to country- the rich benefiting sooner and more substantially than the poor , in general.

There are many benefits to India from its membership of the WTO

- The globalization process that WTO ensures is the course chosen by India as a part of the economic reforms launched in 1991.
- It is a multilateral trade body with 153 members and so can set the pace for globalization to benefit all
- Most Favoured Nation(MFN) treatment is given to all members within the body by one another. MFN essentially means normal trade among member countries.
- The one country one vote system of decision making makes WTO a democratic body where rich do not command greater voting weightage
- Dispute settlement process is rule based and transparent
- India has advantage in the services sector and will benefit from its opening up
- Lower tariffs, introduced gradually and the right pace, will make Indian economy competitive
- Reduction of subsidies on agriculture by the developed countries will help India tap its agricultural potential to capture global markets

The opponents argue the following

- While globalization is welcome, its pace must be set by the sovereign government
- The agreement on TRIPS works against affordable medicines

- Multinational corporations influence the agreements and their working in WTO to their advantage
- Farmers may lose their livelihood as agriculture is compulsorily thrown open to imports at lower import duties
- Rich countries are not following their treaty obligations and reduce agricultural subsidies and tariffs
- The dispute settlement process gives the impression of being fair and transparent but works against poor countries as there is no way of enforcing the verdict of the dispute settlement body.

TBT and SPS

The Agreement on Technical Barriers to Trade --- commonly referred to as the TBT Agreement --- is an international treaty administered by the World Trade Organization.
TBT exists to ensure that technical regulations, standards, testing, and certification procedures do not create unnecessary obstacles to trade. The agreement prohibits technical requirements created in order to limit trade, as opposed to technical requirements created for legitimate purposes such as consumer or environmental protection.

The TBT agreement is closely linked to the Agreement on the Application of Sanitary and Phytosanitary Measures.

The Agreement on the Application of Sanitary and Phytosanitary Measures - also known as the SPS Agreement is an international treaty of the World Trade Organization.

Under the SPS agreement, the WTO sets constraints on member-states' policies relating to food safety (bacterial contaminants, pesticides, inspection and labelling) as well as animal and plant health (phytosanitary) about imported pests and diseases.

For example, Indian measures against imports of toys from China on safety considerations (first the ban and then its revision to new mandatory safety standards).

Singapore Issues

The first ministerial conference was held in Singapore in 1996. Rich countries introduced four issues that came to be known as the "Singapore issues"

- Investment by foreign companies on same terms as national companies
- Competition laws that deal with monopolies and cartels , price fixing, mergers etc
- Transparency in government procurement and creating a level playing field for all players- domestic and foreign
- trade facilitation: standardization and simplification of customs procedures

The four issues have been controversial. Poor countries do not allow them to be brought into the agendas they feel that they might damage their economic interests. In Cancun Ministerial, trade facilitation is admitted by consensus as it has only procedural implications.
The opposition of the poor countries rests on the following grounds.

- Doha agenda should not be overloaded and the existing issues need to be implemented first like cutting agricultural subsidies.
- large, multinational corporations dominate and threaten the young and growing domestic firms
- they are too intrusive

- policy should be the prerogative of the government . It should be made at its own discretion because such policy depends on a country's unique market conditions

The common theme of three of the issues (investment, competition, government procurement) is to maximise the rights of foreign enterprises to have market access to developing countries through their products and investment; to reduce to a minimum the rights of the host government to regulate foreign investors; and to prohibit government from measures that support or encourage local enterprises.
U.S. and the E.U support the introduction of the Singapore issues arguing that unfair competition/investment and procurement policies distort trade as much as tariffs do, and therefore should be regulated by the WTO rather than left up to individual country governments. However, the US and other developed nations should first implement their commitments in agriculture before expanding the agenda.

H1B Visa Fee Hike and WTO-Compatibility

The recent - Border Security Act – of US earmarks funds from the visa fee hike to pay for the US government's plans to boost security along its border with Mexico to crack down on illegal immigration and drug smuggling.

The visa fee hike "is WTO incompatible and India is considering challenging the US legislation before the World Trade Organisation.

The 600-million-dollar measure, will nearly double visa fees for some Indian information technology workers entering the United States.

The National Association of Software and Services Companies (NASSCOM), which represents India's top software exporters, has said the measure will increase annual US visa costs for the sector by 200-250 million dollars.

The US legislation affects those skilled workers brought in by companies whose employees are more than 50 per cent foreign, a move that largely affects India's IT and outsourcing industries.

US high-tech firms such as Microsoft, which bring skilled immigrants into the United States on the same visas, will not be hit because the vast majority of their workforce is American.
More than half of the world's top 500 companies outsource work to India, which has become the world's back office where Western firms have set up call centres and number-crunching and software development outlets to cut costs.

But the industry also flies employees to the US each year to work at their clients' locations as on-site technicians and engineers.

Under the law, fees for non-immigrant 'H1B' and 'L' visas go up by 2,000 dollars for firms with more than a 50 per cent non-American workforce. The fee now is 2,500 dollars.

Anti-outsourcing sentiment in the United States has been stoked by high unemployment.

US Cotton Subsidies

American subsidies to the cotton growers makes US cotton so cheap that it hurts other countries producing cotton. It distorts international trade. Brazil dragged the USA to WTO on this score and had an important victory in 2009 August. Brazil was allowed to slap sanctions on US goods and drugs upto $300million annually.

Protectionism

Protectionism is the economic policy of restricting trade and economic relations between countries , through methods such as tariffs on imported goods, restrictive quotas, and a variety of other restrictive government regulations designed to discourage imports, and prevent foreign participation in local markets and companies. This policy is closely aligned with anti-globalization, and contrasts with free trade, where government barriers to trade are kept to a minimum. Protectionism refers to policies or doctrines which "protect" businesses and workers within a country by restricting or regulating trade with foreign nations.

Historically, protectionism was associated with import substitution. Contemporary economists agree that protectionism is harmful in that its costs outweigh the benefits, and that it impedes economic growth. Recent examples of protectionism in first world countries are typically motivated by the desire to protect the livelihoods of individuals in politically important domestic industries. US stimulus package encourages `buy American ' philosophy. Whereas formerly blue-collar jobs were being lost to foreign competition, in recent years there has been a renewed discussion of protectionism due to offshore outsourcing and the loss of white-collar jobs. However, most economists agree that the benefits from free trade in the form of consumer surplus and increased efficiency outweigh the losses of jobs.

Instruments of protectionism

A variety of policies can be used to achieve protectionist goals. These include:

- Tariffs: Typically, tariffs (or taxes) are imposed on imported goods. Tariff rates usually vary according to the type of goods imported. Import tariffs will increase the cost to importers, and increase the price of imported goods in the local markets, thus lowering the quantity of goods imported. Tariffs may also be imposed on exports.
- Import quotas: To reduce the quantity and thus protect the domestic producers. The economic effects of an import quota is similar to that of a tariff more or less.
- Administrative Barriers: Countries are sometimes accused of using their various administrative rules (eg. regarding food safety, environmental standards etc.) as a way to introduce barriers to imports.
- Anti-dumping legislation: Supporters of anti-dumping laws argue that they prevent "dumping" of cheaper foreign goods that would cause local firms to close down. However, in practice, anti-dumping laws are usually used to impose trade tariffs on foreign exporters.
- Direct Subsidies: Government subsidies (in the form of lump-sum payments or cheap loans) are sometimes given to local firms that cannot compete well against foreign imports. These subsidies aim to "protect" local jobs, and to help local firms adjust to the world markets.
- Export Subsidies: Export subsidies are often used by governments to increase exports. Export subsidies are the opposite of export tariffs, exporters are paid a percentage of the value of their exports. Export subsidies increase the amount of trade and help the local producers.
- Exchange Rate manipulation: A government may intervene in the foreign exchange market to lower the value of its currency by selling its currency in the foreign

exchange market. Doing so will raise the cost of imports and lower the cost of exports, leading to an improvement in its trade balance. However, such a policy is only effective in the short run, as it will most likely lead to inflation in the country, which will in turn raise the cost of exports, and reduce the relative price of imports.

Other initiatives besides tariffs have also been cited as protectionist. For example, some commentators, such as Jagdish Bhagwati, see developed countries efforts in imposing their own labor or environmental standards as protectionism. Also, the imposition of restrictive certification procedures on imports are seen in this light.
Further, others point out that free trade agreements often have protectionist provisions such as intellectual property, copyright, and patent restrictions that benefit large corporations.
There are three types of protectionism:

- help protect infant industries as India followed them in the pre-reform period. It allows domestic industries to grow and become strong before they are opened up for competition
- protectionism for public interest and social good like SP and SSM mechanisms under WTO
- the third variety is when the economy is in crisis and politically it becomes necessary to close the economy for imports to save jobs. For example, may countries in the global recession (2008-09). These are temporary measures lasting till the crisis lasts.

Arguments against Protectionism
Protectionism is frequently criticized as harming the people it is meant to help. Free trade helps all including third world economies and workers. This is because "the growth of manufacturing has a ripple effect throughout the international economy" and creates competition among producers, lifting wages and living conditions. Protectionist proposals stunt economy and make it uncompetitive and so harm jobs and increase prices and lose out on innovation.

The Tragedy of the Commons
It is an influential article written by Garrett Hardin in 1968. The article describes a dilemma in which multiple individuals acting independently in their own self-interest can ultimately destroy a shared limited resource even when it is clear that it is not in anyone's long term interest for this to happen.

Beggar thy neighbour
It is a policy and means that one nation develops at the expense of others. Beggar thy neighbour, or beggar-my-neighbour policy is an attempt to remedy the economic problems in one country by means which tend to worsen the problems of other countries. The term was originally devised to characterize policies of trying to cure domestic depression and unemployment by shifting effective demand away from imports onto domestically produced goods, either through tariffs and quotas on imports, or by competitive devaluation.

Agriculture

With about 14.5% contribution at 2004-05 prices, to the gross domestic product (GDP), agriculture provides livelihood support to about two-thirds of country's population. The sector provides employment to 57% of country's work force and is the single largest private sector occupation. Agriculture accounts for about 10% of the total export earnings and provides raw material to a large number of Industries (textiles, silk, sugar, rice, flour mills, milk products). Besides, the rural areas are the biggest markets for low-priced and middle-priced consumer goods, including consumer durables. It means, if agriculture performs, rural demand is high. Rural domestic savings are an important source of resource mobilisation.

The agriculture sector is crucial in maintaining food security and, in the process, national security as well. The allied sectors like horticulture, animal husbandry, dairy and fisheries, have an important in improving the overall economic conditions and health and nutrition of the rural people. Thus, any change in this sector, positive or negative, has a multiplier effect on the entire economy. India is the world's largest producer of milk, pulses, and spices, and has the world's largest cattle herd (buffaloes), as well as the largest area under wheat, rice and cotton. It is the second largest producer of rice, wheat, cotton, sugarcane, farmed fish, sheep & goat meat, fruit, vegetables and tea.

Recognising the crucial role played by the agriculture sector in enabling the widest dispersal of economic benefits, the Eleventh Plan has emphasised that agricultural development is central to equitable and fast economic development of country.

Considerable progress has been made on this front. Foodgrains production rose from 52 million tonnes in1951-52 to 259 million tonnes in 2013-14. The share of agriculture in real GDP has fallen given its lower growth rate relative to industry and services. However, what is of concern is that growth in the agricultural sector has quite often fallen short of the Plan targets. During the period 1960-61 to 2010-11, food grains production grew at a compounded annual growth rate (CAGR) of around 2 per cent. In fact, the Ninth and Tenth Five Year Plans witnessed agricultural sectoral growth rate of 2.44 per cent and 2.30 per cent respectively compared to 4.72 per cent during Eighth Five Year Plan. During the 11th Five Year plan, agriculture growth is estimated at 3.28 per cent against a target of 4 per cent. The Approach Paper to the Twelfth Five Year Plan emphasises the need to "redouble our efforts to ensure that 4.0 per cent average growth" is achieved during the Plan if not more.

Without incremental productivity gains and technology diffusion across regions, achieving this higher growth may not be feasible and has implications for the macroeconomic stability given the rising demand of the 1.2 billion people for food. Achieving minimum agricultural growth is a pre-requisite for inclusive growth, reduction of poverty levels, development of the rural economy and enhancing of farm incomes

Food deficit to food surplus

After remaining a food deficit country for about two decades after Independence, India has become self-sufficient in food grains.

From the mid 1960s , food security improved with the introduction of high yielding varieties (HYVs) of crops, and the development of agriculture infrastructure for irrigation, input supply, storage and marketing. The HYVs motivated farmers to adopt improved production technologies with the use of water, fertilisers and agrochemicals. Besides the public sector rural infrastructure, farmers developed their own 'onfarm' resources. The extension support for production technology and the marketing support through procurement operations encouraged farmers to step up production. The production of various crop commodities has increased substantially, over the various Plan periods.

Accounting for Success in Agriculture

The main factors for the all-round success of agriculture have been

- increase in net sown area
- expansion of irrigation facilities
- land reforms,especially consolidation of holdings
- development and introduction of high yielding seeds
- fertilizers
- improved implements and farm machines
- technology for pest management
- price policy based on MSP and procurement operations
- infrastructure for storage/cold storage
- improvements in trade system
- increase in investments, etc.

However, in spite of the spectacular achievements, various constraints and disturbing trends continue to hamper the requisite growth of the agriculture sector.

Foodgrain production 2012-13

India's foodgrains production was an all-time high of 252.56 million tonne in 2011-12.The country produced 244.78 million tonne in the previous year.

Rice production has been revised to a record 103.41 million tonne .Wheat output, too, has been pegged higher at 90.23 million tonne. However, the production figure of coarse cereals and pulses has been revised downwards to 41.91 million tonne and 17.02 million tonne, respectively.

In the 2010-11 crop year, rice production stood at 95.98 million tonne, wheat — 86.87 million tonne, pulses — 18.24 million tonne and coarse cereals — 43.68 million tonne.

Crisis and Challenge in Agriculture

One of the major challenges of the 12th Plan is to reverse the deceleration in agricultural growth from 3.2% observed between 1980 and 1996-97 to a trend average of less than 2% subsequently. This deceleration is the root cause of the problem of rural distress that has surfaced in many parts of the country- unemployment, underemployment, declining incomes, distress migration etc.

Low farm incomes due to inadequate productivity growth, high prices of inputs and lack of credit at reasonable rates pushed many farmers into crippling debt. Uncertainties have

increased- prices, quality of inputs ,weather and pests which, coupled with unavailability of proper extension and risk insurance have led farmers to despair. This has also led to widespread distress migration, a rise in the number of female headed households in rural areas and a general increase in women's work burden and vulnerability.

To reverse this trend, corrective policies are being implemented under the 11th Plan-focused not only on the small and marginal farmers who continue to deserve special attention, but also on middle and large farmers who suffer from productivity stagnation arising from a variety of constraints. Bharat Nirman with irrigation component is an example.

(w/o Big farmers investment in agriculture will drop)

It is vital to increase agricultural incomes for reasons of employment; equity; food security etc. A second green revolution is urgently needed to raise the growth rate of agricultural GDP to around 4% in an ever green way(ecologically friendly). This is not an easy task since actual growth of agricultural GDP, including forestry and fishing, was below 2% for the 10th Plan period. The challenge posed, therefore, is to at least double the rate of agricultural growth. The 12th plan Approach Paper(2012-17) targets 4% growth rate for agriculture.

Causes for low agricultural growth since mid-1990s

There are region-specific causes for the decelerating growth in the agriculture sector during the 1990s. Some of these are:

- Low public investment in irrigation.
- Poor maintenance of rural infrastructure, specially canals and roads.
- Decline in investments in rural electrification and in its availability. This has greatly affected production in eastern India, where huge groundwater potential remains untapped.
- Rising level of subsidies for power, water, fertilisers and food are eroding public sector investments in agriculture, besides encouraging inefficient use of scarce resources such as water. This further aggravates environmental problems leading to loss of soil fertility and decline in groundwater, which reduces returns on capital. Farmers then demand further subsidies to maintain the same level of production.
- Inadequate credit support till 2004
- Distortions brought in marketing mechanism
- Continuing imbalanced use of NP &K fertilisers, (6.4:2.5:1) as against the desirable norm of 4:2:1 and increasing deficiency of micro nutrients in the soil.
- Stringent controls on movement, marketing, credit, stock and export of agri-products that affect their profitability.
- Controls on the agro-processing industry.
- Poor extension service. (such as community radio, echaupal...)

Remedies

In recent years, several new initiatives have been taken which included :

- Announcement of National Policy for Farmers (2007).
- Kisan Credit Card (1998-1999).
- Creation of a Watershed Development Fund
- Bharat Nirman

- National Horticulture Mission.
- Technology Mission on Cotton (1999-2000).
- Implementation of the National Agriculture Insurance Scheme/Rashtriya Krishi Bima Yojana .
- programmes for elimination of post-harvest losses
- Lifting some of the restrictions and controls on the movement and storage and exports of foodgrains/agri produce.
- De-reservation of the manufacture of some farm implements/machines from the smallscale industries sector
- Vishesh Krishi Upaj Yojana: The objective of the scheme is to promote export of fruits, vegetables, flowers, minor forest produce, and their value added products, by incentivizing exporters of such products. Exporters of such products shall be entitled for duty rebates.

Rebate
↓
Partial argument

- AEZs
- Contract farming
- Loan waiver to revive farming
- NRAA was set up in 2006(read ahead)
- Nutrient based fertilizer subsidy (2008-09)

11th Plan and Agriculture: Some areas (2007-12)

Accelerating Agricultural Growth

The crisis of stagnation in agriculture needs urgent attention. As pointed out by the National Commission on Farmers, we need a new deal that rebuilds hope about farming by making it a viable and profit-making enterprise. This involves finding larger public resources.

Concerns

Initially, public sector investment played a crucial role in the development of infrastructure like irrigation, electricity, agriculture research, roads, markets and communications. Investment in agriculture declined in the last three five year plans This decline was due to a fall in public investment. This calls for a review of policies so that productive investment is made in capital formation. Diversion of scarce resources from creation of productive assets - rural electricity, irrigation, credit and other agricultural inputs to subsidies needs to be resisted. The declining trend in public sector investment will need to be reversed by better targeting of subsidies. Following are the concerns:

Firstly, the share of agriculture in GDP has declined from 61 per cent in 1950-51 to 17 per cent (2009), whereas the dependence of population on agriculture has declined only marginally from 3/4ths to 2/3rds during the period. In all the developed countries, there has been a major shift of population from agriculture as an occupation to other sectors. However, this has not happened in India.

Secondly, the average size of holdings has reduced from 2.28 ha in 1970-71 to less than 1 ha in 2009 with the pressure on land increasing proportionately . Small plots do not permit introduction of modern technology due to high costs.

Thirdly, during the 1990s, foodgrains production growth rate and productivity growth rate declined: the growth rate of foodgrains production declined to 1.92 per cent per annum from 3.54 per cent per annum during 1980s. Similarly the growth rate of productivity in food grains decelerated to 1.32 per cent per cent as compared to 3.33 per cent per annum during the 1980s. The per unit area productivity of our crop commodities is much lower as compared to that of the other major crop producing countries . There is also a wide gap in the yield levels among and within States.

Fourthly, during the 1990s, the policy of various States has been to increase production through subsidies on inputs such as power, water and fertilisers, rather than by building new capital assets in irrigation and power. These problems are particularly severe in the poorer states. Lower public investment and deteriorating quality of public services in agriculture are the major problems. The poor base of rural productive assets and poorer technological base because of past public/private patterns of spending has been recognised as a serious constraint in increasing production and productivity.

11th Plan strategy to raise agricultural output is based on the following elements:

- Double the rate of growth of irrigated area;
- Improve water management, rain water harvesting and watershed
- development;
- Reclaim degraded land and focus on soil quality;
- Bridge the knowledge gap through effective extension;
- Diversify into high value outputs, fruits, vegetables, flowers, herbs and
- spices, medicinal plants, bamboo, bio-diesel etc., but with adequate measures to ensure food security;
- Promote animal husbandry and fishery;
- Provide easy access to credit at affordable rates;
- Improve the incentive structure and functioning of markets;
- Refocus on land reforms issues.

Boosting agricultural productivity by making available institutional credit adequately and affordably, support for investments in land development structures, farm mechanisation, biotechnology, cold storages, value adding enterprises and marketing to improve productivity and profitability in
Agriculture is the need of the hour.

12th FYP and agriculture

The Planning Commission set annual agriculture growth target for the 12th Five Year Plan (2012-17) at 4 per cent as it was in the previous two plans.

During the 11th five year plan (2007-12) average farm growth of about 3.5 per cent was achieved ."The investment in farm research should be 2 per cent of agriculture gross domestic product (GDP) which ranges from 0.5-0.6 per cent at present.

12th Plan expressed concerns over relatively lower agriculture yields in India compared to the developed world.Production could be increased by reducing knowledge deficit.

The farm growth is crucial in the back drop of high food prices in the country. The performance of the farm sector was dismal in the previous fiscal as the growth was just 0.2 per cent against the annual average target of 4 per cent in the 11th Plan (2007-12), on account of widespread drought.

The annual average farm growth during the 10th Plan (2002-07) also missed the 4 per cent target, and grew instead at the rate of 2.13 per cent.

The annual average farm growth which was 4.72 per cent in 8th Plan (1992-97), slowed down to 2.44 in 9th Plan and further to 2.13 per cent in 10th Plan period.

Capital Formation in Indian Agriculture

Capital formation is one of the basic factors for increasing production. It means addition to the physical stock of dams, roads, power plants and other infrastructure. This is all the more important in agriculture where we are faced with the need of increasing production against vagaries of weather to keep pace with the increase in population. Judicious use of natural resources for sustainable production of agriculture, adoption of advanced technology and development of infrastructure for facilitating all agricultural activities, ensuring food security in the broader sense of making adequate nutritious food available and accessible to all and making agriculture a profitable commercial activity at par with other industries in the arena of global economy are the problems that can be successfully tackled only with a strong capital base.

It is necessary to have a broader measure of agricultural capital formation which can be called **capital formation for agriculture** in comparison with **capital formation in agriculture.** That is, rural roads, powers etc should also be considered capital formation for agricultural growth while they may not be directly related to agriculture.

As agriculture is getting diversified, there is a need to not only augment but also re-structure the pattern of investment in agriculture. Historically, the public sector has taken the lead in directing the growth and pattern of agriculture investment. Steps should be taken to improve capital formation for agriculture in both Public and Private Sectors. Otherwise, it may be difficult to sustain the agriculture growth and rural purchasing power. Currently, irrigation accounts for the bulk of public investment in agriculture (above 90%).

The new strategy of agriculture growth and diversification of agriculture from traditional crop cultivation to horticulture etc. would require more investments on cold storage, rural roads, communication, marketing network and facilities, warehouses etc.

Simultaneously efforts should be made to revitalize agriculture through introduction of bio-technology and other innovations. This would require substantial increase in investment on research & development for agriculture.

Recent steps are showing positive results: gross capital formation in agriculture as a proportion of agriculture GDP improved.

The Gross Capital Formation (GCF) in the agriculture and allied sectors in the country rose by 87 per cent to Rs 1,42,254 crore in the 2010-11 fiscal as compared to 2004-

Q:- Bharat Nirman

Q:- Suggering in investment for capital formation

Q:- Rational for agriculture diversification.

05.Capital investment in agriculture and allied sectors has witnessed a steady increasing trend in recent years. It has risen from 13.5 per cent of GDP in 2004-05 to 20.1 per cent in 2010-11.

This growth has been possible because of initiatives taken by the government to make agriculture a sustainable vocation- Bharat Nirman is responsible for the good performance. **Bharat Nirman** is the plan for creating basic rural infrastructure. It comprises projects on irrigation, roads (Pradhan Mantri Gram Sadak Yojana), housing (Indira Awaas Yojana), water supply, electrification (Rajiv Gandhi Grameen Vidyutikaran Yojana) and telecommunication connectivity..

Investment in public sector includes irrigation works, command area development, land reclamation, afforestation and development of state farms, it added.

Private sector investment includes construction activities including improvement / reclamation of land, construction of non-residential buildings, farm houses, wells and other irrigation works, it said.

The share of public investment in gross investment increased.

Reclaim → Make waste land usable

Efforts are being intensified to boost investment in agriculture .These programmes are likely to increase capital formation in agriculture by the public sector and induce the private sector to increase investment in agriculture. The improved availability of credit for agriculture and liberalized trade for agricultural products should enhance private investment in agriculture.

Government stepped up public investment significantly for rural roads and rural employment programmes. Major measures taken for agricultural development through enhanced capital formation include the following:

- A roadmap for agricultural diversification has been prepared with focus on horticulture, floriculture, animal husbandry and fisheries.
- Strengthening of agriculture marketing infrastructure.
- National scheme for the repair, renovation and restoration of water bodies.
- Focus on micro irrigation, micro finance, micro-insurance and rural credits.
- Setting up a Knowledge Centre in every village.
- Setting up a National Fund for strategic agricultural research.
- Provision of urban amenities in rural areas through creation of new growth poles
- New fertilizer subsidy regime that is nutrient based so as to fortify soil
- Bharat Nirman
- Pradhan Mantri Gram Sadak Yojana
- Loan waiver also will enable fresh investment as farmers become eligible for loans again due to write off.

Sustainable Agriculture: Water Management and Irrigation

Sustainable development of land and water resources becomes important for the nation like India, which shares about 16 per cent of the global population but has only 2.4 per cent of the total land and 4 per cent of the total water resource. Scarcity of water in rainfed areas is causing serious hardships. Ground water resources are dwindling fast due to poor water

harvesting leading to excessive run off and poor recharging of ground water. This is accompanied by excessive drawal/ exploitation mainly to meet the household needs of growing population as also irrigation needs of new high yielding crops. The number of dark blocks/mandals where there is over exploitation of groundwater (over 85 per cent) is increasing in most of the States with large rainfed areas (Andhra Pradesh, Karnataka, Rajasthan, Madhya Pradesh, Chattisgarh etc.). If this continues, the number of over exploited blocks will double over a period of every twelve and a half years.

Water is a critical input for agriculture and this calls for more effective utilization of existing irrigation potential, expansion of irrigation where it is possible at an economic cost, flood forecasting and better water management in rainfed areas where assured irrigation is not possible. The Bharat Nirman programme envisages creation of 10 million hectares additional assured irrigation during the 4 years period (2005-2009).

Along with expansion of irrigation facilities, steps need to be taken to ensure that water is distributed equitably and that it is used efficiently. The pattern observed in the past where tail-enders are denied water because upper end-users appropriate it for highly water intensive crops must be avoided. Participatory Irrigation Management (PIM) by democratically organised water user associations empowered to set water charges, collect and retain substantial part of it, would help to maintain field channels, expand irrigated area, distribute water equitably and provide the tail enders their just share of water. Experience in Andhra Pradesh and Gujarat has shown the effectiveness of such PIM.

Watershed management, rainwater harvesting and ground water recharge can help augment water availability in rainfed areas. Micro-irrigation is also important to improve water use efficiency.

Warabandi

Warabandi means fixing of turns for irrigation water for each farmer so as to make it available to its potential users, i.e. farmers. It aims at use of water judiciously and equitably.

Soil Health

Soil health is a critical factor for agricultural productivity and human health. The following steps are being taken to improve it.

Government will issue Soil Health Cards to all farmers in the country detailing the deficiencies in the soil and the amount of fertilizers needed, Soil Health Cards would give farmers information about the quality of the soil and what is the normal quantity of fertilizer to be used for a particular crop. For this, setting up of 500 new soil testing laboratories and 250 new mobile soil testing laboratories had been sanctioned in the Budget for 2008-09.

Studies have found that over-dose and injudicious use of conventional chemical fertilizers and pesticides affect soil fertility, vegetation, human and animal health. The government is also encouraging use of organic fertilizer and wormicompost as overdose of conventional fertilizers has been found to affect fertility of the soil in many places. Land under organic farming has increased from 42,000 hectares in 2003-04 to 464,000 hectares currently.

The introduction of nutrient based fertilizer subsidy will enhance soil health as it will be demand driven and not price driven.

Soil reclamation

It is necessary to offset the loss of agricultural land by bringing more land under cultivation. There is a large amount of degraded land that can be reclaimed through watershed development. There is also a considerable amount of saline and sodic land, which can be brought back to cultivation with treatment. It is being done by making many government programmes including MNAREGA. Vast areas of cultivated land are acidic, where significant yield increases are possible through treatment using waste material from industry. There is sulphur deficiency in large parts of the country, but this can be treated effectively, particularly for pulses and oilseeds. More generally, Indian soils are relatively deficient in organic matter and are suffering inadequate manuring and composting, aggravated in many regions by unbalanced use of chemical fertilisers, especially excessive application of nitrogen. This raises prospects of large yield increases by applying nutrients, including micronutrients, that have been seriously depleted.

The NBS based fertilizer subsidy can restore soil fertility.

Extension services

The National Commission on Farmers (NCF) has drawn attention to the knowledge deficit that exists at present and explains much of the difference between yields realised in experiments and what farmers actually get. One reason for this is the virtual collapse of extension services in most states. Farmers are not fully aware of the adverse consequences of unbalanced fertiliser use or of benefits of micronutrient application and soil testing to determine optimal nutrient requirements is hardly practised on a regular basis even by State Agriculture Departments. Similarly, although many new varieties of seeds and pesticides have entered the market during the last decade and farmers are using these, they do not appear to have significantly higher productivity and there are frequent complaints about quality. A problem is that input dealers, who have narrow commercial interests have emerged as the main vehicle for technology diffusion and farmers do not have access to reliable third-party advice which an effective and knowledgeable extension service should be able to provide. Lack of credit also pushes farmers to purchase inputs from local suppliers who often provide sub-standard inputs.

To overcome information gaps and for advice in contingencies such as pest-attacks, it is necessary to revitalise the extension system in a manner which links universities and best practices effectively to farmers. States need to take urgent steps in this area. Central initiatives on this also need to be strengthened. Krishi Vigyan Kendras set up by Indian Council of Agricultural Research (ICAR), can be better used. Agricultural Technology Management Agency (ATMA) model of extension being promoted by Department of Agriculture & Cooperation (DAC) will deliver results.

The Department of Agriculture and Cooperation, along with NABARD, has introduced a scheme for establishment of agri-clinics / agri-business centres / ventures by the agricultural graduates.

The ICAR is also associated in agriculture extension activities not only through KVKs but also Institute Village Linkage Programme (IVLP) and also its institutes / centres all over the country. The interaction of KVKs activities with the State / district extension machinery is being strengthened. It is planned to strengthen linkages between research and extension to improve quality and effectiveness of research and extension system. The extension system , thus, is being revitalised and broad based through KVKs, NGOs, farmers' organisations, cooperatives, the corporatesector and agri-clinics / agri-business centres. KVKs and ICAR/SAUs units are designated nodal agencies for quality certification including organic products, bio-fertilisers, and bio-pesticides. The supply of inputs, agro-processing and trade through such cooperatives / companies is encouraged through the availability of credit with the help of NABARD.

The NCF has suggested ways to synergise at the village level, for example through Farmer Knowledge Centres, and this is already being implemented in some places with PRI and NGO help. Since synergies across line departments and Centrally sponsored schemes can be derived best through district plans, the Planning Commission and Ministry of Panchayati Raj have begun strengthening the process of district planning. The recent MoA initiative to set up technical bodies such as the National Fisheries Board and the National Rainfed Areas Authority should help to improve synergy.

Agri clinic and agri business centre

The Ministry of Agriculture, Government of India, in association with NABARD has launched a unique programme to take better methods of farming to each and every farmer across the country.This programme aims to tap the expertise available in the large pool of Agriculture Graduates. AgriClinic offers professional extension services to innumerable farmers.

Government is now also providing start-up training to graduates in Agriculture, or any subject allied to Agriculture like Horticulture, Sericulture, Veterinary Sciences, Forestry, Dairy, Poultry Farming, and Fisheries, etc. Those completing the training can apply for special start-up loans for venture

Agribusiness Centres would provide paid services for enhancement of agriculture production and income of farmers. Centres would need to advise farmers on crop selection, best farm practices, post-harvest value-added options, key agricultural information (including perhaps even Internet-based weather forecast), price trends, market news, risk mitigation and crop insurance, credit and input access, as well as critical sanitary and phyto-sanitary considerations, which the farmers have to keep in mind.

Farmers could make use of the clinic to undertake soil testing and get professional counsel.The programme was started in 2002 as a supplement to government's extension services.

ITC's e-choupal is another development in the field of strengthening extension services.

SFAC

Small Farmers' Agribusiness Consortium (SFAC), a specialized agency of the Dept. of Agriculture & Cooperation, Govt. of India, supports entrepreneurs, farmer producer

Consortium → Association of several companies

groups, cooperatives, companies and other entities to set up agribusiness enterprises which add value to agriculture produce by offering risk capital through its Venture Capital Assistance Scheme.

Rainfed agriculture

The ministry of agriculture classifies areas, which receive less than 750 mm rainfall annually, and have less than 30 per cent land under irrigation (both surface and ground water) as drylands.

Rainfed regions are those where crop production is exclusively dependent upon rainfall. In India rainfed regions cover 177 districts and exist in all agro-climatic zones. However, they are mostly concentrated in arid and semi-arid areas. Most of these districts are country's poorest. Rainfed regions account for 68 per cent of the total net sown area in the country, according to the Union Ministry of Agriculture.

Rainfed agriculture plays an important role in India's economy. Rainfed crops account for 48 per cent of the total area under food crops and 68 per cent of the area under non-food crops in the country.

Nearly 50 per cent of the total rural workforce and 60 per cent of the livestock in the country are concentrated in the dry districts.

As opportunities for further agricultural growth in irrigated regions get exhausted, food security and productivity growth in agriculture in India in the coming years will increasingly depend on improved utilisation of resources and productivity growth in rainfed regions.

Most agricultural lands in rainfed areas in Orissa, West Bengal, Bihar and Chhattisgarh suffer from sulphur and phosphorous deficiency. Thus soil has become acidic in nature. These areas need interventions from agriculture scientists in dealing with the crisis.

Promotion of appropriate cropping patterns and livestock development is necessary. Development of suitable varieties and lab to land transfer is required.

Region specific watershed programmes need to be developed.

There is a need to divert a portion of the population dependent on agriculture to areas like fisheries, agro-processing and horticulture.Fisheries have a lot of potential in areas, which get good rainfall. It is quite clear that agriculture cannot sustain such a large mass of people in rainfed areas. The policy towards rainfed areas has to look beyond crop production and rainwater management.

National Rainfed Area Authority

National Rainfed Area Authority was set up in 2006 to coordinate the work of five ministries and improve productivity of the 85 million hectares of non-irrigated agricultural land- panchayati raj, rural development, agriculture, water resources and environment and forests. NRAA works under the agriculture ministry

command area → Area which comes under the dam constructed for irrigation purpose

Q: Challenges for

NRAA aims to build synergy among these ministries on their schemes, programmes and policies that are relevant to non-irrigated lands. It works for wholistic and integrated development of the rainfed areas.

The NRAA would prepare a national prospective plan, which would look at regional variations. The plan would be flexible and dynamic.

Drought

Droughts is of the following three types

Meteorological drought is when the actual rainfall in an area is significantly less than the climatological mean of that area. The country as a whole may have a normal monsoon, but different meteorological districts and sub-divisions can have below normal rainfall.

Long Period Average

India Meteorological Department (IMD) defines a rainfall range between 96 and 104 per cent of the LPA as being "near normal", while 90 to 96 per cent is considered "below normal", 104 to 110 per cent "above normal", above 110 per cent "excess" and below 90 per cent "deficient".

Hydrological drought means marked depletion of surface water causing very low stream flow and drying of lakes, rivers and reservoirs.

Agricultural drought means inadequate soil moisture resulting in acute crop stress and fall in agricultural productivity.

Droughts can throw out of gear the rural and national economy. Cattle, human beings and crops suffer a water shortage.

Drought occurs mainly due to failure of monsoon.

With wide variations in agro-climatic zones, drought occurs somewhere in India each year. While parts of Rajasthan and Andhra's Anantpur and Chittoor districts see two droughts in five years, western UP and northern Gujarat face it once in three years. Maharashtra alone has about a quarter of India's drought-prone districts. About 50 million Indians are affected every year.

Climate change is accelerating drought attacks. There were six between 1900 and 1950 and 12 in the following 50 years. We have already faced three droughts between 2000 and 2009.

There is an official checklist of symptoms to diagnose drought.. The early warning signs include delay in onset of SW monsoon, long 'break' within a monsoon, less rain in July, rise in fodder prices, fall in water reservoir levels, dwindling water supply, slower crop sowing.

Initially, government advises farmers to grow less water-seeking crops, increase fodder supply, and keep the Centre's National Crisis Management Committee (NCMC) informed. It becomes an emergency when there is virtually no rain during the sowing period; monsoon withdraws mid-season; and a dry spell for more than a month. The deficit in

rainfall by now grows and could be as much as 40% and crops start to wilt with no water and excessive heat.

The problem becomes acute and gets classified as a potential disaster when there is no rain for more than six weeks in a crop area, and the monsoon withdraws early, leaving behind parched land and people.

If 20%-40% of India's area is affected , it is called a drought year. If more than 40% of the country is reeling from rainfall shortage, the met department calls it an All India Severe Drought Year.

The primary responsibility of catching the early signs, offering relief and managing droughts lies with states.

The situation may warrant loan rescheduling , insurance premium waivers, and relief from the Centre. The state's budget can come under severe strain.

Once a drought is declared, Central government starts considering deferring/rescheduling farm loans, moving water and fodder by rail, hiking food allocation to poor families, creating more jobs, importing foodgrains to meet likely demand-supply gap, and check inflation.

A ministerial task force is set up to take rapid decisions. Drought-declared states are monitored individually and more carefully by the Centre. The Essential Commodities Act is used to prevent hoarding, and states get money for relief programmes.

Landless labourers and marginal farmers move to cities in search of casual jobs. Families with loans from moneylenders get further entrapped in poverty. Health suffers and schooling is disrupted as money dwindles. The impact on cities is by way of migration stress; declining farm growth pulls down industry, urban goods and services.

Proper water management, drought-resistant agriculture, income diversification, smarter subsidies and technology can ensure no one is left devastated by it anymore.

Drought-resistant varieties of seeds should be made available sufficiently.

Remedies lie in the form of better water management; sprinkler irrigation;drought resistant varieties of seeds; creation of irrigation; better credit facilities; shifting to dairy and other animal husbandry activities.

Contingency plan 2012

According to India Meteorological Department data, rains in the country are deficient by 21 per cent as of the beginning of August 2012.Sowing area of total kharif crops has declined by 10 per cent so far at 66.82 million hectare. Coarse cereals is worst affected with 23 per cent shortfall, followed by pulses (18 per cent), paddy (9 per cent) and cotton (7 per cent).

Government prepared contingency plans for 320 districts where monsoon rains have been poor. The plan has been prepared by the Central Research Institute for Dryland Agriculture (CRIDA), Hyderabad.

Among various measures being taken to tackle the drought-like situation, the Centre is providing knowledge input twice a week from ICAR besides seeds for alternate crop. The government is also trying to provide states with additional electricity to draw water from tubewells.

Centre has sanctioned 300 mega watt (MW) of power to Punjab and Haryana and about 275 MW for Uttar Pradesh for the purpose.

Centre has taken decisions to introduce diesel subsidy scheme, hike seed subsidy and release funds under National Rural Drinking Water Programme (NRDWP) and Integrated Watershed Management Programme.

A new Calamity

Since 2012, , damage to crops due to cold wave/frost will be eligible for central and state assistance following the government's decision to consider such weather condition as natural calamity.At present, cyclone, drought, earthquake, fire, flood, tsunami, hailstorm, landslide, avalanche, cloud burst and pest attack are treated as natural calamities and are eligible for relief under the State Disaster Response Fund (SDRF) and National Disaster Response Fund (NDRF).

The proposal was taken by the GoM on requests from the chief minister of Madhya Pradesh, which faced damage to rabi crops like wheat and pulses last year due to extreme cold conditions.

NDRF and SDRF

Government has created State Disaster Response Fund (SDRF)/National Disaster Response Fund (NDRF) to mitigate hardships due to natural calamities including drought. There is ready availability of funds with State Governments under SDRF to take immediate relief measures. Government of India supplements efforts of State Governments with financial assistance and logistic support. Government of India and State Governments contribute to SDRF in ratio of 3:1 for 17 General Category States and 9:1 in case of 11 Special Category States covering North-Eastern States including Sikkim and 3 hill States of Himachal Pradesh, Uttarakhand and Jammu & Kashmir.

Additional financial assistance, over and above SDRF, is considered from NDRF for natural calamities of severe nature. Allocation for SDRF/NDRF is made on the basis of recommendations of the 13th Finance Commission.

UN and drought

WMO, UN weather agency says that there's an urgent need for nations to adopt drought-management policies as farmers from Africa to India struggle with lack of rainfall and the United States endures the worst drought it has experienced in decades.

The World Meteorological Organization says the US drought and its ripple effects on global food markets show the need for policies with more water conservation and less consumption.WMO Secretary-General Michel Jarraud said the world must "move away from a piecemeal, crisis-driven approach and develop integrated risk-based national drought policies" because of climate change projections for more drought.

WMO

The **World Meteorological Organization (WMO)** is an intergovernmental organization with a membership of 189 Member States and is a specialised agency of the United Nations for meteorology (weather and climate), operational hydrology and related geophysical sciences. It has its headquarters in Geneva, Switzerland, and is a member of the United Nations Development Group..

As weather, climate and the water cycle know no national boundaries, international cooperation at a global scale is essential for the development of meteorology and operational hydrology as well as to reap the benefits from their application. WMO provides the framework for such international cooperation.

Since its establishment, WMO has played a unique and powerful role in contributing to the safety and welfare of humanity. Under WMO leadership and within the framework of WMO programs. National Meteorological and Hydrological Services contribute substantially to the protection of life and property against natural disasters, to safeguarding the environment and to enhancing the economic and social well-being of all sectors of society in areas such as food security, water resources and transport.

Rural credit

Nabard

The National Bank for Agricultural and Rural Development (Nabard) was set up in 1982, as the apex development bank for agriculture and rural development under an Act of Parliament. The bank began by taking over the agriculture credit functions of the Reserve Bank of India and the refinance functions of the then Agricultural Refinance and Development Corporation (ARDC).

Nabard's mission is to "promote sustainable and equitable prosperity in rural India through effective credit support, related services, institution development and other innovative initiatives." Its prime function continues to be that of refinancing, supplementing the resources of co-operative banks, regional rural banks (RRBs) and commercial banks against the amounts lent at the grassroots level for agriculture and rural development.
Apart from its developmental role, Nabard has also been entrusted with certain supervisory functions in respect of co-operative banks and RRBs under the Banking Regulation Act, 1949.

Nabard is now a major shareholder in the Agricultural Insurance Corporation of India. It also has equity stake in NCDX (National Commodity and Derivatives Exchange) in association with other national-level institutions such as ICICI Bank, the LIC and the NSE (National Stock Exchange).

Promoting self-help groups reflects Nabard's capabilities in capacity-building and nurturing the rural credit delivery system.

Nabard manages RIDF.

RIDF is made up of the priority sector shortfalls of public sector commercial banks, which were assigned the task of channelling at least 18 per cent of their total lending to agriculture.

The fund was set up in 1995-96 for providing loans to State governments and state-owned corporations for projects relating to minor and medium irrigation, soil conservation, watershed management and rural infrastructure (such as roads, bridges and market yards). Investment projects under social infrastructure, such as construction of primary health centres/schools, providing drinking water, and so on, were also supported under the RIDF. (Read ahead)

Rural credit institutions
They comprise cooperative banks, RRBs and LABs.

Co-operative credit structure
Co-operative credit institutions continue to play a crucial role in dispensation of credit for agriculture and rural development.

She short-term credit structure is managed by State co-operative banks (SCBs) and district central co-operative banks (DCCBs). Primary agricultural credit societies (PACSs) are short-term co-operative credit institutions dealing directly with individual borrowers.
The long-term co-operative credit structure is managed by State co-operative and agriculture rural development banks (SCARDBs) and primary co-operative agriculture and rural development banks (PCARDBs).

RRBs
Regional rural banks were set up in 1975 under an Act of Parliament to exclusively cater to the credit needs of the rural population, especially small and marginal farmers. The ownership structure of RRBs is, the Central Government (50 per cent), the State government concerned (15 per cent) and the sponsor commercial bank (35 per cent). The sponsor bank manages the RRB concerned.

At present, the 86 RRBs in the country are sponsored by 26 PSU banks . RRBs have a strong branch network across the country and the branches are located in 588 out of the 622 districts of the country.Since 2005, the Union Government has taken up a process for consolidation through amalgamation of different RRBs in a particular state sponsored by the same bank. As a result of this process of consolidation , the number of RRBs in the country had reduced from 156 to 82.

There are 11.55 crore farmer households in the country, of which, 9.27 crore belong to small and marginal farmers. Institutional rural credit is accessible to only around 50 per cent of these farmers.

Local area banks

LABs were started in 1996 with a view to providing institutional mechanisms for promoting rural savings as well as for the provision of credit for viable economic activities in the local areas. They are in the private sector. This is expected to bridge the gaps in credit availability and enhance the institutional credit framework in the rural and semi-urban area.

The bank shall be registered as a public limited company under the Companies Act, 1956. It will be licensed under the Banking Regulation Act, 1949 and will be eligible for including in the Second Schedule of the Reserve Bank of India Act, 1934.

The minimum paid up capital for such a bank shall be Rs.5 crore. The promoters' contribution for such a bank shall at least be Rs.2 crore.

The area of operation of the proposed bank shall be a maximum of three geographically contiguous districts in one or more states. Backward and less developed districts are considered for area of operation of LABs.

Priority sector

The Government of India through Reserve Bank of India (RBI) directs certain type of lending from the Banks operating in India irrespective of their origin. RBI sets targets in terms of percentage (of total money lent by the Bank) to be lent to certain sectors, which would not have had access to organised lending market or could not afford to pay the interest at the commercial rate. This type of lending is called Priority Sector Lending. Financing of Small Scale Industry, Small business, Agricultural Activities and Export activities fall under this category. This is also called directed credit 40% of net bank credit should be for the priority sector and of the 40%, 18% should be for the agriculture.22% is for the non-agri sectors.Rate of interest charged on such loans is less. The targets and sub-targets set under priority sector lending for domestic and foreign banks operating in India are given below

	Domestic banks (both public sector and private sector banks)	**Foreign banks operating in India**
Total Priority Sector advances	40 percent of NBC	32 percent of NBC
Total agricultural advances	18 percent of NBC	No target
SSI advances	No target	10 percent of NBC
Export credit	Export credit does not form part of priority sector	12 percent of NBC
Advances to weaker sections	10 percent of NBC	No target

(NBC denotes net bank credit)

Direct Agricultural advance means advances given by banks directly to farmers for agricultural purposes. These include short-term loans for raising crops i.e. for crop loans.

Indirect finance denotes to finance provided by banks to farmers indirectly, i.e., through other agencies. For example, credit for financing the distribution of fertilisers, pesticides, seeds, etc.The weaker sections under priority sector include small (1-2 hectares)and marginal farmers(upto 1 hectare) landless labourers, tenant farmers and share croppers;beneficiaries of Differential Rate of Interest (DRI) scheme where loans are given at 4% interest rate. It is an example of financial inclusion.

(Read along with the Nair Committee recommendations and the RBI policy changes in July 2012 as given in the Chapter on Banking) ৫৩ \৬৭

RIDF

RIDF was introduced by Government of India during the year 1995-96 for implementation and timely completion of various rural oriented schemes/ projects in the States which were languishing for shortage of funds. The fund is placed with NABARD for providing loan assistance to the State. It is composed of priority sector shortfalls of public sector banks, as mentioned above.

In the Union Budget 2013-14, allocation under RIDF enhanced to Rs 20,000 crore. Rs 5,000 crore earmarked exclusively for creating warehousing facilities.

Nabard and SHGs

A pioneer in the self-help group (SHG)-bank linkage concept, Nabard has brought banking to the doorsteps of the poor people, especially the women.

SHGs represent a unique approach to financial intermediation, Self Help Groups (SHGs) are small groups of 10-20 members. These groups collect savings from their members and provide loans to them. These groups also obtain loans from banks and on-lend them to their members. SHGs are formed and supported usually by NGOs or banks or by Government agencies. Linked not only to banks but also to wider development programmes, SHGs are seen to confer many benefits, both economic and social. SHGs enable women to grow their savings and to access the credit which banks are increasingly willing to lend. SHGs can also be community platforms from which women become active in village affairs, stand for local election or take action to address social or community issues (the abuse of women, alcohol, the dowry system, schools, water supply).

Being made up mostly of women, their default rate is negligible. Group lending ensures peer pressure to repay. Transaction costs are also dramatically reduced. With extension services and counseling, deployment of funds is effective.

Microfinance

Microfinance is defined as provision of credit and other financial services like insurance of very small amount to the poor in rural, semi-urban and urban areas for enabling them to raise their income levels and improve living standards. Micro finance Institutions are those which provide these facilities.

Microfinance covers not only consumption and production loans for various farm and non-farm activities of the poor but also include their other credit needs such as housing and shelter improvements.

A Self-Help Group (SHG) is a registered or unregistered group of micro entrepreneurs having homogenous social and economic background voluntarily coming together to save small amounts regularly, to mutually agree to contribute to a common fund and to meet their emergency needs on mutual help basis.

While the SHG-bank linkage programme has surely emerged as the dominant micro finance dispensation model in India, other models too have evolved as significant micro finance channels.

Government allows 'Micro Credit/Rural Credit' (non-banking financial company, NBFC) activities for Foreign Direct Investment (FDI)/Overseas Corporate Bodies (OCB)/Non-Resident Indians (NRI) investment to encourage foreign participation in micro credit projects.

Types of micro credit providers in India

- Domestic Commercial Banks:Public Sector Banks; Private Sector Banks & Local Area Banks
- Regional Rural Banks
- Co-operative Banks
- Co-operative Societies
- Registered NBFCs
- Unregistered NBFCs
- Other providers like Societies, Trusts, etc.

In the area of microfinance, there are many areas of concern in India. They are

a) unjustified high rates of interest
b) lack of transparency in interest rates and other charges.
c) multiple lending
d) upfront collection of security deposits
e) over-borrowing
f) ghost borrowers
g) coercive methods of recovery

Malegam Committee

Aimed at reviving the crisis- ridden micro finance sector, Reserve Bank of India Committee suggested that micro finance institutions (MFIs) be allowed to charge a maximum interest of 24 per cent on small loans which cannot exceed Rs.25,000.

The committee, headed by Reserve Bank's Central Board Director Y. H. Malegam, also recommended creation of a separate category of non-banking financial companies (NBFC-MFI) for the micro finance sector.

The panel also said small loans of up to Rs.25,000 could be given to families having an income up to Rs.50,000 per annum.

It further said at least 75 per cent of loans extended by MFIs should be for income generation purposes. It further recommended that a borrower cannot take loans from more than two MFIs.

These recommendations, the committee said, should be implemented from April 1, 2011. The RBI constituted the committee in October last in the wake of allegations of overcharging and using coercive recovery practices by MFIs that led to a spate of suicides in Andhra Pradesh.

About the regulations of MFIs, the Malegam Committee, suggested that it should be done by the National Bank for Agriculture and Rural Development (NABARD) in close coordination with the RBI.

With regard to NBFC-MFIs, the committee suggested that they should have a minimum net worth of Rs.15 crore.

It recommended that bank lending to NBFCs, which qualify as NBFC-MFIs, will be entitled to the 'priority lending' status.

- It has made a number of recommendations to mitigate the problems of multiple-lending, over borrowing, ghost borrowers and coercive methods of recovery. These include: a borrower can be a member of only one self-help group or a joint liability group(where money is lent to the whole group, it is called JLG); not more than two MFIs can lend to a single borrower; there should be a minimum period of moratorium between the disbursement of loan and the commencement of recovery; the tenure of the loan must vary with its amount; a credit information bureau has to be established; the primary responsibility for avoidance of coercive methods of recovery must lie with the MFI and its management; and the RBI must prepare a draft customer protection code to be adopted by all MFIs.

NBFC-MFI (given elsewhere in the material)

National Vegetable Initiative

The union government has launched a new scheme called vegetable initiative for urban clusters during 2011-12 with an outlay of Rs. 300 crore under the aegis of the Rashtriya Krishi Vikas Yojana.

The scheme envisages development of vegetable clusters for ensuring supply of good quality vegetables to one city or town in every state having a population of one million and above. In the case of states which do not have any city with one million population such as in the North East and the Goa, the state capital city or township having less than one million population is covered.

The scheme covers all aspects relating to vegetable production, from production and supply of planting material to marketing upto the retail level along with support for conducting base line survey, formation of farmer groups, their linkage to aggregators/markets besides training and capacity building of vegetable growers in the identified clusters.

The production of vegetables in the country has increased from 111.39 million tonnes in 2005-06 to 133.7 million tonnes in 2009-10. Accordingly, per capita availability of vegetables has increased from 279 gm per day to 317 gm per day over a period of 5

years. However, there are issues relating to enhancement of productivity, post-harvest losses and improvement in quality of vegetables.

NMFP

National Mission on Food Processing has been launched from 2012.The National Mission on Food Processing (NMFP) is a new Centrally Sponsored Scheme for giving of greater role to State/UTs; decentralized administration, better outreach and effective supervision and monitoring. The NMFP would also provide flexibility to States / UTs in the selection of beneficiaries, location of projects etc. for the development of food processing sector. This initiative of the Ministry would give an impetus to food processing industries in the country.

NMFP Scheme provides for sharing of the cost between Government of India (75%) and States (25%) for all States except North Eastern States, where, it is at 90:10 pattern. All Union Territories would be provided funds on 100% basis.

Kisan Credit Cards

The scheme of Kisan Credit Card (KCC) was introduced in 1998-99 for timely, easy and flexible availability of production credit to farmers. Commercial banks, cooperative banks and RRBs are implementing this scheme. Each farmer is

provided with a Kisan Credit Card and a passbook for providing revolving cash credit facilities. The farmer is permitted any number of drawals and repayments within a stipulated date, which is fixed on the basis of land-holdings.

All categories of farmers including tenant farmers, share croppers, oral lessees are eligible for a Kisan Credit Card .

Agricultural Price Policy in India

Prices of agricultural produce are important for farmers as these determine their Incomes. Farming should become economically viable and profitable for agriculture to boom and country to have food security. Agricultural produce shows maximum price fluctuation. So farm sector needs a price policy for price stabilisation.

The main objective of the Government's price policy for agricultural produce continue to aim at ensuring remunerative prices to the growers for their produce with a view to encouraging higher investment and adoption of modern farm technology for achieving higher levels of production as also to safeguard the interests of consumers by making available supplies at reasonable prices. Each season Government announces Minimum Support Price (MSP) for 24 major agricultural commodities and organises purchase operations through public and cooperative agencies. It operates effectively only for rice and wheat.

At the beginning of the sowing season for kharif and rabi crops, the Government announces Minimum Support Price (MSP) at which it is prepared to procure the produce that the farmer is willing to sell to the FCI for the PDS and buffer stock operations. When it actually procures when harvesting is done, the MSP is added to and the procurement price

Farmer → FCI → PDS

is arrived at. The grain is sold at the PDS outlets at issue price. The FCI's economic cost is what it costs the FCI to procure, store, distribute etc.

The Government decides on the support price for various agricultural commodities based on the recommendations of the commission for agricultural costs and prices (CACP). Commission for Agricultural Costs and Prices (CACP), while recommending prices takes into account all-important factors, viz.

- Cost of Production
- Changes in Input Prices
- Input/Output Price Parity
- Trends in Market Prices
- Inter-crop Price Parity
- Demand and Supply Situation
- Effect on Industrial Cost Structure
- Effect on General Price Level
- Effect on Cost of Living
- International Market Price Situation
- Parity between Prices Paid and Prices Received by farmers (Terms of Trade).

CACP recommends MSPs for 24 important crops.Of all the factors, cost of production is the most tangible factor and it takes into account all operational and fixed demands. Government organises Price Support Scheme(PSS) of the commodities, through various public and cooperative agencies such as FCI, CCI, JCI, NAFED, Tobacco Board, etc., for which the MSPs are fixed. For commodities not covered under PSS, Government also arranges for market intervention on specific request from the States for specific quantity at a mutually agreed price. The losses, if any, are borne by the Centre and State on 50:50 basis. The price policy paid rich dividends. Production improved and food security is being realized.

However, the criticism of MSP is that it is promoting rice and wheat while the need is for diversification. It helps the big farmer while the majority of farmers in India are subsistence farmers. Food subsidy burden is increasing and needs to be rationalized so as to spend on infrastructure.

National Food Security Mission

The Department of Agriculture & Cooperation, Ministry of Agriculture, has launched a Centrally-sponsored scheme on National Food Security Mission (NFSM) in pursuance of the resolution of the National Development Council (NDC) to increase the production of rice, wheat and pulses by 10, 8 and 2 million tonnes, respectively, over the benchmark levels of production, by the end of the Eleventh Five Year Plan period.

The Mission aims at increasing foodgrains production of the above crops through area expansion and productivity enhancement; restoring soil fertility and productivity; creating employment opportunities; and enhancing farm level economy to restore confidence of farmers of targeted districts.

Various activities of NFSM relate to demonstration of improved production technology, distribution of quality seeds of HYVs and hybrids, popularization of newly released varieties, support for micronutrients, and training and mass media campaign including awards for best performing districts. The identified districts are given flexibility to adopt any local area specific interventions as are included in the Strategic Research and Extension Plan (SREP) prepared for the agriculture development of the district. Rs. 2 crore each will be provided during the Eleventh Five Year Plan period to those districts which have a programme for two or more crops of the NFSM and Rs. 1 crore to the districts having a programme for any one of the crops.

The national food security mission (NFSM) is being implemented in 312 identified districts of 17 states of the country.

Food subsidy

Provision of minimum nutritional support to the poor through subsidized foodgrains and ensuring price stability in different states are the twin objectives of the food security system. In fulfilling its obligation towards distributive justice, the Government incurs food subsidies. The difference between economic cost of foodgrains and the issue price is reimbursed to FCI. Food subsidy is provided to FCI and states/ UTs undertaking DCP operations . Food subsidy is provided to distribute wheat and rice to the poor and also maintain a buffer stock. In 2012-13, food subsidy is budgeted at Rs.75,000 crores. However, it is expected to go up due to the concessional food planned to be supplied through the Food security Act.

Rashtriya Krishi Vikas Yojana (RKVY)

The NDC in its 53rd meeting (2007) decided to launch a programme to incentivise the States to increase the share of investment in agriculture in their State plans. Accordingly, the Government approved the Rashtriya Krishi Vikas Yojana (RKVY) with an allocation of Rs. 25,000 crore for the Eleventh Five Year Plan.

The RKVY aims at achieving the 4 per cent annual growth in the agriculture sector during the Eleventh Five Year Plan period by ensuring a holistic development of agriculture and allied sectors. The RKVY will be a State Plan Scheme and the eligibility for assistance under the scheme would depend upon the amount provided in the State budgets for agriculture and allied sectors, over and above the baseline percentage expenditure incurred on agriculture and allied sectors. The funds under the RKVY would be provided to the States as 100 per cent grant by the Central Government.

The main objectives of the schemes are:

- To incentivise the States to increase public investment in agriculture and allied sectors
- To provide flexibility and autonomy to the States in planning and executing agriculture and allied sector schemes
- To ensure the preparation of plans for the districts and the States based on agro-climatic conditions, availability of technology and natural resources.
- To ensure that the local needs/crops/ priorities are better reflected.
- To achieve the goal of reducing the yield gaps in important crops, through focused interventions.

- To maximize returns to the farmers.

Under the Scheme of RKVY, the following indicative broad activities have been identified for focused attention – Integrated Development of Food Crops, including coarse cereals, minor millets and pulses; agriculture mechanization; soil health and productivity; development of rain-fed farming systems; integrated pest management; market infrastructure; horticulture; animal husbandry, dairying and fisheries; organic and biofertilizers; and innovative schemes, National vegetable initiative

Second Green Revolution

The first Green Revolution has run its course. Cereal yields are rising very slowly, water tables are plunging, and agricultural growth now averages only 2% annually.

Second Green Revolution is necessary and is being ushered in , spearheaded by the corporate sector and helped by new laws. Second Green Revolution, focusing on fruits and vegetables, can double agricultural growth to 4% per year.

Land reform laws ban corporates from farming. But contract farming is possible: corporates contract to provide high-tech farm inputs on credit, and lift the output at guaranteed prices.

The biggest rural initiative comes from ITC, whose e-choupals.

E-choupals are electronic buying and selling centres, which also provide information to farmers on prices, weather, and scientific farming practices.

By cutting out middlemen, e-choupals can pay farmers a higher price than they get in mandis, yet lower ITC's procurement costs. The company started with soyabeans, wheat and shrimps, and is now diversifying into oilseeds, spices and fruit.

FieldFresh, run by Sunil Mittal of Bharti Telecom, already has 1,000 acres under horticulture in Punjab. Pepsi and McDonalds have started contract cultivation of citrus fruits and lettuce respectively. Godrej is into contract cultivation of maize, used to make cattle feed.

Global Green, a Thapar company, uses contract cultivation for gherkins and other products for export, and has a turnover of over Rs 100 crore.

Paper companies like Ballarpur and ITC provide farmers with fast-growing clonal varieties of trees that mature in just four years, and buy the output.

This corporate upsurge is being encouraged by a new political urgency to uplift rural India. A raft of new laws aim to end historical hurdles.

The Agricultural Produce Marketing Committee Act forces farmers to sell only at mandis, ostensibly to protect them from rapacious traders. But this makes contract farming illegal; companies cannot directly buy from farmers.

However, many states have now repealed their versions of the APMC Act, Second, India has long been plagued by a maze of 16 different food laws, some of which are self-contradictory (one law permits sweeteners in jams and another bans the practice).

Chilli paste is a widely sold product in Asia but cannot be produced in India because the law prohibits the use of thickeners. The central government wants to make a new comprehensive model law - integrated food law to replace the old laws.

Third, the government proposes a Warehousing Receipts Act, which will make warehousing receipts negotiable instruments, and thus qualify for bank financing.

This, along with futures trading in the NCDEX and other commodity exchange, can modernise agricultural trading just as stock market reforms earlier modernised the capital market.

Fourth, in order to curb hoarding, the Essential Commodities Act has long placed limits on commodity stocks. This makes large-scale corporate investment impossible.

Now that chronic agricultural shortages have given way to surpluses, the list of essential commodities has been drastically cut and optimists hope that the Act will soon be scrapped.

Fifth, tax laws and incentives are being liberalised to encourage private investment.
Sixth, banks are very keen to get into rural business, and many are now lending to self-help groups, which can enter into contracts with companies.

Cheap credit from banks and corporates can facilitate horticulture.
If new GMOs are added to it along with rural infrastructure(Bharat Nirman) and sustainability, the second green revolution can be the ever green revolution unlike the first one.

Horticulture

Vast areas of India have tropical and agro-climatic conditions which are well suited for cultivation of horticulture and plantation crops. They are also ideal substitutes for marginal and degraded lands, which are unsuitable for crop husbandry. They can help in diversification of agriculture. The horticulture sector contributes about 24.5 per cent towards agriculture GDP from only about 8 per cent of the cultivated area. Besides, providing nutritional and livelihood security and helping poverty alleviation and employment generation, this sub-sector sustains a large number of agro-Industries, which generate huge additional non-farming employment opportunities. The range of horticultural products includes fruits, vegetables, spices, coconut, medicinal and aromatic plants, mushrooms, cashew, cocoa etc. India accounts for 10 per cent of the world production of fruits and stands second after Brazil and is second largest producer of vegetables after China, contributing 13.4 per cent of the world vegetables production.The thrust areas for providing boost to the horticulture sector are as follows:

- Area Expansion
- Improving production
- Improving productivity

- Reducing cost of production
- Improving quality of products
- Value addition
- Promotion of marketing and exports
- Strengthening of credit and organisational
- support
- Human resource development
- Addressing relevant policy issues
- Cold chains.

National Horticulture Mission (NHM)

The National Horticulture Mission (NHM) is facilitating the holistic development of horticulture by promoting latest technologies involving production and supply of good quality planting material through tissue culture as well as nurseries, area expansion with improved cultivars, rejuvenation of senile orchards, organic farming, protected cultivation, integrated pest management/ integrated nutrient management along with creation of infrastructure for post harvest management and marketing. The post harvest management component includes the setting up of primary/mobile processing facilities. Besides, the cluster approach adopted under mission provides opportunities for setting up of food processing units for fruits and vegetables.

The Government has allocated a sum of Rs.1100.00 crore under the National Horticulture Mission during 2008-09 for taking up various activities involving production and productivity enhancement, post harvest management and marketing which in turn will create job opportunities in the field of horticulture.

Vishesh Krishi Upaj Yojana

The objective of the scheme is to promote export of fruits, vegetables, flowers, minor forest produce, and their value added products, by incentivizing exporters of such products.Exporters of such products shall be entitled for duty rebates.

AGRINDIA

The Union Cabinet has approved the proposal of Ministry of Agriculture, Department of Agricultural Research & Education (DARE) for setting up of a new company, called AGRINDIA.

AGRINDIA is a registered company under the Companies Act, fully owned by Government of India in the Department of Agricultural Research and Education (DARE) with a share capital of Rs.100 crore and initial paid up capital of Rs.50 crore.The company will undertake protection and management of intellectual properties generated in the system and its commercialization/distribution for public benefit. It will also set up research and development farms adn assist in setting up production units outside India, especially in Africa and the Asia Pacific regions, besides Latin America.

Livetock

India's livestock sector is one of the largest in the world. In 2010-11 livestock generated output worth Rs 2075 billion (at 2004-05 prices) which accounted for 4 per cent of the

national GDP and 26 per cent of the agricultural GDP. The output worth was higher than the value of food grains. Distribution of livestock is more equitable compared to that of land. Livestock sector grew about 1.5 times larger than in the crop sector over the years. Livestock, however, received only about 12 per cent of total public expenditure on agriculture and allied sector and about 4-5 per cent of the total institutional credit that went into agriculture and allied sector.

In the livestock sector, poor contribute to growth directly instead of getting benefit from growth generated elsewhere. The ownership of the livestock is more evenly distributed with landless labourers and marginal farmers owning bulk of livestock. The progress in the sector results in balanced development of the rural economy particularly in reducing the poverty amongst the weaker sections. The rural women play a significant role in Animal Husbandry and are directly involved in most of the operations relating to feeding, breeding, management and health-care of the livestock.

Livestock biodiversity is a valuable asset and provide insurance and buffer in adverse situation. The sector is playing a major role in the rural economy and a driving force for food security and sustainable agriculture in India. Livestock provide a diverse range of output for agriculture, irrigation, transport, fiber, leather, manure besides production of 90.7 million ton milk, 45 billion eggs and around 45 million kg wool.

Livestock is the major source of animal protein through milk, meat, eggs, etc, the demand for which is constantly increasing.

Problems

The livestock sector is presently facing serious constraints due to huge unproductive population, with low genetic potential, e.g. low milk yield, low body weight etc., shortage of feed grains, fodder and pasture lands and the presence of a large number of animal diseases. All these contribute to poor productivity and low levels of production inspite of large population of livestock. In the dairy sector, only 15% of the milk produced gets processed in the organized sector. There is also very little awareness on the safe and clean production system of livestock.

It was being contemplated for quite some time now to bring out a National Livestock Policy for holistic development of the livestock sector in the country. The Policy aims at higher growth rate of the sector to meet the future and increasing demand of livestock products without disturbing the existing fabric of small-holding system of production. The Policy also contemplates to double the per capita availability of protein from approximately 10 gm at present to 20 gm within a decade. The main focus of the Policy is on improving productivity, infusion of technologies, enhanced farmer participation, safety and quality assurance, marketing linkages, restructuring of institutions and enhanced investments.

Shortage of fodder is a major constraint. Various actions like distribution of quality fodder seeds, appropriate land use planning, promoting of fodder development technologies, assistance of Krishi Vigyan Kendras to promote these technologies and training on balanced feeding of livestock with appropriate supplementation are being taken. Encouraging mineral supplement, use of by-pass protein and by-pass fat are other interventions proposed. Better utilization of crop residues and use of unconventional crop

residues, e.g., bagasse for supplementation of feed are being considered. Growing fodder trees in degraded forest will also be encouraged. **(Dairy farmers do not want the protein in their cow's feed to be digested by the microbes in the rumen. This means the protein has to be protected so it can bypass the stomachs and can be absorbed in the intestines.)**

Two important schemes are being launched during XI Plan on sheep and goat Development and on Piggery Development. While the first one is targeted towards generating rural livelihood opportunities by promoting goat and sheep husbandry the later is more oriented towards the North Eastern States, where there is huge demand for pork and other pig meat products.

Livestock diseases take a huge toll on our livestock every year. FMD is most economically important disease prevalent in the country for many years.

Bird-flu as a exotic disease took a heavy toll on our poultry industry consecutively on three occasions in the last three years.

In order to mitigate the threat of breach on biosecurity and thereby compromise nutritional security, the quarantine system in the country is being revamped.

The issue of climatic stress on livestock productivity is also being addressed and research areas have bee prioritized. Special emphasis is being laid on protection and conservation of indigenous breeds, who have high endurance as well as more resistance to disease etc.

Livestock development has been as an important tool for poverty alleviation and sustainable livelihood security in terms of income generation for more than 500 million people in the country. In India 70-80 percent of the total livestock produce is contributed by underprivileged families and livestock are central to their livelihood and culture. According to FAO (2012), India ranks top in milk, third in egg and fifth in meat production but still insufficient to provide food security.

Livestock biodiversity: The Indian sub-continent occupies a pre-dominant position in so far as its animal genetic resources are concerned. Over 140 breeds of livestock including cattle (30), buffaloes (10), sheep (40), goats (20), camel (4), horse (6), pigs, donkey, mule, yak and mithun including poultry (18) have been distributed over the large area spread in different afro-ecological zones of the country. The usefulness of a breed is now judged not only on the basis of physical fitness and utility but also on monetary return.

Role of livestock: Livestock systems, if managed properly, play an important role in alleviating hunger and counteracting environmental degradation. These days concepts of organic farming and increased demand for cow based products such as bio-fertilizers, bio-pesticides, bio-energy and panch-gavya medicines gives an opportunity to make agriculture economically viable on a sustainable basis. The livestock production systems of the rural poor and underprivileged families are different from those of resource-rich farmers since they aim at optimizing use of the limited available resources and minimizing external input and avert risks, as against maximizing profits by the resource-rich. Livestock have strong socio-cultural linkages and for most rural families

particularly for women, livestock are a part of the family. The multi-functionality of livestock and their existence in developing countries particularly in smallholder production systems directly link them with poor rural communities.

Animal production practices: In the early part of this country, most farms integrated both crop and livestock operations. Indeed the two were highly complementary both biologically and economically. Livestock activities are normally integrated in the existing farming systems. Animals are kept mainly for the purpose of food security and poverty alleviation, which involves millions of small, landless and marginal farmers.

The growing population of the world need not only more animal proteins and products but also specific constituent and there is a pressure to multiply livestock species and make improvements and conservation of dwindling resources with modern biotechnological methods. The potential of livestock to reduce poverty is enormous.

Milk

Milk production increased from about 20 million tonnes in 1960s to 115 million tonnes in 2010-11. It grew at an annual rate of 4.4 per cent during 1990's and 3.8 per cent during 2000s. Although per capita availability of milk has increased from 128 gms per day in 1980-81 to 276 gms per day in 2010-11, it is far below the requirement of 280 gms per capita. In an effort to increase milk production, the Government of India has been implementing the National Project for Cattle and Buffalo Breeding since 2000 with focus on genetic upgradation of cattle and support system. Over the years the availability of feed resources has improved. But the deficit of dry fodder, concentrate and green fodder is high.

Milk is the main output of livestock sector accounting for 66.7 per cent of the total value of output of livestock. The growth in milk production decelerated from 4.4 per cent during 1990s to 3.8 per cent during 2000s. There remains a huge gap between the potential and realised yields in Indian livestock, on account of constraints relating to feeding, breeding, health and management. Crossbreeding of indigenous species with exotic stocks to enhance genetic potential has been successful only to a limited extent. Even after more than three decades of crossbreeding, the crossbred cattle population is just 16.6 per cent. Livestock sector did not receive the policy and financial attention it deserved. Further, livestock extension has remained grossly neglected — only about 5 per cent of farm households in India have access to information on livestock technology. The Working Group reports that the number driven progress in livestock production may not sustain in the long run due to increasing stress on the limited natural resources and that future growth has to come from improvement of technology and service delivery system leading to accelerated productivity, processing and marketing.

The Working Group has analysed various programmes related to cattle and buffalo development, particularly, National Project on Cattle and Buffalo Breeding (NPCBB). It has observed that NPCBB has significantly contributed to strengthening of semen stations . The group has suggested reformulation of strategy on breeding programme during the 12th Plan to achieve a sustained growth rate of at least 5 per cent in milk production. Technologies on sexed semen, embryo transfer and ovum pick up should be integrated in breed improvement programme. In view of climate changing scenario,

improvement of indigenous breeds that have the potential to contribute and be part of production system should be identified, evaluated and improvement programmes for them initiated on priority basis. These should include *Gir, Red Sindhi, Sahiwal, Kankrej* and *Rathi*breeds.

National Dairy Plan

Launched in 2012 at an initial outlay of Rs 2242 crore, the six year NDP-1 will be implemented in 14 major milk producing states including Andhra Pradesh, Bihar, Gujarat, Haryana, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh and West Bengal. While 80 per cent of the scheme will be financed through International Development Association (IDA) of World Bank, the rest will be funded by the Government of India and implemented by National Dairy Development Board (NDDB) through end implementing agencies (EIA)s in the states. The total outlay for the National Dairy Plan has been set at Rs 17,000 crore.

As of today, milk production is growing at four per cent which should increase to six per cent in the next few years. Through the NDP we intend to enhance breeding, feeding and milk procurement in the country to increase milk production. The demand for milk is projected to be around 200 million tonnes in 2021-22 as against the production of 122.8 million tonnes in 2010-11. The plan is expected to cover about 1.2 million milk producers in 23,800 villages.

National Dairy Plan-Phase 1 (NDP-1) looks to increase milk procurement by co-operatives from current 30 per cent to 65 per cent in next 15 years.

The project aims at boosting milk production using scientific breeding and feeding programmes covering about 2.7 million milch animals in 40,000 villages. It will also focus on modernising village-level infrastructure for milk collection and bulking such as milk cans, bulk milk coolers for a cluster of villages, associated weighing and testing equipment and related IT equipment.

India was the largest milk producing nation in 2010-11 with a production of 116.2 million tonne. This is close to 16% of world milk production. Milk production in the country is growing at 3.3% per annum while consumption is growing at 5% leaving a gap in demand and supply. We need to plug that gap to steady the domestic supply and milk prices.The National Dairy Plan (phase-1) was launched at Anand (Gujarat)

Modified Crop insurance

In 2010, the Government of India approved the modified National Agricultural Insurance Scheme (mNAIS), moving from a social crop insurance program with ad-hoc funding from the Government of India to a market-based crop insurance program with actuarially sound premium rates and product design. Given the technical and operational challenges associated with moving from the NAIS to the mNAIS, implementation began with a three-season pilot, starting with 34 districts across 12 states for the Rabi 2010-11 crop. Over time it could be expanded to India's 110 million farmer households.

Under the actuarial regime, farmer premiums and government subsidies will both be paid upfront at the start of the crop season to the insurer. The insurer, which could be the

June

Actuary → A person who calculates insurance risks & Premiums

public insurer AICI or a private sector competitor at the choice of each state, will then be responsible for settling all claims as they fall due. (if crop fails or there is calamity)

Increasing competition and expanding the role of the private sector in crop insurance contributes to the promotion of effective public-private partnerships in agricultural insurance.

With the introduction of the modified scheme, it is expected that an increased number of farmers will be able to manage risk in agriculture production in a better way and will succeed in stabilizing farm income particularly at the times of crop failure on account of natural calamities.

Keeping in view the various risks involved in agriculture production, the Ministry of Agriculture has been implementing the National Agricultural Insurance Scheme (NAIS) as a Central Sector Scheme since Rabi season 1999-2000 to insure the farming community against these risks. The modified scheme has the following features:

(i) Actuarial premiums will be paid for insuring the crops
(ii) The unit area of insurance for major crops is village panchayat;
(iii) Indemnity amount shall be payable for prevented sowing/planting risk and for post harvest losses due to cyclone;
(iv) payment up to 25% of likely claims would be released as advance for providing immediate relief to farmers;
(v) More accurate basis for calculation of threshold yield and minimum indemnity level of 70% instead of 60%;
(vi) Modified NAIS with improved features will have two components i.e. compulsory and voluntary. Loanee farmers will be insured under 'compulsory category' while non-loanee farmers will be insured under 'voluntary category';
(vii) Private sector insurers with adequate infrastructure and experience would also be allowed in the implementation of MNAIS.

Marketing and reforms

In order to provide the farmers with the choice of alternative marketing channels for sale of their produce at better and remunerative price and to encourage private investment in development of market infrastructure and supply chains, Ministry of Agriculture has formulated a model Agricultural Produce Marketing (Development & Regulation) Act, 2003. It has been circulated it to all the States/Union Territories for its adoption in their respective Agricultural Produce Marketing Committee (APMC) Act for facilitating the market reforms.

The Model Act provides for direct marketing, contract farming and setting up of market in private and cooperative sectors.

The provisions of contract farming, direct marketing by corporate and setting up of private and cooperative markets will facilitate better market access by farmers, reduce transportation cost and post harvest losses thus helping to increase the farmers' income.

'Krishi Karman' Awards

In August 2011, ten States have been selected for the newly instituted 'Krishi Karman' awards for best performance towards raising production of food grains.

Three awards are being given for total food grain production and four awards for production of rice, wheat, coarse cereals and pulses – the crops that constitute the food grain basket. Krishi Karman awards are the first-ever awards being given to States for their effort and contribution towards raising the country's food grain production.

Punjab and Uttar Pradesh are the joint winners of the Krishi Karman award in the category of States with overall food grain production of more than 10 million tonnes recorded in the last five years.

Assam and Orissa get the award in the category of States with overall food grain production of between one and 10 million tonnes.

Tripura is the sole winner in the category of States with overall food grain production of less than one million tonnes.

In the second set of four awards, being given for individual crops and crop groups, the award for rice goes to Chhattisgarh, wheat to Haryana, pulses to Maharashtra and Rajasthan, and coarse cereals to Karnataka.

Each award winning State gets a trophy, a citation and cash award. The cash award (for each State) is Rs. 2 crore for total food grain production and Rs. 1 crore for each of the four crops included in food grains.

Krishi Karman

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Agriculture and climate change

Impact of climate change on agriculture

Indian agriculture, with two-third rainfed area remains vulnerable to various vagaries of monsoon, besides facing occurrence of drought and flood in many parts of the country. Natural calamities such as drought and flood occur frequently in many parts of the country. Climate change will aggravate these risks and may considerably affect food security through direct and indirect effects on crops, soils, livestock, fisheries, and pests. Building climate resilience, therefore, is critical. Potential adaptation strategies to deal with the adverse impacts of climate change are developing cultivars tolerant to heat, moisture, and salinity stresses; modifying crop management practices; improving water management; adopting new farm practices such as resource-conserving technologies;

crop diversification; improving pest management; making available timely weather-based advisories; crop insurance; and harnessing the indigenous technical knowledge of farmers.

The Indian Council of Agricultural Research has initiated a scheme on National Initiative on Climate Resilient Agriculture with an outlay of 350 crore for 2010-12. This initiative has been planned as a multi-disciplinary, multi-institutional effort covering crops, livestock, and fisheries and focusing mainly on adaptation and mitigation of climate change in agriculture.

It also has a component for demonstration of climate-coping technologies on farmers' fields in 100 most vulnerable districts. State-of-the-art infrastructure is being set up at key research institutes to undertake frontier research on climate change adaptation and mitigation.

Agriculture has to become more competitive, efficient, and profitable and develop mechanism to reduce its vulnerability to climate change. Indian farmers, scientists and policy-makers have to address these issues in totality and develop strategies to increase adaptive capacity.

Earlier India had built capacity to withstand climatic extremes such as drought by establishing buffer food stocks, strengthening irrigation infrastructure and developing agriculture insurance schemes. We now need to put more emphasis on anticipatory adaptation measures that will allow attainment of sustainable development goals even if there is no climatic change or its magnitude is different from current projections.

A key requirement is to substantially increase the capital investment in agriculture, which has been continuously going down in last few years. Investment in irrigation infrastructure, silos for food and feed, timely implementation of contingency planning, rural roads and power could enhance agriculture's resilience to climatic extremes.

Establishment of early warning systems of climatic risks, disease and pests could help in determining the potential food insecure areas and communities and in providing assistance to policy planners in arranging relief.

Focused agricultural research on development of more adaptive varieties of crops, livestock and fish in future climate and development of water and carbon conservation practices will also be useful.

ICAR has launched a large networked project named National Initiative on Climate Resilient Agriculture to enhance the resilience of Indian Agriculture and demonstrate site-specific technology package on farmers fields for adapting to current climate risks.

Under Prime Minister's National Plan on Climate Change, 8 National Missions are being launched on climate change and National Mission of Sustainable Agriculture is one of them.

India Celebrates Declaration of Global Freedom from Rinderpest

A national ceremony was held to celebrate the declaration of global freedom from Ruinderpest, the dreaded cattle plague.

It took almost 150 years to wipe-out the disease once called Cattle-Plague due to very high level of mortality.

Productivity of Foodgrains

The productivity of foodgrains has increased from 1756 kg/ha during 2006-07 to 1921 kg/ha during 2010-11. Similarly, productivity of oilseeds has also increased from 916 kg/ha during 2006-07 to 1159 kg/ha during 2010-11.

The crop-wise productivity of various foodgrains crops and oilseeds from 2006-07 to 2010-11 is as under:

Crop	Yield (Kg/ha)				
	2006-07	2007-08	2008-09	2009-10	2010-11
Rice	2131	2202	2178	2125	2240
Wheat	2708	2802	2907	2839	2938
Coarse cereals	1182	1431	1459	1212	1528
Pulses	612	625	659	630	689
Foodgrains	1756	1860	1909	1798	1921
Oilseeds	916	1115	1006	959	1159

For enhancing the productivity of various foodgrains and oilseeds crops further in the country, various crop development programmes such as National Food Security Mission (NFSM), Integrated Cereals Development Programmes (ICDP) under Macro Management Mode of Agriculture, Rashtriya Krishi Vikas Yojana (RKVY) and Integrated Scheme of Oilseeds, Pulses, Oilpalm & Maize (ISOPOM) are being implemented. Besides, new initiatives have also been taken by the Government to enhance productivity of various crops by launching Bringing Green Revolution in Eastern India (BGREI), Initiatives for Nutritional Security through Intensive Millet Promotion (INSIMP) and Integrated Development of 60,000 Pulses Villages in Rainfed Areas as sub-schemes of RKVY.

In addition, frontline demonstrations of various crops are also organized by Indian Council of Agricultural Research (ICAR) for transfer of latest technology among the farmers at their fields.

Agrisnet Scheme to Provide IT Enabled Services to Farmers

The Government has launched the Agriculture Information System Network (AGRISNET) in the country.

AGRISNET envisages promotion of e-Governance by use of Information & Communication Technology (ICT). The objective of the programme is to provide IT

enabled services to farmers and also for computerization of various offices in the States in agriculture & allied sectors.

Kisan Call Centres

Kisan Call Centres function from 6.00 AM to 10.00 PM on all days throughout the year. They receive calls through the toll-free number 1800-180-1551. Call Centre agents reply farmers' queries instantaneously by using their own expertise as well as by referring to reference material available with them. They also browse Kisan Knowledge Management System data base for answering farmers' queries in local language. If some of the queries cannot be answered by the Call Centre agents, such calls are referred to experts. Call Centre agents record the details of every call in terms of farmer's details, query asked, reply given etc.

Pulses development

India's allocation of funds for boosting pulses production has multiplied eight fold in the last four years. India, leading producer and consumer of pulses in the world, has been investing more for food security(pulses are poor man's protein) and reducing imports. The allocations have risen from 105.59 crore in 2007-08 to 837.03 crore in 2010-11. A total of Rs. 1805.87 has been allocated for pulses development in these four years.

Government has approved Accelerated Pulses Production Programme (A3P) under National Food Security Mission (NFSM)on Pulses from 1.04.2010 for the remaining period of 11th Plan.

In the next two years, 10 lakh hectares of total pulses area would be targeted for coverage for village level demonstrations in 1000 blocks for five major crops of pulses namely Arhar (Tur), Moong, Chana, Urad, Masoor covering an area of 1000 hectares each in NFSM Pulses districts.

Farmers would be provided institutional support for supply of quality seeds, kits of nutrients and plant protection chemicals. Development and research projects focusing on inherent constraints of pulses production would also be encouraged for increased pulses production.

Implementation of A3P is estimated to bring in additional pulses production of 0.5 million tonnes.

Besides, a sum of Rs.300 crores has also been earmarked for organizing sixty thousand "Pulses and Oilseeds Villages" in the rainfed areas during 2010-11 for agricultural development under RKVY. The states which are not covered under NFSM Programme get assistance for pulses development under the Macro Management of Agriculture (MMA) scheme.

Government raised the minimum support prices (MSP) for pulses in mid-2010.

The major schemes such as the National Food Security Mission (NFSM), the Rashtriya Krishi Vikas Yojna (RKVY) and the Macro Management of Agriculture Scheme, now have special components for pulses development.

Under NFSM, 10 lakh hectares would be covered in the next two years for village level demonstrations for five major crops - arhar (tur), moong, chana, urad and masoor.

Under RKVY, Rs.300 crore have been earmarked for organising 60,000 "pulses and oilseeds villages" in the rainfed areas.

It is envisaged that productivity of pulses would increase by at least 10 percent with the implementation of this new programme. 2010-11 saw a record pulses production of over 18mt.

Q:- Terms of trade for agriculture in country are improving!

- TOT means the returns or benefit which the investor will get
- It is increasing bcoz - Credit facility improving
  - Bharat Nirman
  - Minimum support price ↑

*Food credit

- Credit lent by Banks to FCI to procure foodgrain

Infrastructure

Infrastructure is basic physical and organizational structures needed for the growth of economy-. It represents the goods and services necessary for an economy to function. It includes roads, bridges, water supply, sewers, electrical grids, telecommunications, and so forth.

Viewed functionally, infrastructure facilitates the production of goods and services, and also the distribution of finished products to markets, as well as basic social services such as schools and hospitals; for example, roads enable the transport of raw materials to a factory.

"Hard" infrastructure refers to the large physical networks necessary for the functioning of a modern industrial nation, whereas "soft" infrastructure refers to all the institutions which are required to maintain the economic system , health, and cultural and social standards of a country, such as the financial system, the education system, the health care system, the system of government, and law enforcement.

Various types of Infrastructure

Transport infrastructure

- Road and highway networks, including structures (bridges, tunnels, culverts)
- Mass transit systems (Commuter rail systems, subways, tramways, and bus transportation)
- Railways (rail yards, railway stations), level crossings, signalling and communications systems
- Canals and navigable waterways requiring continuous maintenance (dredging, etc.)
- Seaports
- Airports, including air navigational systems

Energy infrastructure

- Electrical power network, including generation plants, electrical grid, substations, and local distribution.
- Natural gas pipelines, storage and distribution terminals
- Petroleum pipelines
- Specialized coal handling facilities for washing, storing, and transporting coal.

Coal mines, oil wells and natural gas wells may be classified as being part of the mining and industrial sector of the economy, not part of infrastructure.

Water management infrastructure

- Drinking water supply
- Sewage collection, and disposal of waste water
- Drainage systems
- Major irrigation systems (reservoirs, irrigation canals)
- Major flood control systems

Communications infrastructure

- Postal service, including sorting facilities
- Telephone networks (land lines) including telephone exchange systems
- Mobile phone networks

- Television and radio transmission stations
- Cable television physical networks including receiving stations and cable distribution networks
- The Internet, including the internet backbone
- Communications satellites
- Undersea cables
- Major private, government or dedicated telecommunications networks, such as those used for internal communication and monitoring by major infrastructure companies, by governments, by the military or by emergency services, as well as national research and education networks

Solid waste management (Urban infra)
- Municipal garbage and recyclables collection
- Solid waste landfills
- Solid waste incinerators and plasma gasification facilities(**Plasma gasification** is a process which converts organic matter into synthetic gas, electricity, and slag using plasma.)
- Materials recovery facilities
- Hazardous waste disposal facilities

Types of soft infrastructure

Soft infrastructure includes both physical assets such as highly specialized buildings and equipment, as well as non-physical assets such as the body of rules and regulations governing the various systems, the financing of these systems, as well as the systems and organizations by which highly skilled and specialized professionals are trained, advance in their careers by acquiring experience, and are disciplined if required by professional associations (professional training, accreditation and discipline).

Unlike hard infrastructure, the essence of soft infrastructure is the delivery of specialized services to people.

Governance infrastructure

Economic infrastructure
- The financial system, including the banking system, financial institutions, the payment system, exchanges, the money supply, financial regulations, as well as accounting standards and regulations
- Major business logistics facilities and systems, including warehouses as well as warehousing and shipping management systems
- Manufacturing infrastructure, including industrial parks and special economic zones, plus the public safety, zoning and environmental laws and regulations that govern and limit industrial activity, and standards organizations
- Agricultural, forestry and fisheries infrastructure, including specialized food and livestock transportation and storage facilities

Social infrastructure
- The health care system, including hospitals, the financing of health care, including health insurance,
- The educational and research system
- Social welfare systems, including both government support and private charity for the poor, for people in distress or victims of abuse
- Sports and recreational infrastructure, such as parks, sports facilities, the system of sports leagues and associations

- Cultural infrastructure, such as concert halls, museums, libraries, theatres, studios, and specialized training facilities
- Business travel and tourism infrastructure

Critical infrastructure

The term critical infrastructure has been widely adopted to distinguish those infrastructure elements that, if significantly damaged or destroyed, would cause serious disruption of the dependent system or organization. Storm, deluge, or earthquake damage leading to loss of certain transportation routes in a city, for example bridges crossing a river, could make it impossible for people to evacuate, and for emergency services to operate; these routes would be deemed critical infrastructure.

Critical infrastructure is a term used by governments to describe assets that are essential for the functioning of a society and economy. Most commonly associated with the term are facilities for:

- electricity generation, transmission and distribution;
- gas production, transport and distribution;
- oil and oil products production, transport and distribution;
- telecommunication;
- water supply (drinking water, waste water/sewage, stemming of surface water (e.g. dikes and sluices));
- agriculture, food production and distribution;
- public health (hospitals, ambulances);
- transportation systems (fuel supply, railway network, airports, harbours, inland shipping);
- financial services (banking, clearing);
- Security services (police, military).

Recently(2013), in the cyber field, central government has decided to establish five-year project for strengthening the overall **cyber security structure of critical sectors of India.** This move has come following increase in the number of incidents of cyber attacks as well as security threats. In 2011, India faced around 13000 cyber incidents.

Who will implement the Project?

It will be realized by **National Critical Information Infrastructure Protection Centre (NCIPC).** NCIIPC functions under the guidance of National Technical Research Organization (NTRO).NCIPC is the nodal agency which coordinates the cyber security operations related to critical infrastructures in India.NCIPC will set up sectoral Computer Emergency Response Teams (CERTs) and will also install sensors on critical systems for getting real-time information regarding cyber attack of any kind for preparing a quick response.

NCIPC of India has been proposed. NCIPC will ensure critical infrastructure protection and critical ICT infrastructure protection in India.

Sectors whose cyber security falls under NCIPC are:

- Energy (natural gas, coal, oil and power)
- Finance and banking
- Transportation (civil aviation and railways)

- Space
- Law enforcement
- Security
- Telecom
- Defense

Critical infrastructure protection (CIP) is a concept that relates to the preparedness and response to serious incidents that involve the critical infrastructure of a region or nation

Urban infrastructure

Urban or municipal infrastructure refers to hard infrastructure systems generally owned and operated by municipalities, such as streets, water distribution, and sewers. It may also include some of the facilities associated with soft infrastructure, such as parks, public pools and libraries.

Green infrastructure

Q critically examine EIA.

Green infrastructure is a concept that highlights the importance of the natural environment in decisions about land use planning. In particular there is an emphasis on the "life support" functions provided by a network of natural ecosystems, with an emphasis on interconnectivity to support long-term sustainability. Examples include green belts, wild life sanctuaries; eco sensitive regions, Tiger, lion, and elephant reserves; bird sanctuaries; western ghats being conserved etc.

Hard infrastructure generally has the following attributes.

- Capital assets that provide services
- Large networks
- Interdependence: system components are interdependent
- In public economics theory, infrastructure assets such as highways and railways tend to be public goods, in that they carry a high degree of non-excludability, where no household can be excluded from using it, and non-rivalry, where no household can reduce another from enjoying it.

Ownership and financing: Infrastructure may be owned and managed by governments or by private companies, such as sole public utility or railway companies. Generally, most roads, major ports and airports, water distribution systems and sewage networks are publicly owned, whereas most energy and telecommunications networks are privately owned.

Impact on economic development

Investment in infrastructure is part of the capital accumulation required for economic development and has an impact on socioeconomic measures of welfare. In developing nations, expansions in electric grids, roadways, and railways show marked growth in economic development.

Adequate transportation infrastructure is an essential ingredient for economic development and growth. Beyond simply facilitating cheaper and more efficient movements of goods, people, and ideas across places, transportation infrastructure impacts the distribution of economic activity and development across regions; helps business to multiply; consumer welfare; productivity enhancement; balanced regional development; employment; demand; and makes the government access higher levels of fiscal resources to direct and indirect taxes. It is proved in the case of Golden Quadrilateral and PMGSY- the latter accounting for benefits for agriculture too.

During the Great Depression of the 1930s, many governments undertook public works projects in order to create jobs and stimulate the economy. The economist John Maynard Keynes provided a theoretical justification for this policy. It is called Keynsian stimulus that increases public spending on infrastructure. Following the global financial crisis of 2008–2009, some again proposed investing in infrastructure as a means of stimulating the economy.

Infrastructure in the developing world

Lack of infrastructure in many developing countries represents one of the most significant limitations to economic growth and achievement of the Millennium Development Goals (MDGs). Infrastructure investments and maintenance contributed to significantly improved growth performance in India and increased investment is necessary to maintain growth and tackle poverty. The returns to investment in infrastructure are very significant, with on average thirty to forty percent returns for telecommunications (ICT) investments, over forty percent for electricity generation, and eighty percent for roads.

Sources of funding

Currently, the source of financing varies significantly across sectors. In India, some are monopoly: railways and nuclear power. Some sectors are dominated by government spending, others by overseas development aid (ODA), and yet others by private investors.PPP is emerging as the dominant model. Debt and equity are, like anywhere else, the ways of raising resources. Read ahead.

Infrastructure Investment and GDP

The share of infrastructure as a percentage of GDP has increased from 5.04 per cent in the Tenth Plan to about 7.21 per cent of GDP in the Eleventh Plan. It can also be seen that the share of private sector as percentage of GDP has gone up from 1.12 per cent to 2.64 per cent during the same period. Starting from a base of 5.61 per cent of GDP in 2006–07, infrastructure investment reached an all- time high of 8.41 per cent of GDP in 2010–11.

12th FYP and Infrastructure (2012-17)

The strategy for the Twelfth Plan encourages private sector participation directly as well as through various forms of PPPs, wherever desirable and feasible. The share of private sector in infra- structure investment will have to rise substantially from about 36.61 per cent anticipated in the Eleventh Plan to about 48 per cent in the Twelfth Plan. It is expected that competition and private investment will not only expand capacity, but also improve the quality of service, besides minimising cost and time overruns in implementation of infrastructure projects.

The Central share in the overall infrastructure investment is likely to decline from 35.34 per cent in the Eleventh Plan to 28.72 per cent in the Twelfth Plan, and the States' share is likely to decline to 23.13 per cent compared to 28.05 per cent in the Eleventh Plan. The share of the private sector is expected to increase from 36.61 per cent in the Eleventh Plan to 48.14 per cent in the Twelfth Plan.

Financing Infrastructure Investment in the Twelfth Plan

The total public sector investment in infrastructure envisaged in the Twelfth Plan by the Centre and by the States is about 52%. Investment by the private sector, which includes PPP projects, makes up the balance of about 48 per cent of the required investment during the Twelfth Plan, a much higher share than the anticipated 36.61 per cent during the Eleventh

Centre & state – 52%

Public + private = PPP – 48%

Inter & Extra Budgetary Revenues

• Money given by govt to public sector other than budgeted amount is called IEBR.

Plan. Of the projected investment by the Central Government, about 60% is likely to be funded out of IEBR. (Please raise this issue in the class!)
↳ raised by CPSEs

The total requirement of debt by the public and private sectors is likely to be `27,75,641 crore. However, the availability of debt financing for infrastructure during the Twelfth Plan is estimated at `22,65,171 crore. There is a likely funding gap of about `5,00,000 crore for the debt component.

Institutional Framework for PPP

Cabinet Committee on Infrastructure

The approach to PPPs must remain firmly grounded in principles which ensure that PPPs are formulated and executed in public interest with a view to achieving additional capacity and delivery of quality public services at reasonable costs. These partnerships must ensure investment for supplementing scarce public resources while improving efficiencies. The government's current initiatives in the area of PPPs are designed to achieve these objectives. The following steps have been taken to promote private investment in infrastructure sector:

1. Setting up robust institutional structure for appraising and approving PPP projects
2. Developing standardised documents such as model concession agreements across infrastructure sectors
3. Increasing availability of finance by creating dedicated institutions and providing viability gap funding

The Committee on Infrastructure (CoI) was constituted in 2004 under the Chairmanship of the Prime Minister, with the objectives of initiating policies that would ensure time-bound creation of world class infrastructure, delivering services matching international standards, developing structures that maximise the role of PPPs and monitoring the progress of key infrastructure projects to ensure that targets are achieved. In 2009, the CoI was replaced by a Cabinet Committee on Infrastructure (CCI) under the Chairmanship of the Prime Minister. CCI reviews and approves policies and projects across infrastructure sectors. It considers and decides on financial, institutional and legal measures required to enhance investment in infrastructure sectors. In 2013, the CCI was merged in the CCAI when the CC on Investment was formed.

Regulatory Framework

In recent years, independent regulatory authorities have been established in the power, telecom, and civil aviation sectors. Tariffs in the port sector are also fixed by an independent authority. These authorities discharge numerous responsibilities, which were earlier in the domain of the government. For initiating further improvements in the regulatory structures and practices, Regulatory Reforms Bill is under consideration of the Government. Regulators for coal, roads and civil aviation are on the anvil (2013 July)

December 2013

The government gave its go ahead to the proposed Draft Regulatory Reform Bill, 2013 which aims to make regulators across key infrastructure sectors accountable to the Parliament besides giving them power of licensing.

The bill aims to fill a lacuna since India does not have a law to monitor the functioning of a large number of regulatory authorities existing in the country. The draft bill will apply to key sectors such as electricity, oil and gas, coal, telecommunications and internet, broadcasting and cable television, posts, airports, ports, waterways, railways, mass rapid transit system, highways and water supply, and sanitation.

The overall functioning of the regulator will be subject to scrutiny by the Parliament on a yearly basis.

Viability Gap Funding

The VGF Scheme was notified in 2006 to enhance the financial viability of competitively bid infrastructure projects, which are justified by economic returns, but do not pass the standard thresholds of financial returns. Under the scheme, grant assistance of up to 20 per cent of capital costs is provided by the Central Government to PPP projects undertaken by any Central Ministry, State Government, statutory entity or local body, thus leveraging budgetary resources to access a larger pool of private capital. An additional grant of up to 20 per cent of project costs can be provided by the sponsoring Ministry, State Government or project authority.

India Infrastructure Finance Company Limited (IIFCL)

IIFCL was incorporated by the Ministry of Finance in consultation with the Planning Commission in 2006 for providing long-term loans for financing infrastructure projects that typically involve long gestation periods. IIFCL provides financial assistance up to 20 per cent of the project cost both through direct lending to project companies, and by refinancing banks and financial institutions. IIFCL raises funds from both domestic and overseas markets on the strength of government guarantees. IIFCL has sanctioned loans aggregating `40,373 crore for 229 projects involving a total investment of `3,52,047 crore and disbursed `20,377 crore till the beginning of the fiscal year 2012-13.

IIFCL is expected to graduate in the Twelfth Plan from the existing role of a normal lender to that of a catalyst mobilising additional resources for financing of infrastructure. This could be achieved by IIFCL providing guarantees for bonds issued by private infrastructure companies rather than expanding its direct lending operations. This would enable mobilisation of insurance and pension funds, external debt and household savings. IIFCL would also make subordinated debt available as an additional source of finance. Further, IIFCL may also substitute its take-out financing scheme with an Infrastructure Debt Fund.

IDFC

IDFC was founded on the recommendations of the 'Expert Group on Commercialisation of Infrastructure Projects' under the Chairmanship of Dr. Rakesh Mohan. IDFC, a Public Private Partnership, is incorporated in Chennai. Government holds 54% of the company, rest is held by foreign shareholders and domestic entities.

Infrastructure Debt Fund

Infrastructure projects are capital intensive and have long payback periods, and, therefore, require long-term funds at comparatively low costs. Infrastructure projects in India are financed mainly by commercial banks, as insurance and pension funds do not normally lend for new projects. The present bond market lacks depth to address the needs for a long-term debt. With a view to overcoming these shortcomings, Infrastructure Development Funds (IDFs) are being set up for channelising long-term debt from domestic and foreign pension and insurance funds, as well as from other sources. These IDFs will also carry adequate credit enhancement in terms of implicit government guarantees for repayment of debt. The Reserve Bank of India, and the Securities and Exchange Board of India have already laid down regulatory framework for the IDFs.

Besides augmenting debt resources for financing infrastructure, the IDFs would refinance PPP projects after their construction is completed and operations have stabilised. By refinancing bank loans of existing projects, the IDFs are expected to take over a significant volume of the existing bank debt, and this will release an equivalent volume of fresh lending for infrastructure projects.(Read ahead for more IDFs)

Deepak Parekh committee on financing infrastructure

High Level Committee on Financing Infrastructure under the Chairmanship of Shri Deepak Parekh submitted its Interim Report to the Government of India in 2012. The Committee in its recommendation has suggested "rationalization of tariff" in order to maintain the inflow of investment. This would also result in improving the collection efficiency and reducing their losses. The report lays down detailed plans for every infrastructure sector, with special attention to the railways. The report titled '**Financing of Infrastructure**' recommended regulatory reforms through an overarching legislation. It says reforms are necessary for ensuring future investments in the infrastructure sector. It has warned that in the absence of reforms, even existing investments would be jeopardized.The panel has suggested public-private partnership (PPP) as the means of achieving target levels of investment.Issues related to the General Anti-Avoidance Rules (GAAR) and delays in environmental clearances and land acquisition should be resolved to attract investment in the infrastructure sector.

Engineering, Procurement, Construction (EPC) Contract

Developed countries are preferring Engineering, Procurement and Construction (EPC) contracts where the contractor is responsible for design and construction on a turnkey basis and for a fixed price. The Planning Commission has published a model EPC contract for Highways. It is expected that about 20,000 km of two-lane National Highways would be developed under this model. (More ahead)

PPPs: General Introduction

Public-private partnership (PPP) in infrastructure is a relatively new experience in most developing countries of the Asian and Pacific region. So far, only few countries have established institutional arrangements and developed manuals and resource materials in support of PPP development and for the capacity-building of their public officials. In the absence of such established institutional arrangements and resource materials, public officials face difficulties in project development and implementation, and general public can have many misunderstandings about PPPs.Governments in most developing countries face the challenge to meet the growing demand for new and better infrastructure services. As available funding from the traditional sources and capacity in the public sector to implement many projects at one time remain limited, governments have found that partnership with the private sector is an attractive alternative to increase and improve the supply of infrastructure services.

The partners in a PPP, usually through a legally binding contract or some other mechanism, agree to share responsibilities related to implementation and/or operation and management of an infrastructure project. This collaboration or partnership is built on the expertise of each partner that meets clearly defined public needs through the appropriate allocation of:

1. Resources
2. Risks
3. Responsibilities, and
4. Rewards

Governments worldwide have increasingly turned to the private sector to provide infrastructure services in energy and power, communication, transport and water sectors that were once delivered by the public sector. There are several reasons for the growing collaboration with the private sector in developing and providing infrastructure services, which include:

- Increased efficiency in project delivery, and operation and management;
- Availability of additional resources to meet the growing needs of □investment in the sector; and
- Access to advanced technology (both hardware and software). □Properly executed planning and development of a project also allows better screening of options, and helps in deciding appropriate project structure and choice of technology considering cost over the whole life cycle of the project.

Often, lack of government funding has been the main reason for considering a PPP option for a project. However, lack of government funding may not be the main reason for deciding a PPP option for the implementation of a project. A project may not be considered for being implemented as a PPP project unless efficiency gains from improved project delivery, operation and management, and access to advanced technology can offset the costs. In fact, many countries have established value for money as the main criterion in judging the merits of a PPP option for a project.

PPPs have become attractive to governments as an off-budget mechanism for infrastructure development as:

- They can enhance the supply of much-needed infrastructure services.
- They may not require any immediate cash spending. They provide relief from the burden of the costs of design and construction.
- They allow transfer of many project risks to the private sector.
- They promise better project design, choice of technology, construction, □operation and service delivery.

There are significant differences between a conventional construction procurement project and a PPP project that need to be clearly understood. The main differences include:

- PPP projects are different from conventional construction projects in terms of project development, implementation, and management. The administrative and approval processes in the case of PPP projects are also different.
- A PPP project is viable essentially when a robust business model can be developed.
- The risk allocation between the partners is at the heart of any PPP contract design. Both partners should clearly understand the various risks involved and agree to an allocation of risks between them.

There are many important economic, social, political, legal, and administrative aspects, which need to be carefully assessed before approvals of PPPs are considered by the government. PPPs have various limitations which should also be taken into account while they are being considered. The major limitations include:

- Not all projects are feasible (for various reasons: political, legal, commercial viability, etc.).
- The private sector may not take interest in a project due to perceived high risks or may lack technical, financial or managerial capacity to implement the project.
- A PPP project may be more costly unless additional costs (due to higher transaction and financing costs) can be offset through efficiency gains.

Often, the success of PPPs depends on regulatory efficiency.

Features of PPP Projects
- Promise of better project structure and design.
- Better service delivery, especially if performance based payment is □considered.
- Better chances of completion on time and within the budget.

A wide spectrum of PPP models has emerged. These models vary mainly by:
- Ownership of capital assets;
- Responsibility for investment;
- Assumption of risks; and
- Duration of contract.

The PPP models can be classified into 4 broad categories in order of □generally (but not always) increased involvement and assumption of risks □by the private sector.
The four broad categories are:
- Supply and management contracts
- Turnkey contracts
- Lease
- Concessions

Each of these four categories has many variants. While the spectrum of models are possible as individual options, combinations are also possible such as, a lease or (partial) privatization contract for existing facilities which incorporates provisions for expansion through Build-Operate- Transfer. In fact, many PPP projects of recent times are of combination type.

Supply and management contracts
A management contract is a contractual arrangement for the management of a part or whole of a public enterprise (for example, a specialized port terminal for container handling at a port or a utility) by the private sector. Management contracts allow private sector skills to be brought into service design and delivery, operational control, labour management and equipment procurement. However, the public sector retains the ownership of facility and equipment. The private sector is assigned specified responsibilities concerning a service and is generally not asked to assume commercial risk.
The private contractor is paid a fee to manage and operate services. Normally, the payment of such fees is performance-based. Usually, the contract period is short, typically three to five years. But the period may be longer for large and complex operational facilities such as a port or an airport.

Turnkey /EPC
Turnkey is a traditional public sector procurement model for infrastructure facilities. Generally, a private contractor is selected through a bidding process. The private contractor designs and builds a facility for a fixed fee, rate or total cost, which is one of the key criteria in selecting the winning bid. The contractor assumes risks involved in the design and construction phases. This type of private sector participation is also known as Design-Build.

The main pros and cons of this model include the following:
Pros:
- Well understood traditional model.
- Contract agreement is not complex.
- Generally, contract enforcement is not a major issue.

Cons:

- The private sector has no strong incentive for early completion.
- All risks except those in the construction and installation phases are borne by the public sector.
- Low private investment for a limited period.
- Only limited innovation may be possible.

Lease In this category of arrangement, the operator (the leaseholder) is responsible for operating and maintaining the infrastructure facility (that already exists) and services, but generally the operator is not required to make any large investment. However, often this model is applied in combination with other models such as build- operate-transfer. Under a lease, the operator retains revenue collected from customers/users of the facility and makes a specified lease fee payment to the contracting authority. Generally, the government undertakes the responsibility for investment and thus bears investment risks. The operational risks are transferred to the operator. However, as part of the lease, some assets also may be transferred.

The main pros and cons of this model include the following:

Pros:

- Can be implemented in a short time.
- Significant private investment possible under longer term agreements.
- In some countries, legally and politically more acceptable for strategic projects like ports and airports.

Cons:

- Has little incentive for the private sector to invest, particularly if the lease period is short.
- Almost all risks are borne by the public sector.
- Generally used for existing infrastructure assets.
- Considerable regulatory oversight may be required.

Concessions

In this form of PPP, the government defines and grants specific rights to an entity (usually a private company) to build and operate a facility for a fixed period of time. The government may retain the ultimate ownership of the facility and/or right to supply the services. In concessions, payments can take place both ways: concessionaire pays to government for the concession rights and the government may pay the concessionaire, which it provides under the agreement to meet certain specific conditions. Usually, such payments by the government may be necessary to make projects commercially viable (Like in the VGF) and/or reduce the level of commercial risk taken by the private sector, particularly in a developing or untested PPP market. Typical concession periods range between 5 to 50 years.

The main pros and cons of this model include the following:

Pros:

- Private sector bears a significant share of the risks.
- High level of private investment.
- Potential for efficiency gains in all phases of project development and implementation and technological innovation is high.

Concession → something granted

Cons:

- Highly complex to implement and administer.
- Difficult to implement in an untested PPP market.
- May have underlying fiscal costs to the government.
- Negotiation between parties and finally making a project deal may require long time.
- May require close regulatory oversight.
- Contingent liabilities on government in the medium and long term.

In a Build Operate-Transfer or BOT type of concession (and its other variants namely, Build-Transfer-Operate (BTO), Build-Rehabilitate-Operate-Transfer (BROT), Build-Lease-Transfer (BLT) type of arrangement), the concessionaire makes investments and operates the facility for a fixed period of time after which the ownership reverts back to the public sector. In a BOT modal, operational and investment risks can be substantially transferred to the concessionaire. In a BOT model, the government has, however, explicit and implicit contingent liabilities that may arise due to loan guarantees and sub-ordinate loans provided, and default of a sub-sovereign government and public or private entity on non- guaranteed loans.

By retaining ultimate ownership, the government controls the policy and can allocate risks to parties that are best suited to assume or remove them. BOT projects may also require direct government support to make them commercially viable.

The concessionaire's revenue in a BOT project comes from managing and marketing of the user facilities (for example, toll revenue in a toll road project) and renting of commercial space where possible. Concessions for BOT projects can be structured on either maximum revenue share for a fixed concession period or minimum concession period for a fixed revenue share, a combination of both, or only minimum concession period.

Suitability and which model to select

Each model has its own pros and cons and can be suitable for achieving the major objectives of private-private partnership to a varying degree. Special characteristics of some sectors and their technological development, legal and regulatory regimes, and public and political perception about the services in a sector can also be important factors in deciding the suitability of a particular model of PPP.

There is no single PPP model that can satisfy all conditions concerning a project's locational setting and its technical and financial features. The most suitable model should be selected taking into account the country's political, legal and socio- cultural circumstances, maturity of the country's PPP market and the financial and technical features of the projects and sectors concerned. As an example, for a new project, a BOT type of model may be quite suitable in a matured PPP market while a BOO type of models may be more appropriate in a developing/untested market.

Understanding the basic structure of a PPP arrangement A typical PPP structure can be quite complex involving contractual arrangements between a number of parties, including the government, project sponsor, project operator, financiers, suppliers, contractors, engineers and customers. The creation of a separate commercial venture called a Special Purpose/Project Vehicle (SPV) is a key feature of most PPPs. The SPV is a legal entity that undertakes a project and negotiates contract agreements with other parties including the government.

SPV has many advantages. Protected finance is available. A project may be too large and complicated to be undertaken by one single investor considering its investment size, management and operational skills required and risks involved. In such a case, the SPV mechanism allows joining hands with other investors who could invest, bring in technical and management capacity and share risks, as necessary.

The government may also contribute to the long-term equity capital of the SPV in exchange of shares. In such a case, the SPV is established as a joint venture company between the public and private sectors and the government acquires equal rights and equivalent interests to the assets within the SPV as other private sector shareholder.

Sometimes, governments want to ensure a continued interest (with or without controlling authority) in the management and operations of infrastructure assets such as a port or an airport particularly those which have strategic importance, or in assets that require significant financial contribution from the government. In such a case, a joint venture may be established. A joint venture is an operating company owned by a government entity and a private company (or multiple companies including foreign companies if permitted by law), or a consortium of private companies.

Often, an SPV is formed as a joint venture between an experienced construction company and a service operations company capable of operating and maintaining the project.
Other than its strategic, financial and economic interest, the government may also like to directly participate in a PPP project. The main reasons for such direct involvement may include:

- To hold interest in strategic assets;
- To address political sensitivity and fulfil social obligations;
- To ensure commercial viability of the project;
- To provide greater confidence to lenders; and
- To have better insight to protect public interest. Direct government involvement in a PPP project is usually guided by the legal and regulatory regime of the country and the government policy on PPPs. For example, the government may hold certain defined percentage of the stake in a strategic project such as an airport or a port.

PPPs in Infrastructure

Private investment in infrastructure is being encouraged in an environment which ensures competition and transparency. Protection of public interest is being ensured by institutionalising the necessary frameworks and processes for due diligence, checks and balances. However, it is recognised that unless governance issues, such as those related to competition in service provision, collection of user charges, institutional capacity, regulation, and dispute resolution continue to be adequately addressed, mobilisation of sufficient resources for the requisite infrastructure investment may not be possible.

Till 2012, government had approved 285 PPP projects involving an investment of `2,47,300 crore.

The government has identified several areas for reform of policies and processes.

PPP in Highways

The National Highway network of the country spans about 70,548 km. The National Highway Development Project (NHDP), covering a length of about 54,000 km of highways, is India's largest road development programme in its history. The government has encouraged increased private sector participation in upgrading the arterial road network of the country to world class standards. More than 60 per cent of the estimated investment requirement is expected to be financed through PPP. With several key projects on the anvil spanning a length of about 45,000 km (including six-laning of four-laned roads, expressways and port connectivity projects) and a large number of projects in States, there are increasing opportunities for the domestic and foreign players in the sector. The government has decided to widen 20,000 km of less than two-lane National Highways to two-lane standard in the EPC mode.

PPP in Civil Aviation

During the Eleventh Plan, the private sector played a major role in the development of metro airports through PPP. The development of Greenfield (new) international airports at Hyderabad and Bengaluru along with the redevelopment of the Delhi International airport was successfully completed during this period. The redevelopment of Mumbai International airport, which was also taken up through PPP, is at an advanced stage of completion. Investment by the private sector on the four metro airports during the Eleventh Plan periodwas `23,187 crore. Further, it was observed that introduction of PPP has led to a significant rise in the collection of revenues, especially non-aviation revenues.

Airports Authority of India has identified 15 operational Airports for taking up operation and maintenance of both terminal and air side through PPP. This would be taken up in two phases. In the first phase, nine airports, namely Guwahati, Jaipur, Ahmedabad, Bhubhaneshwar, Lucknow, Gaya, Udaipur, Khajuraho and Amritsar would be taken up; and in the second phase, six airports would be taken up for operation and maintenance through PPP. Kolkata and Chennai airports have been constructed by AAI with an investment of about 4,200 crore. PPP in management and operation of airports is not only preferable for reasons of efficiency and superior services but also important for keeping passenger charges low, because of the ability of private entities to raise non-aviation revenues that cross-subsidise airport charges. This proposition is borne out by the international experience and the experience of PPP metro airports in India. It is, therefore, recommended that these large airports should be awarded under the PPP mode for their management and operation.

Five green field airports including Navi Mumbai, Goa, Kannur, Chandigarh and Kota have been identified for development through PPP. For building and operating a Greenfield airport on PPP basis, a precise policy and regulatory framework has now been spelt out in the Model Concession Agreement for Greenfield Airports.

CAA in the place of DGCA

- Government decided to set up a new regulator for the aviation sector -- the Civil Aviation Authority -- that will replace the Directorate General of Civil Aviation (DGCA)(July 2013). The Civil Aviation Authority will be responsible for ensuring safety and regulating the Indian civil aviation sector.The government has proposed levying of a "safety fee" on each passenger to fund the new proposed Civil Aviation Authority (CAA).

Brownfield - Buy/develop existing one

PPP in Urban Infrastructure

Private sector participation needs to be encouraged in urban infrastructure sectors like water sup- ply and sewerage and solid waste management. In urban transport, private sector can provide more efficient transport services, construct and maintain modern bus terminals with commercial complexes, over bridges, city roads and so on. PPP initiatives are also being undertaken to develop metro rail systems in Indian cities

Hyderabad Metro Rail Project

Hyderabad Metro Rail Project is presently under construction on PPP mode with a total project cost of `12,132 crore. The project is spread over three high density traffic corridors of Hyderabad with total length of 71 km and is being developed on Design, Build, Finance, Operate and Transfer (DBFOT) mode. The project was awarded to the successful bidder for a VGF of `1,458 crore which will be provided by the Central Government while the remaining investment will be made by the concessionaire. This will be the single largest private investment in a PPP project in India. It is also one of the largest metro rail projects built and operated by a private entity anywhere in the world. The project demonstrates how large volumes of private capital can be deployed in public projects in a transparent, efficient and competitive manner. The concession has been awarded on the basis of the Model Concession Agreement for Urban Transit developed by the Planning Commission.

Delhi Metro is a rapid transit system serving Delhi, Gurgaon, Faridabad, Noida, and Ghaziabad in the National Capital Region of India. Delhi Metro is the world's 13th largest metro system in terms of length. Delhi Metro is India's first modern public transportation system, which has revolutionized travel by providing a fast, reliable, safe, and comfortable means of transport. The network consists of six lines with a total length of 189.63 kilometres (117.83 mi) with 142 stations, of which 35 are underground, five are at-grade, and the remainder are elevated.

Delhi Metro is being built and operated by the Delhi Metro Rail Corporation Limited (DMRC), a state-owned company with equal equity participation from Government of India and Government of National Capital Territory of Delhi. However, the organisation is under administrative control of Ministry of Urban Development, Government of India. Besides construction and operation of Delhi metro, DMRC is also involved in the planning and implementation of metro rail, monorail and high-speed rail projects in India and providing consultancy services to other metro projects in the country as well as abroad.

The Delhi Metro Rail Corporation has been certified by the United Nations as the first metro rail and rail-based system in the world to get "carbon credits for reducing greenhouse gas emissions" and helping in reducing pollution levels in the city by 630,000 tonnes every year. The Government of India and the Government of Delhi jointly set up the Delhi Metro Rail Corporation (DMRC) registered in 1995 under the Companies Act, 1956.

The **Mumbai Monorail** is a monorail system under construction in the city of Mumbai, India as part of a major expansion of public transport in Mumbai. The project is being implemented by Mumbai Metropolitan Region Development Authority (MMRDA), with a consortium of Larsen & Toubro (L&T) and a Malaysian infrastructure firm Scomi Engineering. It will be the first monorail in India Construction began in 2009. The first line is scheduled to be completed soon.

In joint venture management is done jointly unlike in PPP.

PPP in Ports

The government has encouraged private sec- tor participation in port development and operations. Foreign direct investment up to 100 per cent is permitted under the automatic route for port development projects. Private investment has been envisaged on PPP basis in ports of Kolkata, Haldia, Paradip, Vizag, Ennore, Chennai, Tuticorin, Cochin, New Mangalore, Mormugao, Mumbai, JNPT and Kandla.

PPP in Power

To attract private sector participation, government has permitted the private sector to set up coal, gas or liquid-based thermal, hydel, wind or solar projects with foreign equity participation up to 100 per cent under the automatic route. The government has also launched Ultra Mega Power Projects (UMPPs) with an initial capacity of 4,000 MW to attract `160–200 billion of private investment. Out of the total nine UMPPs, four UMPPs at Mundra (Gujarat), Sasan (Madhya Pradesh), Krishnapatnam (Andhra Pradesh) and Tilaiya Dam (Jharkhand) have already been awarded. The remaining five UMPPs, namely in Sundergarh District (Orissa), Cheyyur (Tamil Nadu), Girye (Maharashtra), Tadri (Karnataka) and Akaltara (Chattisgarh) are yet to be awarded. To create Transmission Super Highways, the government has allowed private sector participation in the transmission sector. A PPP project at Jhajjar in Haryana for transmission of electricity was awarded under the PPP mode. Further, to enable private participation in distribution of electricity, especially by way of PPP, a model framework is being developed by the Planning Commission.

PPP in Railways

Dedicated Freight Corridor Corporation of India Limited (DFCCIL) has been set up for implementing the Dedicated Freight project and the Ministry of Railways would explore the possibilities of attracting private investment in some segments of this project. Indian Railways has decided to redevelop 50 railway stations in the metropolitan cities and major tourist centers like Delhi, Jaipur, Chandigarh, Patna, Bypanahalli, Bhubneshwar, Mumbai CST, Howrah and so on as world-class stations through PPP. The proposal to set up of production units for manufacturing of electric and diesel locomotives at Madhepura and Marhowra respectively and passenger coaches at Kanchrapara through PPP has already been approved. Further, movement of container trains has already been opened to the private sector, and this has acquired more than 25 per cent share of the market. Construction of an elevated metro rail project in Mumbai is being undertaken through PPP.

PPP in Micro Irrigation

A scheme for setting up Micro Irrigation Systems (MIS) through PPP will be launched in pursuance of the government's objective to enhance irrigation efficiency, productivity and farm incomesby employing more efficient means of irrigation in integrated clusters. The absence of organised operations in the farm sector would be overcome by farmers coming together for the purpose of implementing this scheme through a single entity in every village. The existing subsidies which are provided by the Central and State Governments for on-farm MIS equipment and solar systems would be availed of under this scheme. Similarly, budgetary support would continue to be provided for the development of infrastructure. PPP in MIS would help in dou- bling the irrigation efficiency as compared to flow irrigation.

PPP in Storage of Food grains

A scheme for setting up modern storage facilities through PPP under the VGF has been formulated in pursuance of the Government decision to create 2MMT of modern storage facilities in the form of silos. This would enhance food security, reduce wast- age and

improve the quality of stored food grains.

Silos will be constructed and operated under the PPP mode across several states. Land for construction and operation of silos would be provided on licence to the private entity and up to 20 per cent of the total project cost will be provided as VGF. For storage of foodgrains at the Silos, the Concessionaire will be entitled to receive a recurring storage charge which shall be payable on adherence to performance and maintenance standards. It is expected that in the first phase, a capacity of 2 million MT of silo capacity would be created under the PPP mode.

PPPs in Social Sectors

The Twelfth Plan lays special emphasis on the development of social sectors in view of their impact on human development and quality of life, especially of the underprivileged sections. The physical targets set in the Plan cannot be met out of public resources alone. It is, therefore, imperative that resources have to be attracted from the private sector to ensure that targets, in physical and financial terms, are met by the end of the Twelfth Plan period.

In the social sectors, it may not be possible to adopt the user-charge-based concessions, although they may not be completely ruled out. However, concessions which would provide reim- bursement of service costs could attract considerable private investment. The main advantages of adopt- ing the PPP approach in the social sectors would be enhanced investment, reduction in time and cost over-runs, improvement in efficiencies and better quality of performance.

PPP in Education

A scheme for setting up 2,500 schools under PPP mode is being rolled out in the Twelfth Plan. The purpose of the scheme is to meet the govern- ment's objective of establishing world-class schools for providing quality education to underprivileged children who cannot afford to pay the tuition fee that good private schools charge. It is expected that the scheme will help in creating capacity for providing quality education to 40 lakh children, out of which 25 lakh will be from the underprivileged category.

The respective rights and obligations of the private entity and the government will be codified in an agreement with the former undertaking to deliver the agreed service on the payment of a unitary charge by the government. Recurring tuition support would be provided for up to 1,000 students from under privileged categories at par with the amount that the Central Government spends on a student in Kendriya Vidyalaya. There would be no capital support and land would have to be procured by the private entity. Infrastructure support shall be made available by the government for the under- privileged students at the rate of 25 per cent of the recurring tuition support. The concession would be for a period of 10 years. There will be no financial bidding. Predetermined criteria relating to capacity and track record of the respective applicants will be taken into account in selection of the private entities.

The scheme for 2,500 PPP schools should be viewed as an opportunity to evolve innovative ways to empower and enable non-government players to engage in providing world-class education, especially to children from low-income families. The objective should be to combine the respective strengths of the public and private sectors to complement each other in pursuit of the shared goal of good education for all. In particular, adoption of the PPP mode would lead to rapid expansion of access to world-class education by low-income families.

PPP in Health Care Services

Several State Governments are experimenting with delivery of health services through different models. Planning Commission is also in the process of preparing a scheme for setting up secondary and tertiary care hospitals through PPPs at various District Headquarters. The principle objective of the scheme is to create a health care delivery mechanism comprising multi-specialty hospital to meet the growing health care needs of the poor, and for supplementing human resources in the sector by setting up nursing schools and medical colleges.

It is expected that in the Twelfth Plan, the pro- posed scheme will be rolled out by the Government, and a 200-bed district-level hospital would serve a catchment area of about 8–10 lakh of population (20 lakh for a 300-bed tertiary care hospital). This will help families from the economically disadvantaged groups get access to quality health care through hospitals set up under this scheme, especially those who are covered under the Rashtriya Swasthya Bima Yojna (RSBY).

PPP in Skill Development

As part of the government's initiative to augment the programmes for skill development, the Prime Minister had announced setting up of 1,500 ITIs through PPP in unserved blocks. The objective is to create centres of excellence in vocational education especially for the youth from low-income families in order to improve their prospects of gainful employment. The programme will be expanded to cover a total of 3,000 blocks during the Twelfth Plan.

A major proportion of the costs incurred by an ITI are of a recurring nature, and it is therefore, proposed to provide support for the recurring expenditure incurred by an ITI towards training students from underprivileged families. Further, it is proposed to provide capital grant to meet a part of the cost of creating the infrastructure for setting up the ITIs. It is expected that 30 lakh youth, including 15 lakh youth from socially and economically disadvantaged groups would be initiated into vocational training and will acquire skills through the ITIs set up under this scheme.(Read along with the Chapter on Inclusive Growth)

Financial Support to PPPs in Social Sectors

A scheme for financial support to PPPs in the social sectors is being formulated as part of the Twelfth Plan initiative to enhance investments and coverage in social sectors, and also to expand the role of private participation.

The scheme envisages that capital investment and recurring costs to be incurred by a non-government entity on the delivery of services to EWS families, based on a concession agreement between government (or a statutory authority) and a non- government entity, will be provided by the respective State Governments, who in turn will be eligible for Viability Support Funding (VSF) from the Central Government.

Capacity Building in the States

The State Governments generally do not have dedicated staff resources for handling PPP projects or for building the requisite capacity. Such capacity is critical for conceptualising project proposals, engaging consultants, interacting with and supervising consultants, analysing and processing their advice for government approvals, interacting with prospective investors, executing the project documents and monitoring implementation. Therefore, the Planning Commission may need to provide financial assistance (ACA) to the State Governments for the setting up a nodal Secretariat for PPP in each State.

The aforesaid PPP Secretariat in each State would be responsible for identifying areas in the respective States amenable to PPP, conceptualise the projects, initiate and approve feasibility studies, appraise and approve bid documentation, guide the process and so on. This would enable capacity building in the States. The total expenditure on this scheme over the next five years would be limited to about `100 crore.

India Front-Runner in the PPP Race: ADB

According to a study by the Economic Intelligence Unit of the Economist commissioned by Asian Development Bank (ADB), while UK and Australia have been categorised as mature economies, India is positioned in the league of developed economies like Republic of Korea and Japan on implementation of PPP projects for infrastructure development. India has outscored China and Japan to rank second on PPP projects performance among the Asian nations and fourth in the Asia-Pacific nations. As per the Report, PPP development in India has been driven by strong political will and advances in public capacity and processes.

The Report states that PPP projects have a huge level of overall acceptance and use in India. It states that government agencies have a relatively high level of proficiency in PPP projects and that as a result of introduction of Model Concession Agreements, the risk allocation has been improving. In terms of finance, matters have improved, with a variety of initiatives (such as the creation of the Viability Gap Funding and the India Infrastructure Finance Company Limited) enabling greater participation of private finance in infrastructure.

To conclude, the gains of private participation in meeting the policy objectives of the Government have been significant during the Eleventh Plan. These initiatives will be expanded and reinforced during the Twelfth Plan, especially in social sectors such as health, education, skill development and so on with a view to meeting the investment targets, while also ensuring inclusiveness. It is envisaged that by the end of the Twelfth Plan, not only will there be `55,74,663 crore worth of investment in infrastructure sectors, but also that PPPs would have successfully forayed into the social sectors to promote universal access, while ensuring quality in the delivery of services.

Financing Infrastructure

Traditionally, infrastructure development used to occur through the public sector. However, given the scarcity of public resources, and the need to shift scarce public resources into health and education, efforts have been made to induct private participation in the development of infrastructure. These efforts have met with a fair degree of success. As of 31 March 2012, 390 PPP projects have been approved involving an investment of 3,05,010 crore. According to a report published by the World Bank, India has been the top recipient of PPP investment since 2006 and has accounted for almost half of the investment in new PPP projects implemented in the first half of 2011 in developing countries. An Asian Development Bank report states that India stands in the same league as developed economies like South Korea and Japan on implementation of PPP projects and the Model Concession Agreements prepared in India and used in our PPP projects have also been commended.

The total investment in infrastructure sectors in the Twelfth Plan is estimated to be `55.7 lakh crore, which is little more than one trillion dollars at prevailing exchange rates (about Rs.60 for a US Dollar in mid-July 2013). The share of private investment in the total investment in infrastructure rose from 22 per cent in the Tenth Plan to 36.61 per cent in the Eleventh Plan. It will have to increase to about 48 per cent during the Twelfth Plan if the infrastructure investment target is to be met. These projections have also been validated by the high level

commit- tee on infrastructure set up under the chairmanship of Shri Deepak Parekh. Its interim report that was presented in October 2012 is given elsewhere in this Chapter) The committee has however qualified its projections as dependent on several policy initiatives that the government would need to take for ensuring this level of investment.

The Twelfth Plan lays special emphasis on the development of social sectors in view of their impact on human development and quality of life. Unlike the case with other infrastructure, experiments with PPP in the social sector have been more limited. Many States have experimented with PPPs in health and education. The Central Government has approved setting up of 2,500 Model Schools in PPP mode and a proposal for setting up 3,000 ITIs through PPP is under consideration. These initiatives will be strengthened during the Twelfth Plan.

Resort to PPPs in the social sector often raises concerns about the commercialisation of services that are normally expected to be provided free or highly subsidised. These are important concerns but they can be addressed by well-drafted concession agreements and strict monitoring to ensure that PPP concessionaires abide by their commitments. This must be reinforced with penalties for non compliance. While extending the concept of PPP to social and urban sector projects, the need for 'people's' participation in the design and monitoring of PPP schemes becomes crucial. Local citizens are direct stakeholders in such projects and therefore their support becomes crucial. Therefore, some cities and States have begun to shape PPPs in the social and urban sectors as People–Public–Private Partnerships (PPPPs). This is a valuable innovation which should be applauded.

Take out financing

In the Union Budget speech for the year 2009-10, the Hon'ble Union Finance Minister stated "To stimulate public investment in infrastructure, we had set up the India Infrastructure Finance Company Limited (IIFCL) as a special purpose vehicle for providing long term financial assistance to infrastructure projects. We will ensure that IIFCL is given greater flexibility to aggressively fulfill its mandate. Takeout financing is an accepted international practice of releasing long-term funds for financing infrastructure projects. It can be used to effectively address Asset-Liability mismatch of commercial banks arising out of financing infrastructure projects and also to free up capital for financing new projects.

Objectives of the Takeout Finance Scheme

- To boost the availability of longer tenor debt finance for infrastructure projects.
- To address sectoral / group / entity exposure issues and asset-liability mismatch concerns of Lenders, who are providing debt financing to infrastructure projects.
- To expand sources of finance for infrastructure projects by facilitating participation of new entities i.e. medium / small sized banks, insurance companies and pension funds.

EPC

EPC Contracts refers to an Engineering, Procurement and Construction contract. In an EPC Contract, the EPC contractor undertakes total responsibilities for the project upto the commissioning stage for a pre-agreed consideration. While conceptually, EPC contract may look similar to turnkey contract, it goes a little further than a turnkey contract as in an EPC contract the EPC contractor undertakes total responsibility as well as liability for the commissioning of the project whereas in a turnkey contract, the contractor is generally responsible for selling of the plant. Road projects with less traffic density, which are unviable on toll mode, may be executed through engineering, procurement and construction (EPC) contracts. According to a high-power committee headed by HDFC Chairman Deepak

Parekh, this will help speed up road construction projects in the country. The conventional item rate contracts are prone to high cost and time overruns.

Viability Gap Funding

The scheme aims at supporting infrastructure projects that are economically justified but fall short of financial viability. Support under this scheme would be available only for infrastructure projects where private sector sponsors are selected through a process of competitive bidding. The total Viability Gap Funding under this scheme will not exceed twenty percent of the Total Project Cost; provided that the Government or statutory entity that owns the project may, if it so decides, provide additional grants out of its budget, but not exceeding a further twenty percent of the Total Project Cost.

The government will provide a Viability Gap Funding (VGF) which shall not exceed 20 per cent of the Total Project Cost; provided that the Government or statutory entity that owns the project may, if it so decides it will provide additional grants out of its budget, but not exceeding a further 20 per cent of the Total Project Cost. VGF under this scheme will normally be in the form of a capital grant at the stage of project construction. Proposals for any other form of assistance may be considered by the Empowered Committee and sanctioned with the approval of Finance Minister on a case-to-case basis. The project should be implemented i.e. developed, financed, constructed, maintained and operated for the Project Term by a Private Sector Company to be selected by the Government or a statutory entity through a process of open competitive bidding; provided that in case of railway projects that are not amenable to operation by a Private Sector Company, the Empowered Committee may relax this eligibility criterion. The project should provide a service against payment of a pre-determined tariff or user charge. The concerned Government/statutory entity should certify, with reasons: That the tariff-user charge cannot be increased to eliminate or reduce the viability gap of the PPP; That the Project Term cannot be increased for reducing the viability gap. Thus, Viability Gap Funding means a grant one-time provided by the Public Sector (Central Government / State Government) for Financial Support to PPPs in Infrastructure, with the objective of making a project commercially viable.

It is a Plan Scheme administered by the Ministry of Finance. Suitable budgetary provisions are made in the Annual Plans on a year-to- year basis for the scheme.

Recently, a government appointed committee headed by the Department of Economic Affairs (DEA) Secretary Arvind Mayaram today approved viability gap funding (VGF) of Rs 1,458 crore for development of Hyderabad Metro Rail.

IDF

Setting up of Infrastructure Debt Funds (IDFs) was announced in the Union Budget for 2011-12. These are aimed at accelerating and enhancing flow of long term debt for funding infrastructure projects in the country. They will also act as a catalyst to channelize domestic savings. IDFs would provide a vehicle for refinancing the existing debt of infrastructure projects which are funded mostly by commercial banks. This would create fresh headroom for commercial banks and enable them to take up a larger number of new infrastructure projects.

An IDF can be structured either as a company or as a trust. If set up as a trust, it would be regulated by SEBI under the Mutual Fund Regulations. If set up as a company, the IDF would be structured as a Non-Banking Finance Company (NBFC) and will be under the

regulatory oversight of RBI. Guidelines with enabling provisions have already been issued by the Reserve Bank of India and SEBI.

An IDF-NBFC would issue either rupee or dollar denominated bonds and invest only in debt securities of Public Private Partnership projects which have a buy-out guarantee and have completed at least one year of commercial operations. Such projects are expected to be viewed as low-risk investments and would, therefore, be attractive for risk-averse insurance and pension funds.

Establishment of Infrastructure Debt Fund through PPP model is taking place in India. A Memorandum of Understanding (MOU) was signed, recently for setting-up India's First Infrastructure Debt Fund(IDF) structured as a Non-Banking Finance Company (IDF-NBFC). The fund is jointly promoted by ICICI Bank, Bank of Baroda, Life Insurance Corporation (LIC) and Citicorp Finance (India) and it is titled Infradebt Limited. Ratings agency Crisil assigned 'AAA' ratings to India Infradebt Limited, the country's first infrastructure debt fund under the non-banking finance company structure which is a PPP.

Infradebt Ltd, the IDF, would seek to raise debt capital from domestic as well as foreign resources and would invest in infrastructure projects under the Public-Private Partnership model that have completed one year of operations. The IDF will expand and diversify the domestic and international sources of debt funding to meet the large financing needs of the infrastructure sector, thereby giving an impetus to the creation of the infrastructure necessary to drive India's growth.A higher credit rating would enable IDFs to access long-term funds for infrastructure sector at competitive rates

CCI

The Cabinet cleared setting up of the Cabinet Committee on Investment for fast tracking decision on big projects on in December 2012.December. Prime Minister heads this super investment body which will fast track clearances for mega projects.

The proposed body will not be a substitute for the Foreign Investment Promotion Board (FIPB). FIPB is for clearance of foreign direct investment proposals and if the investment is upto Rs.1200 crores, its decision is final. For FDI beyond the Rs.1,200 crores, CCEA permission is required.

PM will be the chairman of the committee and he will nominate its members. The cabinet committee on infrastructure will be dissolved and all the powers will be vested with the Cabinet Committee on Economic Affairs (CCEA).

The proposal to set up a high-level body for according speedy clearance to infrastructure projects entailing investment in excess of Rs 1,000 crore was initially mooted by Finance Minister Chidambaram who had proposed setting up NIB to oversee and monitoring large projects. NIB could also be called Cabinet Committee on Investment.

The proposal, however, had evoked sharp criticism from the Environment Ministry, which had said that NIB would dilute its powers.

Environment Ministry said that the proposal seems to have been mooted only for the benefit of large firms and investors, while having no provision for redressing the concerns of affected people.

Finance Minister said there were over 100 projects, each involving investment of Rs. 1,000 crore or more, that have been delayed for various reasons. "The main purpose is to oversee and monitor large projects which will give a fillip to India's economic growth. Our problem is not conceptualising projects. Our problem lies in getting numerous clearances and getting the project off the ground within a reasonable time

The functions of the Committee are as under:

(i) to identify key projects required to be implemented on a time-bound basis, involving investment of Rs 1000 cr or more, or any other critical projects, as may be specified by the Committee, in sectors such as infrastructure, manufacturing, etc.;

(ii) to prescribe time limits for issue of requisite approvals and clearances by the Ministries/Departments concerned in respect of projects in identified sectors;

(iii) to monitor the progress of identified projects including the time prescribed/taken to obtain each approval each approval/clearance and delays, if any;

(iv) to review implementation of projects, that have been delayed beyond the stipulated timeframe, including issues causing delay in grant of clearance/approvals;

(v) to review the procedures followed by Ministries/Departments to grant/refuse approvals and clearances;

(vi) to take decision regarding grant/refusal of approval/clearance of specific projects that are unduly delayed , if deemed necessary;

(vii) To consider and decide measures required for expeditiously granting/refusing approvals/clearances in identified sectors including simplification of rules/procedures followed by the respective Ministries/Departments for decision making; and

(viii) to require statutory authorities to discharge functions and exercise powers under the relevant law/regulation within the prescribed time frames for promoting investment and economic growth.

Accordingly, all the concerned Ministries/Departments have been requested to review projects, both in public and private sectors, having investment of Rs 1000 cr or more that are pending on account of delay in according clearances/approvals and to formulate and circulate the proposals for the consideration of the CCI, after due inter-ministerial consultations, in respect of such delayed projects. If the Administrative Ministry/ Department feels that a proposal needs to be considered by the Committee of Secretaries first, it should send a note/proposal for consideration by the Committee of Secretaries to the Cabinet Secretariat.

The CCI took up the task to debottleneck stalled projects involving cumulative investment of Rs. 1.61 lakh crore. Investment of Rs. 69,000 crore has already been made in these stalled projects. This clearance would facilitate future investment of Rs. 92,000 crore. These initiatives include issue of environment clearance to 106 different development projects; clearances to 30 New Exploration Licensing Policy blocks, where clearances were pending with either the ministry of commerce or the ministry of defence; clearances to 10 power transmission line projects and North Karanpura Thermal Power project in Jharkhand.□A special cell in the Cabinet Secretariat is essentially in the nature of a project monitoring group for all large projects. If a decision of the CCI is required in any case, the special cell will bring the case to the CCI.

2013-14 Union Budget and Infrastructure

The Finance Minister has promised new industrial corridors, smart cities, bigger role for private firms in coal, a regulator for the dispute-ridden highways sector and support for innovative financing for infrastructure projects

Airport express

The Delhi Airport Metro Express (DAME) is a Delhi Metro line from New Delhi Metro Station to Dwarka Sector 21, linking the Indira Gandhi International Airport. The line, also known as the Orange line is operated by the Delhi Airport Metro Express Pvt. Limited (DAMEPL), a subsidiary of Reliance Infrastructure, the concessionaire of the line, and opened in February 2011. The total length of the line is 22.7 km, of which 15.7 km is underground and 7 km, from Buddha Jayanti Park and Mahipalpur, is elevated.

Service was suspended from July 2012 to January 2013 due to technical problems. After reopening, the speed was cut to only 50 km/hr, extending journey time from the airport to New Delhi Station to over 40 minutes. On 27 June 2013 Reliance Infrastructure Ltd intimated DMRC that they are unable to operate the line beyond 30 June 2013. Following this DMRC took over operations of Airport Express line from 1 July 2013.

Why Reliance Infra pulled out?

Delhi Airport Express Private Ltd (DAEPL) was a special purpose vehicle set up by the parties to operate and run the 22.7-km line. Reliance has pulled out of its 30-year contract to operate the Airport Express line. Lessons for the PPP are: The government, having decided that India needs upgraded infrastructure and lacks the public funds to build it, has focused in its planning on partnerships with the private sector. Reliance Infrastructure won the bid to operate the Airport Express on the assumption that it would carry 40,000 people a day. In effect, it has even at its best been carrying half those numbers, around 17,000. As a result, much advertising space has gone unsold. And so made losses; it costs Rs 7 crore a month to run, but the revenue from tickets and advertising is only Rs 3 crore. That is presumably what lies behind the private sector operator's unwillingness to persist with the project; DAMEPL appears to have decided that the prospects of a turnaround in the line's fortunes are not great. The question is, of course, whether the original estimate of 40,000 metro riders was reasonable - another example of how auctions can lead to unrealistic estimates in the hope of renegotiation later. PPP projects have to work out how this problem can be avoided. The project was built at a cost of Rs 5,700 crore, with Reliance spending Rs 2,285 crore and the DMRC paying Rs 3,415 crore. What went wrong? For one, it appears that construction standards were deficient. That meant that the speed of the train was drastically lowered, and a planned 17-minute trip began to take as much as 45 minutes - which made it difficult to attract riders, as the ticket price of Rs 150 became extremely unattractive for a regular metro-rail ride. Scheduling and track layout itself minimised the attractiveness of the Airport Express as an option for travellers. It shut down before midnight, for example, opening at 5.15 am - whereas most international flights take off and land in Delhi between midnight and 4 am. And the Airport Express did not even run to Terminal 1 of Delhi airport, the terminal through which most of Delhi's cost-sensitive passengers fly; nor did it connect seamlessly with the rest of the Metro. The government intends to launch PPP-financed infrastructure worth Rs 1.15 lakh crore in the coming months. If the lessons of the Airport Express are learned, we can be far more gainful.

SIA

Social impact assessment (SIA) is a methodology to review the social effects of infrastructure projects and other development interventions. The origin of SIA comes from the environmental impact assessment (EIA) model, which first emerged in the 1970s in the U.S, as a way to assess the impacts on society of certain development schemes and projects before they go ahead - for example, new roads, industrial facilities, mines, dams, ports, airports, and other infrastructure projects. It has been incorporated since into the formal planning and approval processes in several countries, in order to categorize and assess how

major developments may affect populations, groups, and settlements. SIA is often carried out as part of, or in addition to, environmental impact assessment, but it has not yet been as widely adopted as EIA in formal planning systems, often playing a minor role in combined environmental and social assessments.

Social impact assessment is also of increasing importance as a means to measure and monitor the social returns or social outputs of a business.

Social impacts can be defined as the consequences to people of any proposed action that changes the way they live, work, relate to one another, organise themselves and function as individuals and members of society. This definition includes social-psychological changes, for example to people's values, attitudes and perceptions of themselves and their community and environment. Indeed, some SIA practitioners consider social impacts to be only 'as experienced' (e.g. stress, disruption, hunger) and differentiate these from the causal processes (e.g. over-crowding, infrastructure pressure, poverty)

The main types of social impact that occur as a result of these project-related changes can be grouped into five overlapping categories:

- lifestyle impacts – on the way people behave and relate to family, friends and cohorts on a day-to-day basis;
- cultural impacts – on shared customs, obligations, values, language, religious belief and other elements which make a social or ethnic group distinct;
- community impacts – on infrastructure, services, voluntary organisations, activity networks and cohesion;
- amenity/quality of life impacts – on sense of place, aesthetics and heritage, perception of belonging, security and livability, and aspirations for the future; and
- health impacts – on mental, physical and social well being, although these aspects are also the subject of health impact assessment .

The key points of the above discussion are that:

- social and biophysical impacts are interconnected and should be assessed together;
- SIA is understood to be concerned with the human consequences of development proposals, identifying all significant social impacts that arise in this context; and

National Investment & Manufacturing Zones (NIMZs)

The Government of India has announced a National Manufacturing Policy with the objective of enhancing the share of manufacturing in GDP to 25% within a decade and creating 100 million jobs. The National Investment & Manufacturing Zones (NIMZs) are an important instrumentality of the manufacturing policy.

The basic detail is as follows: State government selects the land and applies to the Central government to accept its proposal to set up an NIMZ. If the central government accepts, it notifies the same and sets up an SPV that manages it. State government owns it itself or makes any other arrangement of ownership.

NMIZs are the cornerstone of the NMP for realising its goals.NIMZs will be developed as green field industrial townships, benchmarked with the best manufacturing hubs in the world.

These NIMZs will seek to address the infrastructural bottleneck which has been cited as a constraining factor for the growth of manufacturing".

The NMIZ will function as "a self-governing and autonomous body and will be declared by the State Governments as an Industrial Township under Art 243 Q (c) of the Constitution.

They would be different from SEZs in terms of size, level of infrastructure planning, and governance structure related to regulatory procedures and exit policies". NIMZ may also have SEZs located in them. While SEZs mainly concentrated on exports, NIMZs have no such role, though they may export if they choose to. SEZs exist for the services secor s well while NIMZ does not.

Thus, NIMZ is going to be an all-inclusive gigantic structure combining production units, public utilities, logistics, environmental protection mechanisms, residential areas and administrative services. It may also include one or more Special Economic Zones (SEZs), Industrial Parks and Warehousing Zones, Export Oriented Units (EOUs) and Domestic Tariff Area (DTA) units.

The NMP prescribes that an NIMZ would have an area of at least 5000 hectares and that the State Government "will be responsible for selection of land suitable for development of the NIMZ, including land acquisition if necessary".

As regards internal infrastructure of NMIZ, it will be provided by a Developer or a group of Co-developers, while external linkages will be provided by Govt. of India and the concerned State Govt. Thus, it requires Centre-State co-ordination. The NMP says that the administrative structure for NMIZ will be headed by an SPV- Special Purpose Vehicle .

While the Central Govt will be responsible for notifying the NIMZ and issuing necessary clearances, the State Governments really have many tasks to perform. Apart from selecting the land and acquiring if necessary: such as ensuring water requirements, power connectivity, infrastructure linkages, etc. .

The NMP empowers the Central Govt. with the creation of a High Powered Committee to ensure necessary coordination among central ministries and state governments and also monitor the progress of environmental and other clearances, as well as ensuring external physical infrastructure in a time bound manner. The latter includes: Rail, Road (National Highways), Ports, Airports and Telecom and it also talks about using public private partnership model for this purpose and providing Viability Gap Funding.

State Govt may also have to provide such external linkages. Other functions of states government include, among other things,

a) land,
b) funding of initial cost of land,
c) exploring funding arrangements, including from international funding institutions, long term tax free debentures, etc
d) power connectivity,
e) water requirements,
f) state roads connectivity,
g) sewerage and effluent treatment,
h) health, safety and environmental issues, etc.

Besides the above major features of NMIZ, the NMP deals at great length on matters of

a) institutional framework [e.g. making Department of Industrial Policy and Promotion (DIPP) as the nodal department of Govt. of India];
b) rationalization and simplification of business regulations – dispensing with complying with 70 laws and regulations and filing sometimes as many as 100 returns a day;
c) making labour laws flexible;
d) exit policy for units in NMIZs that also ensures prospect of loss of job insurance policy for employees;
e) leveraging infrastructure deficit and government procurement, etc.

A typical NIMZ will be of at least 5,000 hectares in size and will be chosen by the state governments from its own land or through acquisitions. The preference will be for non-agricultural land with adequate water supply. If needed, the states may reserve a certain share of the land for MSMEs.

Ownership of an NIMZ will either be with the state government, a state government undertaking in joint ownership with a private partner or under any other appropriate model.

Wasteland, as far as possible will be acquired and agricultural land will be kept to minimum. It should not be in ecologically sensitive area.

SPV: The administrative structure of an NIMZ will include four entities, namely an SPV, a developer, the state government and the central government. After the central government notifies an NIMZ in the official gazette, an SPV will be constituted to exercise the powers, discharge the functions and manage the affairs of the NIMZ. This SPV can be a company, including a Section 25 company, depending upon the MoU between stakeholders.

The appropriate financial and administrative structure of the SPV will depend on the financial participation of different stakeholders who will also have their nominees on the board of the SPV. However, the CEO of the SPV will be a senior central or state government official. The SPV will include an official/expert conversant with the work relating to pollution control/environmental protection. There will also be representation to the industrial units functioning in NIMZs. The main functions of the SPV will include master planning of the zone, preparation of a development strategy and an action plan for self-regulation to serve the purpose of the policy, formulation of rules and procedures for development, operation, regulation and management of NIMZs and their enforcement.

The SPV will also expedite environmental clearance and clearances under the air and water Acts, work out an arrangements with the state government regarding revenue streams including the levy of user or service charges or fees or rent for the use of infrastructure/properties in NIMZs and the creation of specific mechanisms for specialised services.

The SPV can take up the development work on its own through various agencies/contractors or take up the development in partnership with a developer who shall be selected through a transparent process.

Labour advantages: NIMZs will put in place a comprehensive exit policy that will promote productivity while providing flexibility by reducing some of the moving rigidities in the labour market and by ensuring protection of workers' rights as laid down in the statute.

An exit policy will be worked out, keeping in view the provisions for the protection of workers' rights within the statutory framework. Firms operating in NIMZs will have a job-loss policy to insure workers against loss of employment in the event of closure or retrenchment. This policy will be used to make compensation payment to workers at the time of closure or right sizing. The SPV can also opt for a sinking fund mechanism, instead of a job-loss policy, to be funded by contributions to provide compensation to workers. Or both can operate in combination.

Similarly, the SPV will help redeploy labour from one unit to another in case of closures. This redeployment shall be from the date of closure at the same remuneration and on the same terms as before.

Under Section 25FFF of the Industrial Disputes Act there is a mandatory requirement to pay compensation equivalent to fifteen days' average pay for every completed year of continuous service, or any part thereof in excess of six months. NMP makes it 20 days.

By July 2013, Centre has already given in principal approval for 12 NIMZs.
AP has been granted another National Investment Manufacturing Zone (NIMZ) near Ongole in Prakasam district. This will be in addition to the two NIMZs already cleared in principle by the central government in Medak and Chittoor districts. The zones will be developed as integrated industrial townships with state-of-the-art infrastructure, clean and energy-efficient technology and skill development facilities. Andhra Pradesh would be the second state after Maharashtra to have more than two NIMZs. Japan, Germany, the UK, Russia and China have shown keen interest in investing in these NIMZs.

SEZs
According to SEZ Act 2005, a Special Economic Zone can be established either jointly or severally by the Central Government, State Government, or any other person involve in the manufacturing of goods. Even a foreign company can also set up SEZ in India.

In addition to Seven Central Government Special Economic Zones (SEZs) and 12 State/Private Sector SEZs set up prior to the enactment of SEZ Act, 2005, formal approval has been accorded to 574 proposals out of which 391 SEZs presently stand notified. A total of 175 SEZs have commenced export.

As per Entry No. 18 of the State List in the 7th Schedule to the Constitution of India, land is a State subject. The approval for setting up of a SEZ is given on the recommendations of the State Government. Issues related to availability/provisioning of land for SEZs are in the domain of the State Government concerned. SEZ units are under an obligation to achieve positive Net Foreign Exchange (NFE) earnings to be calculated cumulatively for a period of 5 years from the commencement of production.

Golden Quadrilateral

The **Golden Quadrilateral** is a highway network connecting many of the major industrial, agricultural and cultural centres of India. A quadrilateral of sorts is formed by connecting Delhi, Mumbai, Kolkata and Chennai, and hence its name. Other cities among the top metropolises namely Pune, Ahmedabad, Jaipur,Kanpur, Surat at north and Bengaluru, Visakhapatnam & Bhubaneswar at south are also connected by the network.

The largest highway project in India and the fifth longest in the world it is the first phase of the National Highways Development Project (NHDP), and consists of building 5,846 km (3,633 mi) four/six lane express highways at a cost of ₹600 billion (US$9.6 billion). The project was launched in 2001 by Atal Bihari Vajpayee and was planned to complete in January, 2012.

The GQ project is managed by the National Highways Authority of India (NHAI) under the Ministry of Road, Transport and Highways. The Mumbai-Pune Expressway, the first controlled-access toll road to be built in India is a part of the GQ Project though not funded by NHAI.

North-South–East-West Corridor

The **North-South–East-West Corridor** (NS-EW) is the largest ongoing highway project in India. It is the second phase of the National Highways Development Project (NHDP), and consists of building 7300 kilometers of four/six lane expressways connecting Srinagar, Kanyakumari, Porbandar and Silchar, at a cost of US$12.317 billion (at 1999 prices). As of January 2012, 5945 of 7300 kilometers project has been completed.

In combination with India's Golden Quadrilateral, and port connectivity highways, NS-EW Corridor forms a key part of Indian highway network connecting many of its important manufacturing, commerce and cultural centers. As of May 2012, India has completed and placed in use 15800 kilometers of such 4-lane highways.

The NS–EW project is managed by the National Highways Authority of India under the Ministry of Road, Transport and Highways.

Pradhan Mantri Gram Sadak Yojana

The **Pradhan Mantri Gram Sadak Yojana** or **PMGSY** is a nationwide plan in India to provide good all-weather road connectivity to unconnected villages.

This Centrally Sponsored Scheme was introduced in 2000 by the then Prime Minister Of India Shri Atal Bihari Vajpayee.

It is under the authority of the Ministry of Rural Development. It is fully funded by the central government.

The goal was to provide roads to all villages with a population of 1000 persons and above by 2003, with a population of 500 persons and above by 2007, in hill states, tribal and desert area villages with a population of 500 persons and above by 2003, and in hill states, tribal and desert area villages with a population of 250 persons and above by 2007.

Social Responsibility

Social responsibility is an ethical theory that an entity, be it an organization or individual, has an obligation to act to benefit society at large. Social responsibility is a duty every individual has to perform so as to maintain a balance between the economy and the ecosystem. A trade-off always exists between economic development, in the material sense, and the welfare of the society and environment. Social responsibility means sustaining the equilibrium between the two. It pertains not only to business organizations but also to everyone whose any action impacts the environment. This responsibility can be passive, by avoiding engaging in socially harmful acts, or active, by performing activities that directly advance social goals.

Critics argue that Corporate social responsibility (CSR) distracts from the fundamental economic role of businesses; others argue that it is nothing more than superficial window-dressing; others argue that it is an attempt to pre-empt the role of governments as a watchdog over powerful corporations though there is no systematic evidence to support these criticisms.

Corporate governance

Corporate governance refers to the system by which corporations are directed and controlled. The governance structure specifies the distribution of rights and responsibilities among different participants in the corporation (such as the board of directors, managers, shareholders, creditors, auditors, regulators, and other stakeholders) and specifies the rules and procedures for making decisions in corporate affairs. Governance provides the structure through which corporations set and pursue their objectives, while reflecting the context of the social, regulatory and market environment. Governance is a mechanism for monitoring the actions, policies and decisions of corporations. Governance involves the alignment of interests among the stakeholders.

There has been renewed interest in the corporate governance practices of modern corporations, particularly in relation to accountability, since the high-profile collapses of a number of large corporations during 2001–2002, most of which involved accounting fraud. Corporate scandals of various kinds surface often having violated public interest

Corporate governance is based on principles such as conducting the business with all integrity and fairness, being transparent with regard to all transactions, making all the necessary disclosures and decisions, complying with all the laws of the land, accountability and responsibility towards the stakeholders and commitment to conducting business in an ethical manner. Another point which is highlighted in the SEBI report on corporate governance is the need for those in control to be able to distinguish between what are personal and corporate funds while managing a company.

Fundamentally, there is a level of confidence that is associated with a company that is known to have good corporate governance. The presence of an active group of independent directors on the board contributes a great deal towards ensuring confidence in the market. Corporate governance is known to be one of the criteria that foreign institutional investors are increasingly depending on when deciding on which companies to invest in. It is also known to have a positive influence on the share price of the company. Having a clean image on the corporate governance front could also make it easier for companies to source capital at more

reasonable costs. Unfortunately, corporate governance often becomes the centre of discussion only after the exposure of a large scam.

Companies Act 2013

Companies Bill 2013 received assent from President Pranab Mukherjee in August 2013.The new bill, providing for sweeping changes in the way companies operate and are regulated in the country, received Parliamentary approval in August 2013. It will replace the Companies Act 1956.

Highlights:

Certain class of companies should have at least one women director on board. This is an interesting move as it makes mandatory for company boards to have a woman representative, something that will give a greater representation to women in corporate decision-making.
National Company Law tribunal: Separate tribunal to deal with disputes such as winding up amalgamations, rehabilitation, reduction of share.

Employee Protection in Failed Companies: Must pay 2 yrs' salary on winding up of ops. Rights of workers to supersede those of secured creditors

One-Person Company: An individual can set up a 1 person company (Read ahead)

Class Action Suits: Members or depositors can file class action suits. It lays down a stringent regime for those accepting deposits from public, protection for whistleblowers. (Read ahead)

Statuary recognition to the Serious Fraud Investigation Office.

It will have powers to arrest offenders.
Once SFIO begins to investigate a case no other agency can be involved. Listed cos must have at least one-third independent directors.

An independent director cannot hold more than two consecutive terms of 5 yrs each Auditors to be appointed for 5 yrs, to be approved every year.
A person can audit a maximum of 20 companies.

Auditors can face imprisonment up to one year for violating relevant provisions and pay damages for incorrect or misleading statements.

Companies have to spend at least 2% of its average net profit during three preceding years on Corporate Social Responsibility (CSR) activities.

Amount has to be preferably spend near or around the areas the company operates.

Class action Suit

The first time class action suit came to the spotlight in the context of securities market was when the Satyam scam broke out in 2009. At that time, many small investors in India could not take any legal recourse against the software services firm's management while their counterparts abroad filed class action suit claiming damages.
Thanks to the Satyam scam, India has introduced class action suit in the new Companies Act 2013.

A 'class action suit' may be defined as a lawsuit in which a group of shareholders of a company collectively bring an action in court against an identified group of defendants belonging to the company. The Companies Act mandates the initiation of class actions suits by the members and depositors of a company in case they are of the opinion that the management or conduct of the affairs of the company are being done in a manner prejudicial to the interests of the company or its members or depositors. Under the Companies Act, class action suits can be commenced collectively by a minimum of 100 shareholders or depositors, or a minimum prescribed percentage of such shareholders or depositors, whichever is less. A class action suit may be brought against the company, its directors, auditors or any experts, advisors and consultants for their inactions and wrongdoings. Hence, the Companies Bill attempts to cast a wide net on the erring management of the company. Upon admission of a class action application, all similar applications in any jurisdiction are required to be consolidated into one single application. This provision would reduce multiplicity of litigation on the same subject matter.

The features of a class action suit under the Companies Bill certainly carry benefits for investors of a company. It provides investors with a medium to fight as one unit against the errant company or management, thereby reducing multiplicity of suits, costs of ligation and increasing their chances of success in the process. No doubt, 'class action suits' under the Companies Bill may prove to be a potent tool to keep the accountability of a company/management in check and to contain any likely prejudice against the minority. However, on the flipside, such a concept may be open to misuse by unscrupulous minority shareholders in furtherance of their vested interest thereby hampering the efficacious functioning of the company.

Class action suits have to be filed before the National Company Law Tribunal first, but banking companies are excluded from such action.

CSR

The new law would require companies that meet certain set of criteria, to spend at least two percent of their average profits in the last three years towards Corporate Social Responsibility (CSR) activities. But only companies reporting Rs 5 crore or more profits in the last three years have to make the CSR spend. The Act allows companies the freedom to choose areas of work for CSR and the mandate of a rotation in auditors every 5 years gives the process added credibility. In case, entities are unable to comply with the CSR rules, they would be needed to give explanations. Otherwise, they would face action, including penalty.

One person company

Till recently, law mandated a minimum of two shareholders to start a company. Now, Companies Act opened the doors for the entrepreneur looking to set up a company all by himself. This has been made possible by bringing in the concept of One Person Company (OPC). A one person company is a paradigm shift in the Indian corporate regime, bringing it at par with global standards and will provide a significant fillip to micro and small-scale businesses.

CSR

Corporate social responsibility (CSR) is a management concept whereby companies integrate social and environmental concerns in their business operations and interactions with their stakeholders. CSR is generally understood as being the way through which a company achieves a balance of economic, environmental and social imperatives ("Triple-Bottom-Line-

People, Planet & Profit

Furtherance → The advancement of plan/interest

Scrupulous → Very careful and thorough

Money laundering

Approach"), while at the same time addressing the expectations of shareholders and stakeholders. In this sense it is important to draw a distinction between CSR, which can be a strategic business management concept, and charity, sponsorships or philanthropy. Even though the latter can also make a valuable contribution to poverty reduction, will directly enhance the reputation of a company and strengthen its brand, the concept of CSR clearly goes beyond that.

CSR programme follows the Triple Bottom Line (TBL) Approach to meet social and environmental standards without compromising their competitiveness. The TBL approach is used as a framework for measuring and reporting corporate performance against economic, social and environmental performance. It is an attempt to align private enterprises to the goal of sustainable global development by providing them with a more comprehensive set of working objectives than just profit alone. The perspective taken is that for an organization to be sustainable, it must be financially secure, minimize (or ideally eliminate) its negative environmental impacts and act in conformity with societal expectations.

Key CSR issues: environmental management, eco-efficiency, responsible sourcing, stakeholder engagement, labour standards and working conditions, employee and community relations, social equity, gender balance, human rights, good governance, and anti-corruption measures.

A properly implemented CSR concept can bring along a variety of competitive advantages, such as enhanced access to capital and markets, increased sales and profits, operational cost savings, improved productivity and quality, efficient human resource base, improved brand image and reputation, enhanced customer loyalty, better decision making and risk management processes.

The term "corporate social responsibility" came into common use in the late 1960s and early 1970s after many multinational corporations formed the term stakeholder, meaning those on whom an organization's activities have an impact. Proponents argue that corporations make more long term profits by operating with a perspective, while critics argue that CSR distracts from the economic role of businesses.

Development business ethics is one of the forms of applied ethics that examines ethical principles and moral or ethical problems that can arise in a business environment. One of its focal areas is CSR.

ISO 26000 is the recognized international standard for CSR. Public sector organizations (the United Nations for example) adhere to the triple bottom line (TBL). It is widely accepted that CSR adheres to similar principles but with no formal act of legislation. The UN has developed the Principles for Responsible Investment as guidelines for investing entities.

A more common approach to CSR is corporate philanthropy. This includes monetary donations and aid given to local and non-local nonprofit organizations and communities, including donations in areas such as the arts, education, housing, health, social welfare, and the environment, among others, but excluding political contributions and commercial sponsorship of events. Some organizations do not like a philanthropy-based approach as it might not help build on the skills of local populations, whereas community-based development generally leads to more sustainable development.

Another approach to CSR is to incorporate the CSR strategy directly into the business strategy of an organization. For instance, procurement of Fair Trade tea and coffee has been adopted by various businesses including KPMG. Fair trade is an organized social movement that aims to help producers in developing countries. It advocates the payment of a higher price to exporters as well as higher social and environmental standards. It focuses in particular on exports from developing countries to developed countries, most notably handicrafts, coffee, cocoa, sugar, tea, bananas, honey, cotton, wine, fresh fruit, chocolate, flowers, and gold.

Adept → very skilled and effective

Another approach is Creating Shared Value, or CSV. The shared value model is based on the idea that corporate success and social welfare are interdependent. A business needs a healthy, educated workforce, sustainable resources and adept government to compete effectively. For society to thrive, profitable and competitive businesses must be developed and supported to create income, wealth, tax revenues, and opportunities for philanthropy. CSV acknowledges trade-offs between short-term profitability and social or environmental goals, but focuses more on the opportunities for competitive advantage from building a social value proposition into corporate strategy.

Social accounting

It is the process of communicating the social and environmental effects of organizations' economic actions to particular interest groups within society and to society at large. Social accounting is commonly used in the context of business, or corporate social responsibility (CSR), although any organisation, including NGOs, charities, and government agencies may engage in social accounting.

Social accounting broadens the notion of corporate accountability. Environmental accounting may specifically refer to the research or practice of accounting for an organisation's impact on the natural environment. Social accounting challenges conventional accounting, in particular financial accounting, for giving a narrow image of the interaction between society and organizations. Social accounting, a largely normative concept, seeks to broaden the scope of accounting in the sense that it should:

- Concern itself with more than only economic events;
- Not be exclusively expressed in financial terms;
- Be accountable to a broader group of stakeholders;
- Broaden its purpose beyond reporting financial success.

It points to the fact that companies influence their external environment (some times positively and many a times negatively) through their actions and should therefore account for these effects as part of their standard accounting practices. Social accounting is in this sense closely related to the economic concept of externality.

"Social license" generally refers to a local community's acceptance or approval of a company's project or ongoing presence in an area. It is increasingly recognized by various stakeholders and communities as a prerequisite to development. The development of social license occurs outside of formal permitting or regulatory processes, and requires sustained investment by proponents to acquire and maintain social capital within the context of trust-based relationships. Often intangible and informal, social license can nevertheless be realized through a robust suite of actions centered on timely and effective communication, meaningful dialogue, and ethical and responsible behavior.

normative → Establishing a norm

Local conditions, needs, and customs vary considerably and are often opaque, but have a significant impact on the likely success of various approaches to building social capital and trust. These regional and cultural differences demand a flexible and responsive approach and must be understood early in order to enable the development and implementation of an effective strategy to earn and maintain social license. Governments could facilitate the necessary stakeholder mapping in regions for which they are responsible and provide a regulatory framework that sets companies on the right path for engagement with communities and stakeholders.

Exhort
strongly urge
to do something

The scale and nature of the benefits of CSR for an organization can vary depending on the nature of the enterprise, and are difficult to quantify, though there is a large body of literature exhorting business to adopt measures beyond financial ones. Evidence shows a correlation between social/environmental performance and financial performance. However, businesses may not be looking at short-run financial returns when developing their CSR strategy. Intel employs a 5-year CSR planning cycle.

Triple bottom line

People, planet and profit approach is also known as the triple bottom line. People relates to fair and beneficial business practices toward labour, the community and region where corporation conducts its business. Planet refers to sustainable environmental practices. A triple bottom line company does not produce harmful or destructive products such as weapons, toxic chemicals or batteries containing dangerous heavy metals for example. Profit is the economic value created by the organization after deducting the cost of all inputs.

Critics

Milton Friedman and others have argued that a corporation's purpose is to maximize returns to its shareholders, and that since only people can have social responsibilities, corporations are only responsible to their shareholders and not to society as a whole. Although they accept that corporations should obey the laws of the countries within which they work, they assert that corporations have no other obligation to society. Some people perceive CSR as incongruent with the very nature and purpose of business, and indeed a hindrance to free trade. Those who assert that CSR is contrasting with capitalism and are in favor of the free market argue that improvements in health, longevity and/or infant mortality have been created by economic growth attributed to free enterprise.

Critics of this argument perceive the free market has to be inclusive as a part of its own enlightened self interest.

Many religious and cultural traditions hold that the economy exists to serve human beings, so all economic entities have an obligation to society .CSR proponents point out that CSR can significantly improve long-term corporate profitability because it reduces risks and inefficiencies.

Some critics believe that CSR programs are undertaken by companies such as British American Tobacco (BAT), the petroleum giant BP (well known for its high-profile advertising campaigns on environmental aspects of its operations), and McDonald's to distract the public from ethical questions posed by their core operations. They argue that some corporations start CSR programs for the commercial benefit they enjoy through raising their reputation with the public or with government.

Another concern is that sometimes companies claim to promote CSR and be committed to sustainable development but simultaneously engage in harmful business practices.

Ethical consumerism

The rise in popularity of ethical consumerism over the last two decades can be linked to the rise of CSR. As global population increases, so does the pressure on limited natural resources required to meet rising consumer demand . Industrialization, in many developing countries, is booming as a result of both technology and globalization. Consumers are becoming more aware of the environmental and social implications of their day-to-day consumer decisions and are therefore beginning to make purchasing decisions related to their environmental and ethical concerns. However, this practice is far from consistent or universal.

Globalization and market forces

As corporations pursue growth through globalization, they have encountered new challenges that impose limits to their growth and potential profits. Government regulations, tariffs, environmental restrictions and varying standards of what constitutes "labor exploitation" are problems that can cost organizations millions of dollars. Some view ethical issues as simply a costly hindrance, while some companies use CSR methodologies as a strategic tactic to gain public support for their presence in global markets, helping them sustain a competitive advantage by using their social contributions to provide a subtle level of advertising. Global competition places a particular pressure on multinational corporations to examine not only their own labor practices, but those of their entire supply chain, from a CSR perspective.

Social awareness and education

The role among corporate stakeholders is to work collectively to pressure corporations that are changing. Shareholders and investors themselves, through socially responsible investing (SRI) are exerting pressure on corporations to behave responsibly. The extension of SRI bodies driving corporations to include an element of 'ethical investment' into their corporate agenda's generates socially embedded issues. The main issue correlates to the development and overall idea of 'ethical investing' or SRI. The Non-governmental organizations are taking an increasing role, leveraging the power of the media and the Internet to increase their scrutiny and collective activism around corporate behavior. Through education and dialogue, the development of community awareness in holding businesses responsible for their actions is growing.

Public policies

CSR has inspired national governments to include CSR issues into their national public policy agendas. The increased importance driven by CSR, has prompted governments to promote socially and environmentally responsible corporate practices. Over the past decade governments have considered CSR as a public issue that requires national governmental involvement to address the very issues relevant to CSR. The heightened role of government in CSR has facilitated the development of numerous CSR programs and policies.A key debate in CSR is determining what actors are responsible to ensure that corporation's are behaving in a socio-economic and environmentally sustainable manner.

Some Indian examples

Coca-Cola's 'Support My School', Aircel's 'Save Our Tigers' or Tata Tea's "Jaago re'. Jaago re campaign showed simple aspects of our daily life, highlighted how we have forgotten our basic duties as citizens of India, and urged the audience to 'wake up'. In 2013,

NDTV and Vedanta announced the launch of their unique initiative 'NDTV Vedanta Our Girls Our Pride', a first of its kind national movement to create awareness about issues related to the girl child.

To mark its silver jubilee, Tata Tea has unveiled a new television commercial (TVC), Soch Badlo, to salute women for being the agents of change in the society.

The TVC starts on a cynical note, with a husband, who has just finished reading the day's newspaper, telling his wife that he is fed up of reading about scams every day. As he walks over to the kitchen and asks her to make him a cup of tea, she urges him to look at the water boiling in the vessel on the gas oven. She uses the turmoil in the vessel as a metaphor for the kerfuffle that precedes change in society. Just like you get a wonderful cup of tea when you pour tea leaves into boiling water, the mayhem in the country is just an indication that things can only turn for the better, she explains.

The company says "Soch Badlo" is an extension of the highly successful 2007 "Jaago Re" campaign.

Why do companies engage in corporate social responsibility?

At least 120 were killed when a *fire* broke out in a *garment factory* outside Dhaka, *Bangladesh's* capital in November 2012. In mid-2013, the collapse of the Rana Plaza factory in Bangladesh exposed the unsafe working conditions that garment workers endure across the developing world. The tragedy also revealed the inconsistencies of some companies with respect to corporate social responsibility (CSR).

Take the case of Walmart. A month after the disaster, it refused to sign on to the safety measures adopted by more than a dozen European firms. Those companies, including Marks & Spencer, backed a plan in which they agreed to have rigorous, independent inspections of the factories they contract with in Bangladesh and to help pay for improvements in building safety.

Walmart, along with other retailers and the main retail federations, are forging their own plan to promote safety in Bangladesh's apparel industry. This effort will seek to "develop and implement a new program to improve fire and safety regulations in the garment factories of Bangladesh."

Despite their high-profile -- and widely criticized -- resistance to the originally proposed safety measures, Walmart and Gap would no doubt be quick to cite their initiatives in other areas: Gap is often considered an industry leader in CSR, and both companies have proclaimed themselves as champions of efforts promoting women.

Two years ago in 2011, Walmart launched its Global Women's Economic Empowerment Initiative, which doubled the money the firm spends on women-owned businesses and provides women around the world with job training and access to education. Gap has instituted PACE (Personal Advancement & Career Enhancement), a program to help female garment workers in developing countries advance beyond entry-level positions.

To some, the companies' rejection of the European plan -- while also touting these kinds of social programs -- appears contradictory, even hypocritical. A cynical view might be that when firms trumpet their efforts to produce organic foods, sell fair-trade T-shirts or just make the world a better place, they are diverting attention away from the more unseemly elements

of their business strategies -- such as polluting the air, manufacturing goods in unsafe factories or exploiting workers with low wages. For people who see companies doing one thing with their right hand and doing another thing with the left, the question is: What is your more moral calculus?

There are some serious arguments in favor of compelling firms to abide by the standards of CSR. They are particularly relevant in the context of weak countries where even rudimentary regulatory standards might not exist or be enforced, or where such basic regulation might be subverted by corruption. It is certainly possible that industrial operations in weak or corrupt states can produce what economists call negative externalities—air pollution, water contamination, human-rights abuses—and that the need for CSR is self-evident.

CSR in Companies Act 2013

The provision related to Corporate Social Responsibility under present Clause 135 of Companies Bill 2012 applies to all companies; listed, unlisted, public, private, one – person subject to limitation based on its net worth, turnover and net profit. These threshold limits are:

1. Net worth rupees five hundred crore or more (500 crore)
2. Turnover rupees one thousand crore or more (1000 crore)
3. Net Profit rupees five crore of more (5 crore)

There is a requirement of constitution of Corporate Social Responsibility Committee of the Board of Directors consisting of three or more directors. There must be at least one independent director in the board irrespective of nature of constitution of company; public or private. In the report of the Board of Directors under Section 134 (4) shall disclose composition of this CSR Committee.

The mandate of this committee shall be:

1. Formulate and recommend a corporate social responsibility policy
2. Recommend amount to spend
3. Monitor this CSR policy

The Government lists out government directive on this programme under Schedule VII of the Bill. Corporate Social Responsibility activities may include:—

(i) Eradicating extreme hunger and poverty;
(ii) Promotion of education;
(iii) Promoting gender equality and empowering women;
(iv) Reducing child mortality and improving maternal health;
(v) Combating human immunodeficiency virus, acquired immune deficiency syndrome, malaria and other diseases;
(vi) Ensuring environmental sustainability;
(vii) Employment enhancing vocational skills;
(viii) Social business projects;
(ix) Contribution to the prime minister's national relief fund or any other fund set up by the central government or the state governments for socio-economic development and relief and funds for the welfare of the scheduled castes, the scheduled tribes, other backward classes, minorities and women; and
(x) Such other matters as may be prescribed.

The Board has duty to approve corporate social responsibility policy. This corporate social responsibility policy is public document and required to disclose in (i) Board's Report, (ii) company website in prescribed manner. This is duty of board to make sure that the activities

as are included in Corporate Social Responsibility Policy of the company are undertaken by the company.

The Board *shall ensure* that the company spends, in every financial year, at least two per cent of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy. Second proviso to relevant sub – section 5 gives some relief, if the company fails to spend such amount, the Board shall, in its report made under clause (o) of sub-section (3) of section 134, specify the reasons for not spending the amount.

The company shall give preference to the local area and areas around it where it operates, for spending the amount earmarked for Corporate Social Responsibility activities.

CSR directives in the Companies Bill or otherwise are in accordance with Directive Principle of State Policy enumerated by Constitution of India.

Before the Companies Bill was passed, CSR was in the nature of voluntary actions that businesses could take. It was like going the extra mile. But the provisions of the Bill, particularly Section 135, read with Schedule VII, show that the Government has adopted an inclusive growth strategy to implement CSR through corporates.

The intention of the Bill is to eradicate extreme hunger and poverty, promote education, enhance vocational skills and empower women.

The need for CSR has its roots in the fundamental moral thought — "what and how much has been given back over and above what you have taken from society."

Section 135 of the Companies Bill provides that "the functions of the CSR committee shall be to formulate and recommend a CSR Policy which shall indicate the activities to be undertaken by the company as specified in Schedule VII of the Bill.The CSR committee shall also deliberate on the amount to be incurred on activities mentioned in the CSR Policy. It shall also monitor the CSR Policy from time to time.

The company's board, after receiving the panel's recommendations, will adopt a CSR Policy and ensure that the activities it mandates are undertaken.

The company shall not select a project that earns profit for the company, but rather take on work that benefits society.

The right to fair compensation and transparency in land acquisition, rehabilitation and resettlement Act 2013

What is the significance of the new title 'The right to fair compensation and transparency in land acquisition, rehabilitation and resettlement Act 2013'?

The title of the old law conveyed that its primary purpose was to expedite the acquisition of land. However, the principle objective of the new Bill is fair compensation, thorough resettlement and rehabilitation of those affected, adequate safeguards for their well-being and complete transparency in the process of land acquisition. The title has been amended to reflect this.

Why is there a need for a new Act?

There is unanimity of opinion across the social and political spectrum that the current Law (The Land Acquisition Act 1894) suffers from various shortcomings. Some of these include:

- Forced acquisitions: Under the 1894 legislation once the acquiring authority has formed the intention to acquire a particular plot of land, it can carry out the acquisition regardless of how the person whose land is sought to be acquired is affected.
- No safeguards: There is no real appeal mechanism to stop the process of the acquisition. A hearing (under section 5A) is prescribed but this is not a discussion or negotiation. The views expressed are not required to be taken on board by the officer conducting the hearing.
- Silent on resettlement and rehabilitation of those displaced: There are absolutely no provisions in the 1894 law relating to the resettlement and rehabilitation of those displaced by the acquisition.
- Urgency clause: This is the most criticised section of the Law. The clause never truly defines what constitutes an urgent need and leaves it to the discretion of the acquiring authority. As a result almost all acquisitions under the Act invoke the urgency clause. This results in the complete dispossession of the land without even the token satisfaction of the processes listed under the Act.
- Low rates of compensation: The rates paid for the land acquired are the prevailing circle rates in the area which are notorious for being outdated and hence not even remotely indicative of the actual rates prevailing in the area.
- Litigation: Even where acquisition has been carried out the same has been challenged in litigations on the grounds mentioned above. This results in the stalling of legitimate infrastructure projects.
- Recent observations by the Supreme Court: Justice Ganpat Singhvi of the Supreme Court has observed, in the wake of repeated violations that have come to light over the last few months, that the law has "become a fraud". He observed that the law seems to have been drafted with "scant regard for the welfare of the common man".
- Another bench of the Supreme Court has echoed this sentiment in its observation that "the provisions contained in the Act, of late, have been felt by all concerned, do not adequately protect the interest of the land owners/persons interested in the land. The Act does not provide for rehabilitation of persons displaced from their land although by such compulsory acquisition, their livelihood gets affected ...To say the least, the Act has become outdated and needs to be replaced at the earliest by fair, reasonable and rational enactment in tune with the constitutional provisions, particularly, Article 300A of the Constitution. We expect the law making process for a comprehensive enactment with regard to acquisition of land being completed without any unnecessary delay."

Why does the government need to acquire land for private companies as well as public-private partnership projects?

- Land Records in most parts of the country are fragmented and disorganised. In most cases they haven't been updated for decades. The new law overcomes that by ensuring the Collector updates the land records and also pays up to four times the value to correct any inaccuracies.
- If land is purchased then there are no benefits for livelihood losers who are usually far greater in number than the land owners. This Bill ensures that they are taken care of and not simply displaced.
- The inequality in terms of bargaining power between large-scale corporations and small farmers and other marginalised groups increases the likelihood of unfair agreements. Contracts tend to be signed in favour of the party negotiating from a greater position of strength. That is why government is required to bridge the gap and bring balance to this relationship.
- A legitimate need for acquisition by the state itself (to build public goods such as roads, schools and hospitals) can be undermined and stalled by groups with vested interests. If there is no sovereign power to compel these groups, a single individual or group of individuals can hold a process hostage merely by refusing to part with land. Further, in times of crisis such as war, famine and floods, coupled with absence of legislation clarifying and guiding the state's exercise of 'eminent domain', situations can emerge jeopardising human lives.

What are the highlights of the new Act?

- Compensation: Given the inaccurate nature of circle rates, the Bill proposes the payment of compensations that are up to four times the market value in rural areas and twice the market value in urban areas.
- R&R: This is the very first law that links land acquisition and the accompanying obligations for resettlement and rehabilitation. Over five chapters and two entire Schedules have been dedicated to outlining elaborate processes (and entitlements) for resettlement and rehabilitation. The Second Schedule in particular outlines the benefits (such as land for land, housing, employment and annuities) that shall accrue in addition to the one-time cash payments.
- Retrospective operation: To address historical injustice the Bill applies retrospectively to cases where no land acquisition award has been made. Also in cases where the land was acquired five years ago but no compensation has been paid or no possession has taken place then the land acquisition process will be started afresh in accordance with the provisions of this act.
- Multiple checks and balances: A 'comprehensive, participative and meaningful' process (involving the participation of local Panchayati Raj institutions) has been put in place prior to the start of any acquisition proceeding. Monitoring committees at the national and state levels to ensure that R&R obligations are met have also been established.
- Special safeguards for tribal communities and other disadvantaged groups: No land can be acquired in scheduled areas without the consent of the Gram Sabhas. The law also ensures that all rights guaranteed under such legislation as the Panchayat (Extension to Scheduled Areas) Act 1996 and the Forest Rights Act 2006 are taken care of. It has special enhanced benefits (outlined in a dedicated chapter) for those belonging to Scheduled Castes and Scheduled Tribes.
- Safeguards against displacement: The law provides that no one shall be dispossessed until and unless all payments are made and alternative sites for the resettlement and

rehabilitation have been prepared. The Third Schedule even lists the infrastructural amenities that have to be provided to those that have been displaced.

- Compensation for livelihood losers: In addition to those losing land, the Bill provides compensation to those who are dependent on the land being acquired for their livelihood.
- Consent: In cases where PPP projects are involved or acquisition is taking place for private companies, the Bill requires the consent of no less than 70% and 80% respectively (in both cases) of those whose land is sought to be acquired. This ensures that no forcible acquisition can take place.
- Caps on acquisition of multi-crop and agricultural land: To safeguard food security and to prevent arbitrary acquisition, the Bill directs states to impose limits on the area under agricultural cultivation that can be acquired.
- Return of unutilized land: In case land remains unutilized after acquisition, the new Bill empowers states to return the land either to the owner or to the State Land Bank.
- Exemption from income tax and stamp duty: No income tax shall be levied and no stamp duty shall be charged on any amount that accrues to an individual as a result of the provisions of the new law.
- Share in appreciated land value: Where the acquired land is sold to a third party for a higher price, 40% of the appreciated land value (or profit) will be shared with the original owners.

How are interests and concerns of farmers protected?

- Retrospective effect: Where awards are made but no compensation has been paid or possession has not been taken, compensation shall be paid at the rate prescribed under the new Act. Where the Award has not been made the entire process shall be considered to have lapsed. Also where acquisition has taken place five years prior to the commencement of the new law but no compensation/ possession has taken place the proceedings shall be deemed to have lapsed.
- Consent: Prior-consent shall be required from 70% of land losers and those working on government assigned lands only in the case of public-private partnership projects and 80% in the case of private companies. This consent also includes consent to the amount of compensation that shall be paid.
- Return of unutilized land: Land not used can now be returned to the original owners if the state so decides.
- Share in sale of acquired land increased: The share that has to be distributed among farmers in the increased land value (when the acquired land is sold off to another party) has been set at 40%.
- Income-tax Exemption: All amounts accruing under this act have been exempted from income tax and from stamp duty.
- Strict restrictions on multi-crop acquisition: The acquisition of agricultural land and multi-crop land has to be carried out as a last resort. There will be definite restrictions on the extent of acquisition of such land in every state to be determined by the States concerned.
- Safeguards to ensure fair price: Given the way in which market value is to be calculated and the imposition of a solatium of 100% over and above the amount, the farmers are guaranteed a fair price for their land.
- Acquisition only if necessary: The Collector has to make sure that no other unutilized lands are available before he moves to acquire farm land.
- Damage to crops to be included in price: The final award has to include damage to any standing crops which might have been harmed due to the process of acquisition (including the preliminary inspection).

- Share in developed land: In case their land is acquired for urbanization purposes 20% of the developed land will be reserved and offered to these farmers in proportion to the area of their land acquired and at a price equal to the cost of acquisition and the cost of development.
- Fishing rights: In the case of irrigation or hydel projects, affected families may be allowed fishing rights in the reservoirs.
- Additional R&R benefits: Farmers are also entitled to the various rehabilitation and resettlement benefits which are enumerated in response to question 2.
- Time-bound social impact assessment: The Bill mandates a social impact assessment of every project which must be completed within a period of six months.

What are the rehabilitation and resettlement provisions for farmers, landless and livelihood losers?

- Reduced qualifying criteria: To qualify for benefits under this Act the time period has been reduced to three years of dependence (on the acquired land) from five.
- Affected family to include tenants: The definition of affected family includes agricultural labourers, tenants including any form of tenancy or usufruct right, share-croppers or artisans who may be working in the affected area for three years prior to the acquisition, whose primary source of livelihood stands affected by the acquisition of land.
- Houses for all affected families: All affected families are entitled to a house provided they have been residing in an area for five years or more and have been displaced. If they choose not to accept the house they are offered a one-time financial grant in lieu of the same.
- Choice of annuity or employment: All affected families are given a choice of annuity or employment;
  (i) If employment is not forthcoming they are entitled to a one-time grant of Rs.5 lakh per family.
  (ii) Alternatively they will provided with an annuity payment of Rs.2,000 per month per family for 20 years (this will be adjusted for inflation).
- Subsistence allowance: All affected families which are displaced from the land acquired shall be given a monthly subsistence allowance equivalent to Rs.3,000 per month for a period of one year from the date of award.
- Training and skill development: All affected families are also given training and skill development while being offered employment.
- Miscellaneous amounts: All affected families are given multiple monetary benefits such as transport allowance of Rs.50,000 and resettlement allowance of Rs.50,000.
- One-time financial assistance: Each affected family of an artisan, small trader or self-employed person shall get one-time financial assistance of such amount as the appropriate government may, by notification, specify subject to a minimum of Rs.25,000.
- R&R to be completed in all aspects for irrigation projects: In case of acquisition of land for irrigation or hydel project the rehabilitation and resettlement shall be completed six months prior to submergence of the lands proposed to be so acquired.
- Possession upon fulfilment of conditions under Act: The Collector shall take possession of land only ensuring that full payment of compensation as well as rehabilitation and resettlement entitlements are paid or tendered to the entitled persons within a period of three months for the compensation and a period of six months for the monetary part of rehabilitation and resettlement entitlements commencing from the date of the award. However, families will not be displaced from this land till their alternative R&R sites are ready for occupation.

- Time Limit for provision of R&R entitlements: The components of the Rehabilitation and Resettlement Package in the Second and Third Schedules that relate to infrastructural entitlements shall be provided within a period of 18 months from the date of the award.

How are interests and concerns of scheduled castes and schedules tribes protected?

- Separate chapter: A separate Chapter has been carved out to protect interests of tribals and those belonging to the Scheduled Castes. Where acquisition does take place it shall be done as a demonstrable last resort.
- Approval: As far as possible no acquisition shall take place in the Scheduled Areas. And where such acquisition does take place it has to be done with the approval/ consent of the local institutions of self-governance (including the autonomous councils where they exist).
- Development plan: A Development Plan has to be prepared laying down the details of procedure for settling land rights due but not settled and restoring titles of tribals on alienated land by undertaking a special drive together with land acquisition. The Plan must also contain a programme for development of alternate fuel, fodder and non-timber forest produce resources on non-forest lands within a period of five years sufficient to meet the requirements of tribal communities as well as the Scheduled Castes.
- One-third to be paid up-front: In case of land being acquired from members of the Scheduled Castes or the Scheduled Tribes, at least one-third of the compensation amount due shall be paid to the affected families at the outset as first instalment and the rest shall precede the taking over of the possession of the land.
- Resettlement in the same scheduled area: The Scheduled Tribes affected families shall be resettled preferable in the same Scheduled Area in a compact block so that they can retain their ethnic, linguistic and cultural identity.
- Land for community: The resettlement areas predominantly inhabited by the Scheduled Castes and the Scheduled Tribes shall get land, to such extent as may be decided by the appropriate Government free of cost for community and social gatherings.
- Alienation of tribal lands to be void: Any alienation of tribal lands or lands belonging to members of the Scheduled Castes in disregard of the laws and regulations for the time being in force shall be treated as null and void: and in the case of acquisition of such lands, the rehabilitation and resettlement benefits shall be available to the original tribal land owners or land owners belonging to the Scheduled Castes.
- Fishing rights: The affected Scheduled Tribes, other traditional forest dwellers and the Scheduled Castes families having fishing rights in a river or pond or dam in the affected area shall be given fishing rights in the reservoir area of the irrigation or hydel projects.
- If resettled outside scheduled area then additional benefits: Where the affected families belonging to the Scheduled Castes and the Scheduled Tribes are relocated outside of the district then they shall be paid an additional twenty-five per cent rehabilitation and resettlement benefits to which they are entitled in monetary terms along with a one-time entitlement of fifty thousand rupees.
- Higher land-for-land area for SCs/STs: In every project those losing land and belonging to the Scheduled Castes or Scheduled Tribes will be provided land equivalent to land acquired or two-and-a-half acres, whichever is lower (this is higher than in the case of non-SC/ST affected families)
- Additional amounts: In addition to a subsistence amount of rupees 3000 per month for a year (which all affected families get), the Scheduled Castes and the Scheduled Tribes displaced from Scheduled Areas shall receive an amount equivalent to rupees 50,000.

How are interests and concerns of panchayati raj institutions protected?

- SIA in consultation with PRIs: The Social Impact Assessment (SIA) has to be carried out in consultation with the representatives of the Panchayati Raj Institutions (PRIs). In fact, the appropriate Government is required by the law to ensure adequate representation of these institutions during the discharge of the process.
- SIA reports to be shared: Reports prepared under the Social Impact Assessment are to be shared with these individuals in their local language along with a summary.
- Representation in expert group: The expert group has to have two members belonging to the Panchayati Raj Institutions. This is a powerful body that has the power to reject a project.
- Hearings in all gram sabhas: In case where an affected area involves more than one Gram Panchayat or Municipality, public hearings shall be conducted in every Gram Sabha where more than twenty five per cent of land belonging to that Gram Sabha is being acquired.
- Consultation in compliance with PESA: Consultation with the Gram Sabha in scheduled areas under the Fifth Schedule referred to in the Constitution shall be in accordance with the provisions of the Provisions of the Panchayats (Extension to the Scheduled Areas) Act, 1996.
- Representation of panchayat chairpersons on R&R committee at project level: The Rehabilitation and Resettlement Committee at Project Level has to have the chairpersons of the Panchayats located in the affected area or their nominees as representatives.
- Panchayat ghars have to be provided as per the list of Infrastructural amenities given in the Third Schedule.

How are states interests and concerns protected?

- Only a baseline: The Bill only provides the baseline for compensation and has devised a sliding scale which allows States to fix the multiplier (which will determine the final award) depending on distance from urban centres.
- Choice for return to land bank or owner: Where unutilized land is returned the state can decided whether it goes to the original owner or to the land bank.
- Threshold for private purchase left to government: While the Bill requires the discharge of obligations related to Resettlement and Rehabilitation (R&R) even in the case of private purchase provided the purchase exceeds a certain threshold, it leaves the said threshold to the discretion of the state governments.
- In extreme cases, equivalent amount for multi-crop land: While the Bill seeks to discourage acquisition of irrigated multi crop or agricultural land it gives the choice of earmarking how much of such lands should be reserved for protection against acquisition to the States. Furthermore if no alternative land is available to replace the multi-crop land acquired, the state can instruct the payment of an equivalent amount.
- R&R procedure at discretion of state: The procedure related to the functioning of the R&R committee at project-level has been left to the state government if the acquisition is by the state.
- States free to enact other laws: The state governments are free to enact any law to enhance or add to the entitlements enumerated under the Bill which confers higher compensation than payable under the Bill or make provisions for rehabilitation and resettlement which are more beneficial than those provided under the Bill.

How does the compensation mechanism work?

- In urban areas there is no multiplier. This means no enhancement of the market value calculated occurs.
- However a solatium of 100% (which currently exists at 30%) is imposed on this market value calculated. This 'solatium' amount is a compensation to ameliorate the pain of forcible acquisition.
- In rural areas the multiplier has been left entirely to the discretion of state governments which may range on a sliding scale from 1 to 2 depending on the radial distance from urban centres.

What are the safeguards in the law to ensure food security?

- Special provisions have been inserted in the Law to ensure that multi-crop land is acquired only as a last resort.
- States are also required to impose limits on the area of agricultural/ multi-crop land that can be acquired in a State. No acquisition of such lands in excess of that limit can take place.
- When acquiring agricultural land, the state has to cultivate an equivalent area of land elsewhere as agricultural land. If they cannot do this then they must deposit an amount equivalent to its value in an account to be used for the purposes of enhancing food security.

How are investor concerns addressed?

- Consent: In the case of public-private partnership projects consent has been reduced from 80% to 70%. In additional only the consent of land owners is required.
- Definition of market value has been amended to ensure that acquisition price doesn't form the basis for compensation calculation in future acquisitions. Also power has been given to the Collector to not consider transactions which he feels are outliers and not indicative of true value while calculating market value. Earlier there was a danger of a price-spiral as (a multiple of) price of first acquisition in an area would go into calculation of land price for any subsequent acquisitions
- States given large flexibility: A sliding scale will give states flexibility to fix compensation in rural areas (between two and four times market value), depending on their distance from urban areas. Earlier compensation in rural areas was to be four times market value.
- Restrictions/thresholds on amount of irrigated multi-crop land and net sown area per district or state available for acquisition left to the discretion of states. Earlier amount of irrigated multi-cropped irrigated land that could be acquired was capped at 5%, and amount of net sown area that could be acquired was also capped.
- Land size thresholds on when R&R on private purchase of land becomes applicable has now been left to the discretion of States. Earlier R&R on private purchases was to apply to all acquisitions above 100 acres in rural areas and 50 acres in urban areas.
- Payment for R&R costs by acquirer made a 'one-off' acquirer to put all monies in an escrow account, and ongoing commitments like annuities and benefits to be administered by agency established under this Act. Earlier the Buyer would have had to pay and be involved with R&R infrastructure building until complete, and R&R annuities to perpetuity. However, families will not be displaced from this land till their alternative R&R sites are ready for occupation.
- Collector can be considered appropriate government: In cases where the land sought to be acquired is below a certain threshold then the Collector can be the acquiring authority.
- Criticism

- Some criticize the Act citing that it is heavily loaded in favour of land owners and ignores the needs of poor Indians who need affordable housing, impoverished families who need affordable hospitals, schools, employment opportunities and infrastructure and industries.
- mandates that compensation and rehabilitation payments to land owners and livelihood losers be upfront. If the project does not fructify, there will be losses for the promoter.
- places no limit on total compensation or number of claimants; nor does it place any statute of limitations on claims or claimants.
- The beneficiaries of the Bill, with guaranteed jobs, will have no incentive to be productive. The Bill.
- Amartya Sen, Nobel Laureate in economics, claims prohibiting the use of fertile agricultural land for industries is ultimately self-defeating.
- will increase the cost of acquisition of land to unrealistic level. It will be almost impossible to acquire 50-acre or 100-acre land at one place for planned development.
- inflates the cost of land to help a small minority of Indians at the cost of the vast majority of Indian citizens, as less than 10% of Indian population owns rural or urban land.
- It is time consuming

→ Since the acquired fertile land can be put to use for Production of more valuable goods. By doing so the benefit ~~which would have been~~ reaped from ~~agriculture~~ Production on fertile land will outpace agricultural Production.

Development and the spread of Extremism

Assessments of India's internal security challenges take into consideration various threats in various regions, how they are connected- insurgencies, terrorism etc; communalism, international crime syndicates etc.

A succession of high-profile terrorist attacks across India—outside the areas of chronic terrorist and insurgent conflict—through 2008, culminating in the dramatic and devastating attacks in Mumbai on November 26, 2008, created an enveloping atmosphere of insecurity in the country.

Apart from terrorism and insurgency, lesser conflicts—including caste and communal conflicts, as well as criminal disruption—appear to have attained a measure of predictability over the decades. Poor governance and declining standards of administration—including within the areas of security and justice—have been observed to be among the reasons.

In the realm of security, globalisation has produced a whole new range of interactive threats and risks. Globalisation has also led to a blurring of the distinction between external and internal threats.

While it has enormously benefited many, the unequal and often inequitable process of globalization has at the same time marginalized large populations, generating a widening schism between two emerging worlds. Nowhere is the schism more dramatically manifest than in Asia.

India's external environment hardly lends itself to stability, and this is demonstrated with particular urgency by the 2009 Failed State Index. According to the index, 25 of the 60 states most at risk of failure are located in Asia. Significantly, every country that shares India's borders is among those countries listed—Afghanistan ranks 7th; Pakistan, 10th; Myanmar, 13th; Bangladesh, 19th; Sri Lanka, 22nd; Nepal, 25th; Bhutan, 48th; and China, 57th. South Asia is also the new epicenter of global terror—with "Af-Pak" at its core and Bangladesh having an important place.This is the quintessential "bad neighborhood," arguably "the most dangerous place on earth."

Extreme uncertainty and instability, consequently, afflict all aspects of South Asia's enveloping geopolitical context. Briefly, the principal elements that compound regional destabilization include:

1. The release of a variety of violent nationalist and subnationalist movements across Asia and Eastern Europe
2. The resurgence of radical political ideologies of mass mobilization, including religious—particularly but not exclusively Islamist—extremism, ethnic fundamentalisms, and Maoism, across wide regions
3. The emergence of "new ways of warfare"—specifically terrorism and sub-conventional wars— and their adoption by both nonstate actors and a number of state entities to secure political goals
4. The proliferation of technological force multipliers and sophisticated weapons and explosives among nonstate groups, facilitated by irresponsible, predatory, and rogue states
5. Widening areas of escalating environmental, economic, resource, and social stresses
6. Rising challenges to state power, the progressive weakening of governments, and widening spheres of non-governance and disorder

Development -
(i) Political
· Deepening demoracy → democratic institution →

(ii) Social
· Development of all

(iii) Economical
· Balanced development
· Sustainable

Three principal streams of conflict presently dominate the Indian internal security scenario: Islamist extremism and terrorism, left-wing (Maoist) insurgency, and ethnic fundamentalisms and militancy. End-of-year assessments for 2011 indicated that as many as 254 of India's 640 districts are afflicted by chronic conflict variables connected with these various threats. In addition to these theaters of chronic extremism, sporadic attacks have also been executed across the length and breadth of the country, principally by Pakistan-backed Islamist terrorist groups, though now also including at least attack by an incipient extremist group based in Hindutva (the Hindu right wing).

Islamist terrorism, overwhelmingly spawned and supported by Pakistan, finds its principal locus in the north Indian state of Jammu and Kashmir, but has seen progressive expansion through terrorist mobilization, subversion, and attacks across the country.As international pressure to decrease terrorism in Jammu and Kashmir mounted on Pakistan, and as domestic circumstances in the country worsened rapidly, Pakistan's Inter-Services Intelligence (ISI) handlers have found it expedient to increasingly redirect the terrorist goups into areas outside Jammu and Kashmir A steady stream of Islamist terrorism and subversion has been sustained in widening theaters across India over the past several years, culminating in the startling attacks in Mumbai in November 2008.

The networks and support structures of a multiplicity of Islamist terrorist organizations operating in India have been painstakingly constructed by the ISI and, backed by enormous flows of financial support from West Asia and affluent expatriate Muslim communities in the West, are engaged in a sustained strategy of "erosion, encirclement, and penetration" .There is now no doubt that the Mumbai carnage of November 26–29, 2008, was engineered by the Pakistan-based Lashkar-e-Taiba (LeT), which has been permitted to operate openly in Pakistan under the name Jamaat-ud-Dawa (JuD) since its supposed ban in 2002. In addition to the Lashkar formation, the most significant terrorist groups created by the ISI that operate in India include what can be spoken of as the "Harkat Triad," comprising the Harkat- ul-Jihad Islami (HuJI), the Harkat-ul-Mujahideen (HuM), and the Jaish-e-Mohammad (JeM), each of which is also linked with the Afghan jihad, the Taliban, and al Qaeda.

There are a number of other Pakistan-based groups operating in India, playing roles of varying significance in the machinery of Islamist terror that has been assembled over the years, including some that have substantial Indian membership. Students Islamic Movement of India (SIMI) has been involved in terrorist activities— principally as a facilitator for various Pakistan-based groups—since the 1990s, providing a range of services, such as couriers, safe havens, and communication posts for specific terrorist operations or terrorist cells. There has always been an Indian face to terrorism. Terrorism in Kashmir, which has been unambiguously Islamist despite its subnationalist pretensions, was initiated by Indian cadres. Similarly, the 1993 Mumbai blasts were engineered by an Indian organized-crime group, the Dawood Ibrahim gang. Thereafter, groups such as the al Umma, the Deendar Anjuman, the National Development Front, and the Islamic Sevak Sangh, among others, executed a succession of serial blasts throughout the 1990s. Crucially, however, the transition of each of these groups to terrorist activities—and often the very creation of these groups—has been facilitated and supported by Pakistani agencies and actors.

Dealing Extremism -
(i) Constitutional Provisions
eg Art 352
(ii) Statutory Provisions
eg [illegible]

Naxalism

Naxalism refers to militant Communist movement operating in different parts of India under different organizational names. In the eastern states of the mainland India (Chhattisgarh, Jharkhand, West Bengal and Odisha), they are usually known as, or refer to themselves as Maoists while in southern states like Andhra Pradesh they are known under other titles. They have been declared as a terrorist organization under the Unlawful Activities (Prevention) Act of India (1967).

The term 'Naxal' derives from the name of the village Naxalbari in West Bengal, where the movement had its origin. The Naxals are considered far-left radical communists, supportive of Maoist political sentiment and ideology. Their origin can be traced to the split in 1967 of the Communist Party of India (Marxist), leading to the formation of the Communist Party of India (Marxist–Leninist). Initially the movement had its centre in West Bengal. In later years, it spread into less developed areas of rural southern and eastern India, such as Chhattisgarh, Odisha and Andhra Pradesh through the activities of underground groups like the Communist Party of India (Maoist).For the past 10 years, it has grown mostly from displaced tribals and natives who are fighting against exploitation from major Indian corporations and local government whom they believe to be insensitive and indifferent.

Research and Analysis Wing estimated that 20,000 armed cadre Naxalites were operating in addition to 50,000 regular cadres and their growing influence prompted Indian Prime Minister Manmohan Singh to declare them to be the most serious internal threat to India's national security.

In 2009, the Indian Central government announced a new nationwide initiative, to be called the "Integrated Action Plan" (IAP) for broad, co-ordinated operations aimed at dealing with the Naxalite problem in all affected states (namely Karnataka, Chhattisgarh, Odisha, Andhra Pradesh, Maharashtra, Jharkhand, Bihar, Uttar Pradesh, and West Bengal). Importantly, this plan included funding for grass-roots economic development projects in Naxalite affected areas, as well as increased special police funding for better containment and reduction of Naxalite influence in these areas.

In 2011, the number of Naxal affected areas was reduced to 83 districts across nine states.
These conflicts go back to the failure of implementing the 5th & 6th Schedules of the Constitution of India.

Practically all Naxalite groups trace their origin to the CPI(ML). A separate offshoot from the beginning was the Maoist Communist Centre, MCC later fused with the People's War Group to form the Communist Party of India (Maoist). (read ahead)

Ethnic Fundamentalists

Ethnicity-based insurgencies are endemic in India's northeast region, with Assam, Manipur, and Nagaland being the worst-affected states. A ceasefire exists between the government and the two principal insurgent groups in Nagaland, and a negotiated solution is being sought to the half century–old insurgency in this state. Lesser insurgencies afflict Meghalaya, Tripura, and Arunachal Pradesh. There is a vast proliferation of ethnic insurgent groupings representing progressively narrower tribal interests. A majority of the surviving insurgencies in the region are

Terrorist – Kills noncombatant

"degraded"—large organized criminal operations focusing overwhelmingly on extortion, with little coherent ideological or political content or consistency.

The border-management problem in Northeast India is gigantic. The Bangladesh border—a total of 4,095 kilometers long—is by far the most urgent and intractable crisis. Illegal migration, the existence of terrorist safe havens across the border (many of which have recently been dismantled by the Sheikh Hasina government), the growth and entrenchment of organized criminal gangs and syndicates with powerful political and communal influence and patronage along this border, and a strengthening network of well-funded institutions for the communal mobilization of the migrant community are some of the dangerous trends that counterinsurgency forces are required to contend with in the region.

Emerging Trends

India's development offers one of the most dramatic studies in contrast. Despite the most extraordinary dynamism in certain thriving sectors of the economy amply confirms Michael Renner's phrase that "scarcity and abundance may very well coexist."To take some examples, India's GDP grew from $331 billion in 1992 (the first year of reforms) to $2 trillion in 2013 , yet India's current rank in the UN Human Development Index—136th— is abysmal. In the Global Hunger Index, India ranks very low.

There were many Indians on Forbes' 2012 list of billionaires, but 22% of the country's population is BPL(2013 July)

The essential lesson here is that "development" is not a smooth, unidirectional process that benefits all and harms none. Indeed, the processes of development within India mirror the broader disjunctions between a globalizing world order and states and societies that are progressively marginalized by or isolated from the processes of globalization. These disjunctions feed into cycles of local violence and radical mobilization across the ideological spectrum.

One unique driver of ethnic mobilization in India is the appeal to caste and tribal identity. Identity conflicts also have the potential to coalesce into other patterns of conflict, such as the mobilization under the Maoist banner, as has already occurred in many states in India's east, where caste and tribal conflicts have been tapped by the spreading Maoist insurgency. Such patterns of conflict, which simultaneously harness identity and ideology for mass and violent mobilization, could see an extension over the coming decades.

Population, Environment, Ecology, and Resource Conflicts

Environmental stresses and resource crises as a result of population growth, overexploitation of the natural environment, consequential pollution from the irresponsible utilization of resources, and poor resource and waste management, have significant potential for conflict creation. Further, these factors constitute immediate risks in terms of the broader concept of human security, inflicting enormous distress on large populations and directly jeopardizing the country's developmental potential. The declining per-capita availability of fresh water is one of the most urgent concerns in this context.

Rampaging and poorly managed urbanization is creating new and urgent security challenges. Urban vulnerability to political destabilization, terrorism, organized criminal violence, and

administrative disorders has been one of the most underestimated aspects of urban development in India.

It is significant that the rising proportion of the population in urban centers—projected to rise from around 30% in 2011 to 40% in 2020—will not result in any relief in rural India, where the population will increase from 742 million in 2001 to 810 million in 2020. As much as 63% of India's population growth in the first quarter of the present century is expected to be in its most undeveloped states, increasing the share of these states in India's population from 40% to 50%. These are the areas that have demonstrated the most rapid growth of disorder and misgovernance in the recent past. Moreover, the more progressive states of South India have "completed the demographic transition" with very low growth rates of population and an increasing age profile. This could provoke massive migration from the north to these states, and such migrants could take with them the culture of lawlessness and violence that afflicts so many of their states of origin.

Ghettoization has characterized the political economy of urban settlements in India, with ghettos marked by the "concentration of poverty and de-concentration of opportunity." Caste, communal, and class ghettos are a consistent feature of most Indian cities and create the specter of the "gated city" in a tense standoff between sections of its own people. These broad aspects of the city have given rise to escalating trends in crime and a widening sphere of urban terrorism. The Indian city lends itself to terrorism. The sheer size of some Indian cities (Delhi, for instance, has a population greater than 171 of the world's 227 countries), the pervasive and insidious contempt for law, the scant regard for municipal regulations, the absolute anonymity provided by the city's chaos and the lack of a centralized and comprehensive identity system contributed to an air of license and disorder.

At the national level, the Ministry of Home Affairs (MHA) is charged with the maintenance of internal security and the responsibility of protecting states from "external aggression and internal disturbances" under Article 355 of the Constitution of India. Responsibility for maintenance of "public order" and "police," under List II of the constitution (the State List), is, however, vested in the various state governments. This division of responsibility has created a fragmented system that has contributed enormously to the evasion of responsibility by both the central government and the states, and an enduring neglect of the internal security apparatus. The Union Government has the constitutional authority to seize control of a state under certain circumstances of a breakdown in public order (Articles 257, 258, 365, and 356), and a national emergency can also be declared under Article 352, if "a grave emergency exists whereby the security of India or of any part of the territory thereof is threatened, whether by war or external aggression or armed rebellion."

Despite these apparently sweeping powers, there has been a progressive decline in the central government's capacities to influence states on issues relating to internal security management, despite the very significant central outlays supporting police modernization, the augmentation of state security capacities, and the underwriting of the security-related expenditures of the states. The infirmities of the system were highlighted by the Group of Ministers' 2001 report on internal security, which noted that constitutional, legal, and structural infirmities had "eroded the Union Government's authority to deal effectively with any threat to the nation's security" and called for the "appropriate restructuring of the MHA." The report also underlined the growing incapacity of

state governments to "deal with grave offences, which have inter-state and nation- wide ramifications."

The lack of sustained investment in and the neglect of the transforming role of the police within a modernizing state system has enormously compromised the capacities, efficiency, and effectiveness of state police organizations. Constant political interference and a subordination of legal mandate to partisan political objectives has undermined the ability of the police to deal effectively with internal security problems.

The infirmity of the states' internal security apparatuses has resulted in a constant clamor for central assistance and the "paramilitary panacea"—the deployment of increasing numbers of Central Paramilitary Forces (CPMF) in local disorders across the country.

The central government's MHA presides over a multiplicity of CPMFs, most prominently the Central Reserve Police Force (CRPF), the largest of these forces. The CRPF is a "striking reserve to assist the State/Union Territories in Police operations to maintain law and order and contain insurgency," and in 2006 it was designated the "lead agency" to respond to terrorism and insurgency in the country.

Other CPMFs that play a prominent role in the more acute aspects of internal security management include the Assam Rifles (strength: 65,290), the Border Security Force (210,261), the Indo-Tibetan Border Police (50,326), the Central Industrial Security Force (103,860), the Sashastra Seema Bal (armed border police: 48,934), and the National Security Guard (7,334).

The MHA also supervises India's principal domestic intelligence agency, the Intelligence Bureau (IB), which operates across the country through its network of subsidiary intelligence bureaus.

The MHA also maintains a range of specialized technical, forensic, training, and research organizations in support of internal security and policing operations for both central and state organizations. In addition, the National Technical Research Organisation, operating under the national security adviser in the prime minister's office, provides specialized technical intelligence flows to both internal and external security agencies.

The principal instrument for the projection of a coherent Indian framework of internal security management is the centralized Indian Police Service (IPS), which provides the top leadership cadre for almost all central and state police, paramilitary, and intelligence organizations.

In addition to the various central organizations explicitly involved in internal security operations, forces drawn from the 1.1 million–strong Indian Army can also be called "in aid to civil authority" to deal with a wide range of emergencies and crises, including "maintenance of law and order, maintenance of essential services, disaster relief and other types of assistance."

While the preceding outline of central and state forces and organizations available for internal security management creates an illusion of great strength, the reality is that India is afflicted by an acute crisis of capacity.

The crisis of the police has been widely and repeatedly recognized at the national level, with numerous national and state police commissions calling for sweeping reforms. The Supreme

Court of India finally intervened in September 2006 with a seven-point directive
There is concern whether the police structure today has relevance and validity in the rapidly changing circumstances of the 21st century, with insurgency, sub-conventional warfare, and terrorism—and the rising specters of WMD terrorism and cyber-crime and cyber-terrorism.

Perhaps the most visible and dramatic index of the crisis in policing is the general deficit of manpower in all ranks of the police, both in absolute numbers of sanctioned posts and in the numbers of vacancies that exist against such sanctioned posts. At the level of police leadership, according to the MHA data on the shortage of IPS officers, there is a 28.11% deficiency in the number of IPS officers in position (as of January 1, 2011), against sanctioned strengths, and worse, most states feel that the sanctioned strength is deficient. The overall crisis of manpower in the police is even more acute. According to norms set by the United Nations, a minimum police-to-population ratio of 1 to 450 (222 per 100,000) should be maintained for peacetime policing. Most Western countries maintain ratios well above this minimum standard; for instance, the ratio is as high as 559 per 100,000 in Italy and 465 per 100,000 in Portugal. Significantly, most of these countries have policing needs that are certainly less demanding than those confronting India, where the culture of the rule of law is far from entrenched and virtually all compliance needs enforcement. Yet, India's police-to-population ratio stands at a bare 125 per 100,000.
This dismal picture is, in some measure, balanced out by India's extraordinary growth in the recent past and the economic and political resilience that the country has demonstrated in the face of recurring challenges. Financial resource deficits that threatened the very possibility of resolving the country's many problems are a thing of the past, though a range of other structural impediments persist. There is a real danger, however, that widening spheres of disorder may come to threaten the dynamic core on which India's successes and future potential are founded.

Nevertheless, a range of factors constrain the scope of extremism in India and favor— although they cannot guarantee—broad stability. Critically, while cyclical conflagrations and radicalization on the fringes—variously supported by external powers and internal elements—remain a reality, extremism fails to secure sufficient traction among the masses to present a coherent and national challenge to the state. The reasons are many. Chief among them is a cultural proclivity to nonviolence, or at least a rejection of extreme violence. The constitutional edifice, for all its political neglect, is extraordinarily inclusive. Democratic processes, imperfect and even occasionally perverse as they are, do create the spaces for the articulation of grievances and the relatively peaceful expression of political discontent. The sheer diversity of the population is a source of manifold frictions, but it also prevents mobilization on a national scale under any single divisive or extremist banner. These and other structural and cultural factors constrain even radical players from their greatest excesses. Thus, for instance, electoral considerations have repeatedly forced the Hindu (majority) Right to accommodate Muslim (minority) concerns. Parties that exploit narrow caste mobilization find it necessary to progressively widen their caste base as their electoral successes open up a larger regional or national platform. Similarly, even where some state agencies have colluded with extremist elements—as, for instance, in the Gujarat riots of 2002— constitutional checks and balances do eventually reassert themselves to bring offenders to some measure of justice.
Deep national, psychological, and civilizational reserves manifest themselves in the face of catastrophic emergencies. Indeed, India has an extraordinary record of defeating a number of the most virulent insurgencies and terrorist movements and of exhausting and outlasting the country's many adversaries. Harnessing complex national reserves to adopt coherent national

perspectives and policies remains a crucial challenge, but it is clear, especially in the wake of the November 26, 2008, attacks in Mumbai and the rising challenge of the Maoist insurgency, that the national leadership now recognizes the core imperatives of response.

Successes in certain spheres—especially in the realms of economic growth and globalization—over the past decade and a half have also fed a surge in confidence, a relative augmentation of competence, and the launch of a wide range of initiatives intended to address the country's cumulative deficits. While the initial impact has been limited, this combination of factors is expected to snowball once it secures a certain critical mass. Crucially, with a vibrant democracy, substantially non-doctrinaire economic perspectives, progressive engagement with modernity and a globalizing order, and a culture of tolerance and pragmatism, the Indian people have positioned themselves on the right side of history. This reality, above all else, warrants the expectation that India will not only endure but flourish.

Excerpts from PM's speech at the CMs meet on internal security in mid-2013(post-Bastar)

Steps taken by the government include strengthening the security apparatus, improving road connectivity in 34 most Left Wing Extremist affected districts, relaxation of norms of various development schemes in the affected areas, and the Integrated Action Plan for 82 selected tribal and backward districts.

In the last couple of years there has been a substantial reduction in the number of incidents and deaths caused by Left Wing Extremist groups and an increase in the number of Naxalite surrenders. But, major violent attacks by Naxalites like the recent one in Chhattisgarh are setbacks that have occurred periodically.

The year 2012 saw a significant improvement in the security situation in Jammu and Kashmir. Our strategy to prevent cross-border infiltration by militants and our intelligence based counter-terrorism operations in Jammu and Kashmir have resulted in a decline in the level of terrorist violence by about one-third in 2012 as compared to 2011. In fact, terrorist violence parameters in 2012 have been the lowest since the upsurge in terrorist activities two decades ago. The record inflow of tourists and pilgrims during 2012 also points to an improved security situation in the State.

The implementation of several infrastructure projects in Jammu and Kashmir is progressing well. The Himayat and Udaan schemes which aim at providing additional gainful employment to the youth have also achieved a fair measure of success.

The security situation in the North East continues to be complex, with insurgency, extortion and agitations being the main disruptive elements in the hands of the insurgents. However, there has been considerable progress in dialogue with several insurgent and ethnic separatist groups in the North-Eastern region. A Memorandum of Understanding has been signed with both factions of Dima Halam Daogah of Dima Hasao in Assam. Three Metei insurgent groups have signed a Memorandum of Understanding in February 2013. Talks with the National Socialist Council of Nagaland are continuing.

The Gorkhaland Territorial Administration (GTA) has been set up as an autonomous body in August 2012 to administer the Gorkhaland region and ensure its all-round development. The Centre is committed to providing financial assistance of Rs 200 crore per annum for three years for projects aimed at developing the socio-economic infrastructure in the GTA areas.

GOIis committed to undertaking and bringing to a satisfactory conclusion dialogue with all groups and organizations which are willing to give up violence to seek solutions within the framework of our Constitution. GOI is equally firm in the determination to continue assisting the States of the North-East to enhance their law and order enforcement capabilities, so that the people of the North-East enjoy the normal fruits of democracy and development.

On the front of communalism, there is the increase in number and intensity of incidents of communal and sectarian violence during 2012 as compared to the previous year. Maintenance of communal harmony is critical for our continued growth and prosperity. Crimes against women and children are increasing . We have recently enacted several laws providing stringent punishment for such crimes and more sensitive treatment of victims during investigation and trial. These include the Criminal Law (Amendment) Act, 2013; The Sexual Harassment of Women at Workplace (Prevention, Prohibition and Redressal) Act, 2013 and the Protection of Children from Sexual Offenses Act, 2012.

We also need to put in place institutional mechanisms to ensure the safety and security of women and children, particularly in the urban context. Such mechanisms include sensitization of police personnel, particularly at levels with which the victim comes into contact, setting up dedicated help-lines, measures for safety at the work place, and so on.
Capacity building and modernization of State Police Forces are absolutely essential for meeting the emerging challenges to internal security which range from terrorism to urban policing. The Centre is supporting States in this regard. The scheme for modernization of State Police Forces has been extended for a further period of five years with a total outlay of about Rs. 12,000 crore. An amount of Rs. 433 crore has been additionally provided for Mega City Policing in the six cities of Kolkata, Mumbai, Chennai, Bengaluru, Ahmedabad and Hyderabad.

Goi is committed to improving border management and coastal security. Greater focus and priority than before is being given to the work of fencing and construction of additional Border Outposts along the India-Bangladesh border, the construction and up-gradation of roads along the India-China, India-Nepal and India-Bhutan borders as well as the development of integrated check posts on the India-Pakistan and India-Nepal borders. We are also continuing implementation of the Border Area Development Programme and of Phase II of the Coastal Security Scheme.Time has now come to view the challenges of terrorism, communal violence and Left Wing Extremism in a holistic manner.

Extremism

It is any ideology (particularly in politics or religion), considered to be far outside the mainstream attitudes of a society or to violate common moral standards. In liberal societies, individuals or groups that advocate the replacement of democracy with a more authoritarian regime are labelled extremists; in authoritarian societies, those who espouse liberal ideals are labelled as extremists by the ruling class or government.

Pejorative → Expressing contempt or disapproval

Extremists are usually contrasted with centrists or moderates. Political agendas perceived as extremist often include those from the far left or far right, as well as radicalism or fundamentalism..

The term "extremism" is usually pejorative, but it is sometimes used in a purely descriptive sense, referring simply to a viewpoint that is inconsistent with existing norms, rather than implying that the extremist position constitutes a threat (to the society, government, mainstream morality, etc.).

Fourth-generation warfare (4GW)

It is a conflict in which one of the major participants is not a state but rather a violent non-state actor.

AFSPA

The Armed Forces (Special Powers) Act (AFSPA), was passed 1958, by the Parliament It grants special powers to the armed forces in what the act terms as "disturbed areas" in the states of Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland and Tripura. It was later extended to Jammu and Kashmir as The Armed Forces (Jammu and Kashmir) Special Powers in 1990.

The Republic of India has seen a history of insurgency in the states of Kashmir, Punjab, Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland and Tripura. Each of these states are in regions that border with Pakistan or China - countries which India has border disputes with.

State or central government can exercise the power to declare areas as being disturbed following which armed forces could be deployed. For declaring an area as a 'disturbed area' there must be a grave situation of law and order on the basis of which Governor/Administrator can form opinion that an area is in such a disturbed or dangerous condition that use of Armed Forces in aid of civil power is necessary.

According to the Armed Forces Special Powers Act (AFSPA), in an area that is proclaimed as "disturbed", an officer of the armed forces has powers to:

- To arrest without a warrant anyone who has committed cognizable offences or is reasonably suspected of having done so and may use force if needed for the arrest.
- To enter and search any premise in order to make such arrests, or to recover any person wrongfully restrained or any arms, ammunition or explosive substances and seize it.
- Stop and search any vehicle or vessel reasonably suspected to be carrying such person or weapons.
- Any person arrested and taken into custody under this Act shall be made over to the officer in charge of the nearest police station with the least possible delay, together with a report of the circumstances occasioning the arrest.
- Army officers have legal immunity for their actions.

In 2004, in the wake of intense agitation and the indefinite fast undertaken by Irom Sharmila, Central Government set up a five-member committee under the Chairmanship of Justice B P Jeevan Reddy, former judge of the Supreme Court. The panel recommended that the law be scrapped.

Special powers are required to enhance the efficiency of forces so that the grave situation which has arised can be tackled.

Role of the Civil Services in Democracy

In a democracy, power vests with the people. This power is exercised through its elected representatives who have the mandate to govern them for a specific period. The civil services by virtue of its knowledge, experience and understanding of public affairs assist the elected representatives in formulating policy and are responsible for implementing these policies. Parliamentary democracies are usually characterized by a permanent civil service which assists the political executive. Under the Presidential form of government (like in the US), the higher echelons of the civil services are, in contrast, appointed by the government of the day (spoils system). India has adopted the British model.

Some advantages of having an independent, permanent and impartial civil service are as follows:

- The spoils system has the propensity to degenerate into a system of patronage, nepotism and corruption. Having a credible recruitment process through an impartial agency provides a defence against such abuse.
- Public policy today has become a complex exercise requiring in-depth knowledge and expertise in public affairs. A permanent civil service provides continuity and develops expertise as well as institutional memory for effective policy making.
- A permanent and impartial civil service is more likely to assess the long-term social payoff s of any policy whereas the political executive may have a tendency to look for short term political gain.
- A permanent civil service helps to ensure uniformity in public administration and also acts as a unifying force particularly in vast and culturally diverse nations.
- A permanent civil service like any other reputable profession is likely to evolve over time an ethical basis for its functioning.

A healthy working relationship between Ministers and civil servants is critical for good governance. In any democracy, Ministers are responsible to the people through Parliament and therefore the civil servants have to be accountable to the Minister.

However, an impartial civil service is responsible not only to the government of the day but to the Constitution of the land to which they have taken an oath of loyalty. At the same time, implementing the policies of the duly elected government is a core function of civil servants. That is why the division of responsibility between the civil servants and ministers needs to be more clearly defined. A framework in which responsibility and accountability is well defined would be useful.

Constitutional Provisions

The Indian Constitution provides for separation of powers between the legislature, executive and judiciary with well-defined roles and responsibilities for each one of them. Since India is a parliamentary democracy, there is an interface between the legislature and the executive at the level of the Council of Ministers, which is collectively responsible to the legislature. In terms of Articles 53 and 154, the executive power of the Union and the States vests in the President or Governor directly or through officers subordinate to him.

These officers constitute the permanent civil service and are governed by Part XIV of the Constitution.The other part of the executive is the 'political'. The President or Governor is required to act according to the aid and advice of his/her Council of Ministers, appointed under Articles 73 and 163 of the Constitution. The President and Governor frame rules for the

conduct of business in the government. Work is allocated among Ministers as per the Government of India (Allocation of Business) Rules and the manner in which the officers are required to help the President or Governor to exercise his/her executive functions is governed by the Government of India (Transaction of Business) Rules. What this means is that though officers are subordinate to the President or Governor, they carry out the orders of the Council of Ministers in accordance with the rules framed in this behalf. The Rules of Business of Government do provide for the Secretary to the Government to advise his/her Minister about the course of action proposed in a particular matter and to submit to him a note which tells him about the propriety or legality of his/her orders and suggest that either such orders not be given or that they be suitably modified. The relationship between the Secretary and the Minister is organic. The Minister has the mandate of the people to govern, but the Secretary has an equivalent constitutional mandate to advise the Minister.

Once his/her advice has been suitably considered, unless the Minister passes an illegal order, the Secretary is bound to implement it. The Minister, on his/her part, is required to support the Secretary who is implementing his/her order. Once a law is framed or rules and regulations are approved, they apply to everyone, whether a member of the political executive or of the permanent civil service. A civil servant is required to implement the orders of government without bias, with honesty and without fear or favour. It is precisely in this area that a degree of a difference of opinion often occurs between the political executive and the civil servants.

The Civil Services in Post Independence India

In the initial years after Independence, relations between Ministers and civil servants were characterized by mutual respect and understanding of each other's respective roles, with neither encroaching upon the other's domain. However, in subsequent years, matters started changing for the worse. While some civil servants did not render objective and impartial advice to their Ministers, often some Ministers began to resent advice that did not fi t in with short-term political interests. There was also a tendency for some Ministers at the Union and the State levels to focus more on routine administrative matters such as transfers in preference to policy making. At the same time, some civil servants learnt the art of 'maneouvering' for favours in return for pliability in their decision making. This trend was further accentuated by rising materialism and acquisitiveness in society as well as decline in values across the board. As a result, 'political neutrality' which was the hallmark of the civil service earlier in the period right after Independence, was gradually eroded. These trends led to the phenomenon of 'politicisation of the civil service' in India.

Areas of Friction

The areas of potential conflict in the relationship between the political executive and the permanent civil service can be identified as follows:

- The concept of neutrality
- Advisory role of civil servants in policy making
- Statutory role of the civil servants
- Appointments/Recruitment to the civil services
- Transfers and postings of civil servants

The Concept of Neutrality

Sardar Patel had made the following observations in the Constituent Assembly to support the continuance of the pre-independence civil service structure:-

"It needs hardly to be emphasized that an efficient, discipline and contended civil service assured of its prospects as a result of diligent and honest work, is a sine-qua non of sound administration under democratic regime even more than under an authoritarian rule. Th e service must be above party and we should ensure that political considerations, either in its recruitment or in its discipline and control, are reduced to the minimum if not eliminated altogether."

Unfortunately, this vision of civil service neutrality no longer holds good. Changes in governments particularly at the state level often lead to bulk transfer of civil servants. Political neutrality is no longer the accepted norm with many civil servants getting identified, rightly or wrongly, with a particular political dispensation. There is a perception that officers have to cultivate and seek patronage from politicians for obtaining suitable positions even in the Union Government. As a result, the civil services in public perception are often seen as increasingly politicized.

The 2nd ARC is of the view that the political neutrality and impartiality of the civil services needs to be preserved. The onus for this lies equally on the political executive and civil servants. Th e Commission in its Report on "Ethics in Governance" while examining the ethical framework for Ministers has recommended that a code of ethics for Ministers should inter-alia include the following:

"Ministers must uphold the political impartiality of the civil service and not ask the civil servants to act in any way which would conflict with the duties and responsibilities of the civil servants."As observed by Paul Appleby, civil servants should not confuse 'political neutrality' with 'programme neutrality'. At the stage of policy formulation, the role of civil servants is to render free and frank advice which should not be coloured by any political considerations. Once a policy or programme has been approved by the elected government, it is the duty of the civil servant to faithfully and enthusiastically see to its implementation. Not carrying out this task in the right spirit would amount to misconduct inviting appropriate sanctions.

Code of ethics for Ministers

A Group of Ministers (GoM) in mid-2013 asked the government to consider a draft code of ethics for ministers and code of conduct for public servants after it was recommended by the Administrative Reforms Commission (ARC) to safeguard the political neutrality and impartiality of the civil services.

The GoM headed by Defence Minister A.K. Antony met to consider recommendations of the tenth report of the ARC asked the Department of Administrative Reforms and Public Grievances.

The GoM members felt such a code was imperative and that it will certainly add to the neutral and transparent working relationship between bureaucracy and ministers.

"There is a need to safeguard the political neutrality and impartiality of the civil services. The onus for this lies equally on the political executive and the civil services.

"This aspect should be included in the Code of Ethics for Ministers as well as the Code of Conduct for Public Servants," the ARC had recommended.

In addition to the existing code of conduct for ministers, there should be a code of ethics to provide guidance on how ministers should uphold the highest standards of constitutional and ethical conduct in the performance of their duties, the fourth report had suggested.

It had also recommended setting up of dedicated units in the offices of the Prime Minister and the Chief Ministers to monitor the observance of the code of ethics and conduct.

In December 2013, Union Cabinet approved a new code of conduct for ministers that debars them from asking civil servants to carry out actions that are not in line with their duties.

The code, though not given a legal backing, will be enforced by the Prime Minister at the Centre and the chief ministers in the states. As per the revised norms, ministers must uphold the political impartiality of the civil services and avoid instructing a civil servant to do things other than those included in his official duties and responsibilities.

Advisory Role of Civil Servants in Policy Making

Rendering policy advice to the political executive is the most important "staff function" of the civil servant. Policy making is the ultimate responsibility of the Minister. After a policy is approved by the elected government, it is duty of the civil servant to implement such policy in the right earnest whether he/she agrees with it or not. At the same time, it is the duty of the civil servant to provide the factual basis, thorough analysis of all possible implications of any measure under consideration and free and frank advice, without fear or favour, at the stage of policy formulation. However, for civil servants to be able to provide appropriate policy inputs, they must acquire the necessary combination of a broad perspective of the sector as well as of the Government as a whole, combined with conceptual clarity and requisite knowledge.

If a policy that is being formulated is perceived by the civil servant to be against public interest, his/her responsibility is to convince the political executive about the adverse implications of such a policy. However, if the political executive does not agree with such an advice, there is little that the civil servant can do other than putting his/her views clearly on record. It is for the other institutional mechanisms such as Parliament, the CAG, Judiciary and ultimately the electorate to hold the political executive to account for bad policy.

Statutory Role of the Civil Servants

Civil servants are required to discharge statutory functions under various legislative enactments which may sometimes be quasi-judicial in nature. The role of the executive magistrate under the Cr. PC, the role of an Assessing Officer under the Income Tax Act and of the SHO under the Cr. PC and the respective Police Acts are some examples of such functions. It has been observed that there is an increasing trend on the part of the senior functionaries both in the civil services as well as elected representatives including Ministers to interfere in such statutory functions. Acquiescence in the face of such interference is primarily the fault of the officer who has been entrusted with these statutory functions although those bringing such extraneous pressures should also be held to account.

Acquiescence - agree

Appointments/Recruitment to the Civil Services

The Constitution of India provides for an independent Union Public Service Commission (UPSC) and State Public Service Commissions (PSCs). It lays down that it shall be the duty of the Union and the State Public Service Commissions to conduct examinations for appointments to the services of the Union and the services of the States respectively. However, while the UPSC enjoys an untarnished reputation for having developed a fair and transparent recruitment system, the same cannot be said for all the State PSCs. In addition, a large number of recruitments to various positions is done by departments of government and different organizations under their control both at the Union and the State government levels. Examples of such large scale recruitments which have often been the subject of complaints and controversies are recruitments to the posts of Police constables, teachers, bus-drivers and conductors etc. The Commission feels that it is essential to lay down certain principles/norms for such recruitments to avoid complaints of favouritism, nepotism, corruption and abuse of power that have often characterized these recruitment exercises. These principles are :

- Well-defined merit-based procedure for recruitment to all government jobs
- Wide publicity and open competition for recruitment to all posts
- Minimisation, if not elimination, of discretion in the recruitment process
- Selection primarily on the basis of written examination or on the basis of performance in existing public/board/university examination with minimum weightage to interview.

Postings and Transfers of Civil Servants

ingratiat
↓
gain favour
by flattery

The National Commission to Review the Working of the Constitution made the following observations regarding transfers and postings of civil servants:

"Arbitrary and questionable methods of appointments, promotions and transfers of officers by political superiors also led to corrosion of the moral basis of its independence. It has strengthened the temptation in services to collusive practices with politicians to avoid the inconvenience of transfers and to gain advantages by ingratiating themselves to political masters. They would do the politicians' biddings rather than adhere to rules. Lest the situation becomes more vicious, it is necessary that a better arrangement be conceived under the Constitution. The question of appointments, transfers and placements is not to be left to the discretion of the politicians or administrative bosses but be entrusted to independent and autonomous boards. The Commission, therefore, recommends that the questions of personnel policy including placements, promotions, transfers and fast-track advancements on the basis of forward-looking career management policies and techniques should be managed by autonomous Personnel Boards for assisting the high level political authorities in making key decisions. Such civil service boards should be constituted under statutory provisions.

They should be expected to function like the UPSC. Reputed management experts from institutes of management, well known for their excellence, should be inducted into these boards to provide a broad based pool of expertise. The principle is not to take politics out of personnel policy but to make knowledge and information institutionally available to the political decision-makers on the basis of appropriate parliamentary legislation under Article 309. The sanctity of parliamentary legislation under Article 309 is needed to counteract the publicly known trends of the play of unhealthy and destabilizing influences in the management of public services in general and higher civil services in particular."

Arbitrary and motivated transfers of government servants which are not in public interest and good governance have become a matter of great concern particularly in some States.

The Union Government has initiated several measures in order to ensure security of tenure to civil servants. The Rules governing the All India Services have been amended and provision made for fixation of tenures of posts encadred with the AIS. For example, the Indian Administrative Service (Cadre) Rules, 1955, have been amended :A cadre officer, appointed to any post for which the tenure has been so determined, shall hold the minimum tenure as prescribed except in the event of promotion, retirement, deputation outside the State or training exceeding two months.An officer may be transferred before the minimum prescribed tenure only on the recommendation of a Committee on Minimum Tenure . The tenure of several posts has been notified accordingly for many States.

Civil service refers to the body of government officials who are employed in civil administration that are neither political nor judicial. The founding fathers of the Constitution wisely provided, by making provisions in Part XIV of the Constitution, for apolitical and independent civil services, with requisite protection for service matters. These provisions pertain not just to the union but also the states. One of the provisions of the Constitution (Article 312) which was hotly debated and faced considerable opposition, particularly from the provincial governments, pertained to the creation of All India Services (AIS) with recruitment based on All India competitive examination and dual control by the centre and the states. Such a constitutional protection was meant to enable the AIS to operate independently, freely, objectively and fearlessly. Unfortunately, political interference and administrative acquiescence has severely dented the professional fibre of the service.

The civil service system is the backbone of the administrative system which acts as most important tool for governance of our country. In post-independent India civil service was reorganised. There are three tiers of administration – Union/Central Government, State Government, and Local Government. At the central level, the civil service include the All India Services, namely the Indian Administrative Service (IAS). Indian Foreign Service (IFS), Indian Forest Service (IFS), and Indian Police Service (IPS). Apart from these there are various other Central Services like the Indian Income Tax Service, Indian Railways Service, etc. at central level. The State Governments have their own services – State Civil Service.

Over the period the role of civil services has changed. During British period, enforcement of law and order and collection of revenue was the main concern of civil servants. In post independence India, when the Government acquired the role of Welfare State, civil services acted as an important tool for implementing national and state policies of welfare and planned development. From the 1990's, globalisation policies followed by the government have had their impact on the nature of civil services- greater role for entrepreneurs is given and bureaucracy has to accordingly change. In the current century, essentially in the last about one decade, the bottom pressures and entitlement regime has further made changes in the way civil services functions- greater transparency and accountability, e-governance being a major impetus.

The Indian civil services, with its national character, have been a strong binding force to the Union of States. The institution of civil service has rendered service to the overall socio-economic development of the country. It has been at the forefront of the development process right from the 'commanding heights regime' to the 'liberalization and de-regulation era'. It has acted as a force of unity among diversity. It has not only played a pivotal role in designing and activating policies, it has also ensured basic service delivery at the grass root level to the marginal section of our society.

The importance of the civil service to the Indian administrative system stems from the following:

- Service presence throughout the country and its strong binding character
- Non-partisan advice to political leadership in the midst of political instability and uncertainties
- Administrative and managerial capacity of the services
- Effective policy-making and regulation
- Effective coordination between institutions of governance
- Leadership at different levels of administration.
- Service delivery at the cutting edge level
- Provide 'continuity and change' to the administration.

Since civil services are considered as the most important element of Indian administrative system that has the responsibility to fulfil the development objectives of the welfare state, so, any failure or shortcomings in fulfilment of these objectives are attributed to the failure of civil services.

Some of the criticism of Indian civil services is:

- Lack of professionalism and poor capacity building
- Alienation from the public and lack of understanding of what people want
- Inefficient incentive systems that do not appreciate upright and outstanding civil servants
- Lack of performance culture and focus on outputs and not outcomes – inappropriate performance appraisal
- Lack of adequate transparency and accountability procedures
- politicisation
- A gradual erosion in public service values, ethics and morale

So, on the basis of experience so far and some other developments of the present era like globalisation, restless and educated public that has become demanding, technological options in administration, coalition nature of polity, etc., it is recognized that reforming the civil service is necessary.

For 'Good Governance' which is one of the most important goals of the modern welfare State, civil services have to re-orient themselves because with its present attitude and training civil services are not able to come upto people's expectations.

A well-functioning civil service helps to foster good policymaking, effective service delivery, accountability and responsibility in utilizing public resources which are the characteristics of good governance.

Governance reform refers to the improvement of legal, institutional and policy frameworks to create proper decision making and implementation environments for economic growth and distribution. It encompasses participatory systems for elements of civil society to become actively involved in formulation of policies and programmes and their implementation. It also includes effective and transparent systems and processes for accountability in government activities.

Civil Services and Globalisation:

Following factors are relevant

- Fast pace of globalisation is mainly driven by the rapid advancement of communication technology and it is necessary to develop our civil services into a technology savvy force.Recent trends in the compositional make up of civil services - like increasing numbers of engineers, doctors, management degree holders, and agriculture graduates would help in enhancing technical orientation of our civil services.
- In the era of globalisation, the role of the State has changed. Since economic liberalisation has led to the diminishing role of state, it has resulted in the marginalisation of a section of society who is economically weak and can't take advantage of the economic opportunities provided by economic liberalisation. The State will have to take care of this section by redistributive policies .State's main emphasis should be on social sector. For this bureaucracy has to be retrained to deliver and be answerable as most of these programmes are entitlements- employment, information, food etc. Attitudinal changes are called for.
- Globalisation has increased the importance of international organisations like IMF, World Bank, WTO, WIPO etc. IPR laws and their knowledge is becoming critical. Dealing with these organisations needs professionalism, tough negotiating skill, etc.

Civil Service Reforms

Civil service reform is a deliberate action to improve the efficiency, effectiveness, professionalism, broad social base of selection and democratic character of a civil service, with a view to promoting better delivery of public goods and services, with increased accountability. Such actions can include organizational restructuring, improving human resource management and training, enhancing pay and benefits while assuring sustainability under overall fiscal constraints, and strengthening measures for public participation, transparency, and combating corruption.

Civil Service Reform in India

The Indian bureaucracy, with its national character, has been a strong binding force to a Union of States. The institution of civil service has rendered yeoman service to the overall socio-economic development of the country. It has been at the forefront of development process right from the 'commanding heights regime' to the 'liberalization and de-regulation era'. It has not only played a pivotal role in designing and activating policies but also ensured basic service delivery at the cutting edge of government-citizen interface.

Civil Service Reforms and Socio-Economic Development

Civil Service Reform aims at strengthening administrative capacity to perform core government functions. These reforms raise the quality of services to the citizens that are essential to the promotion of sustainable economic and social development. CSR can contribute to good governance, macroeconomic stabilization by restoring budgetary stability, better utilisation of public funds, developmental impact, people friendly approaches to law and order etc.

The reform can contribute to the design and implementation of an equitable programme of social development. Enhancing the capacity of civil servants and improving their morale are critical to all these functions.

The main components of Civil Service
Reform should pertain to the following:

1. Recruitment
2. Capacity building through more relevant training
3. Performance & Promotion
4. Professionalism & Modernity : e-gov; mindset changes
5. Accountability (read ahead)

Recruitment
The recruitment examination for Indian Civil Services is one of the rigorous examination across the world. Globalisation, technological developments, public private partnerships, civil society activism and explosion of expectations form an educated and upwardly mobile public are demanding that recruitment pattern should change. UPSC has responded with a new system from 2011 and 2013 respectively for Preliminary and Mains examination.P rime Minister's Rural Development Fellows appointed in 2012 by selecting young professionals from top professionals institutions like IITs, IIMs, TISS and others is one such measure.

Reforming and Restructuring Human Resource Management
Building a motivated and capable civil service requires merit-based and non-discriminatory recruitment, which rests on the absence of political patronage, transparent rules and procedures, open competition and selection by an independent agency. Subsequently, important elements in meritocracy and the motivation of employees are the opportunities for promotion, recognition and reward for performance, inter-sector mobility, placement in right jobs and the scope for skill upgrading and self-improvement. It is equally important to address demotivating factors like frequent and arbitrary transfers as well as special factors affecting women in office and field jobs. A statutory body Civil Services Board (CSB) can be created to look into issues such as transfers and promotion of Civil servants (NCRWC). This will help in reducing political pressures on the careers of civil servants. As there should be cohesion between the political masters and the civil servant for ensuring good governance, the civil service board can be used to delink civil service performance issues from politics. A clear demarcation line can be drawn between the two with the establishment of such boards.

Civil Service Accountability
The accountability of the civil servant has administrative, financial, judicial and other dimensions. In the recent years, there i a flurry of laws demanding greater transparency and accountability in India. RTI accountability is another area. For greater accountability, the following are some of the measures suggested:

- Strengthening and streamlining reporting mechanisms
- Streamlining and fast-tracking departmental enquiries
- Action on audit findings
- Implementation of Citizens Charters' for monitoring service delivery
- Right to Information Act and its enforcement
- Code of conduct for civil servants

Functions of the civil servant/Officer
A civil servant is responsible for the law and order and general administration in the area under his work. Typically the functions of an IAS officer are as follows:

- To handle the daily affairs of the government, including framing and implementation of policy in consultation with the minister-in-charge of the concerned ministry.
- Implementation of policy requires supervision.

- Filed work: Implementation requires travelling to places where the policies are being implemented.
- In the process of policy formulation and decision making, officers at various levels make their contributions and a final decision is taken by the minister concerned or the cabinet.

From the EPW August 2013 (Edited)

The Constitution made the bureaucracy subordinate to the political power of the elected representatives. Following the liberal democratic framework, it provided functional autonomy to the civil service which was meant to remain politically neutral in implementing policy. Formal neutrality of the services has provided the public-minded civil servant the space necessary to maintain a distance from political pressures and also check the excesses of many elected representatives.

Civil service has been subjected to new pressures for it to become more people-friendly:. A part of this has been a result of a deepening democratisation of Indian society which is challenging vested interests through mass mobilisations, a part is due to the spread of communication, information technology and the media and some also due to the institution of legal weapons like the right to information and the public interest litigation.

Democratic superintendence over the bureaucracy is certainly a must. Such a system of democratic checks and balances helps ensure that bureaucrats fulfil the constitutional mandate of maintaining neutrality and administrative efficiency. But such a balance between the democratic polity and the bureaucracy is possible only if the political culture is not reduced to patronage and narrow populism. In states where democratisation has struck relatively shallow roots democratic control over the bureaucracy becomes a caricature. The influence of the real estate lobby in Haryana, of the mining mafias in UP, Karnataka, Jharkhand and Chhattisgarh, and the big crony corporates in Gujarat are among many examples.

While the public outcry in support of Nagpal is welcome and her victimisation should end, it will be futile if this is seen in terms of an individual and not the systemic infirmities that the case illustrates. Hopefully this will further the move towards a better balance between political oversight and administrative neutrality. However, it will be equally dangerous if this leads to insulating the administration from democratic pressures.

Durga Shakti-related by Shailaja Chandra in the Indian Express August 12, 2013

The suspension of Durga Shakti Nagpal has stunned citizens across the country.

The Indian Administrative Service (IAS) was established in accordance with the provisions of Article 312 of the Indian Constitution. The acceptance rate of candidates aspiring to the IAS is just 0.01 per cent, making their selection among the most competitive in the world. It also makes these officers the most envied.

Every district (there are nearly 600 rural districts) is subdivided into two to three administrative divisions, each headed by a sub-divisional magistrate (SDM). As soon as the initial training is over, the new SDM is expected to enforce a string of laws and oversee the implementation of scores of schemes. The young officer is usually treated as a member of the district collector's family, and often of the divisional commissioner's as well. Their mentoring helps the officer understand and respond to the complexities of maintaining law and order and of providing leadership.

Conferred with magisterial powers under the CrPC, the SDM has to issue prohibitory orders when a danger to public peace or public health is apprehended, and order the search of property when there is suspicion that stolen or contraband goods are being concealed. Every act or rule which involves the maintenance of public order refers only to the district magistrate and the SDM. Nowhere does the CrPC or the law mention a minister or a chief minister. In a democratic set up, the latter are responsible only for laying down policy guidelines in such matters. The legal assessment of a magistrate cannot be faulted, much less overruled, by the political executive. Another reason for the importance of the DM and SDM is their direct role in the conduct of elections, including the maintenance of electoral rolls and the registration of voters under the Representation of the People Act.

It is essential to have a civil service authority that independently decides on the postings and transfers of IAS officers. Recommended by the Administrative Reforms Commission and promised by the Central government, it has been soft-pedalled for too long.

Supreme court and police reforms

In 2006, the Supreme Court of India delivered a historic judgment in Prakash Singh vs. Union of India instructing central and state governments to comply with a set of seven directives laying down practical mechanisms to kick-start police reform. The Court's directives seek to achieve two main objectives: functional autonomy for the police - through security of tenure, streamlined appointment and transfer processes, and the creation of a "buffer body" between the police and the government (SSC)- and enhanced police accountability, both for organisational performance and individual misconduct.The 7 directives are

- Constitute a State Security Commission (SSC) to:
  (i) Ensure that the state government does not exercise unwarranted influence or pressure on the police
  (ii) Lay down broad policy guideline and
  (iii) Evaluate the performance of the state police
- Ensure that the DGP is appointed through merit based transparent process and secure a minimum tenure of two years
- Ensure that other police officers on operational duties (including Superintendents of Police in-charge of a district and Station House Officers in-charge of a police station) are also provided a minimum tenure of two years
- Separate the investigation and law and order functions of police
- Set up a Police Establishment Board (PEB) to decide transfers, postings, promotions and other service related matters of police officers of and below the rank of Deputy Superintendent of Police and make recommendations on postings and transfers above the rank of Deputy Superintendent of Police
- Set up a Police Complaints Authority (PCA) at state level to inquire into public complaints against police officers of and above the rank of Deputy Superintendent of Police in cases of serious misconduct, including custodial death, grievous hurt, or rape in police custody and at district levels to inquire into public complaints against the police personnel below the rank of Deputy Superintendent of Police in cases of serious misconduct
- Set up a National Security Commission (NSC) at the union level to prepare a panel for selection and placement of Chiefs of the Central Police Organisations (CPO) with a minimum tenure of two years.

T.S.R. Subramanian and Others vs Union of India case 2013 October

In October 2013 Supreme Court issued a series of path-breaking directions to insulate civil servants from political influence. The court stated that officers should have a minimum fixed tenure, they should not act on verbal orders from politicians, and civil service boards should be set up at central and state levels within three months to regulate postings, transfers and disciplinary actions. It also asked the government to pass a comprehensive law on the subject.

The directions were issued on a batch of public interest petitions moved two years ago. The petitioners included several former civil servants led by ex-cabinet secretary TSR Subramanian, former chief election commissioner N Gopalaswami, former election commissioner T S Krishna Murthy, former IPS officer Ved Prakash Marwah, and former CBI directors Joginder Singh and D R Kaarthikeyan.

Accepting their suggestions, the court asked the central and state governments to set up civil service boards to deal with transfers and postings of officials. The judges observed in the judgment that frequent transfers should be avoided so that benefits of the implementation of government policies and programmes could reach the poor. They noted that fixed tenures would promote efficiency and good governance. The judgment said much of the deterioration in the functioning of the bureaucracy was due to political interference.

The petitioners had argued that political masters gave oral instructions to civil servants, thus circumventing the Right to Information Act. That, they said, also encouraged corruption. Therefore, they had asked the court to issue directions to allow officials to act only on written directives.

The issue of "verbal orders" was first cited in the Santhanam committee report in 1964, which had asked civil servants to only act on written orders. That was reiterated by the Shah commission which found examples of oral orders being misused by civil servants during the Emergency in 1975.

The Second Administrative Reforms Commission in 2008 suggested the government constitute a civil service authority to decide on appointments to senior government positions. The court has now asked the government to form a civil services board to oversee transfers and postings. This could have long-term implications for the transfers and postings industry, especially at the state level, where ministers have been known to be whimsical and partisan and transfer and post bureaucrats to positions of choice.

Some cautioned against a fixed tenure. Critics say that there can be many reasons for transferring an incompetent officer. Courts cannot impose provisions of transfers and postings on any government, as those are its prerogative. Critics also said fixing a tenure was not a silver bullet, as in many cases incompetent bureaucrats could get positions from which they might be impossible to dislodge. However, such cases are exceptions and not the rule and can be accommodated.

At present, both the Centre and state governments have their own policies to regulate transfers and postings of officers, with a fixed tenure of three years. Most of these regulations provide for a clause under which the condition of a fixed tenure can be circumvented citing "administrative grounds".

'Civil services boards' (CSBs) are to be headed by the cabinet secretary and chief secretaries, respectively.

These boards, which the apex court now wants in the next three months, will recommend to the government which officer is the best one to man a given position of public importance. Government of the day may accept or reject the board's proposals, but the reasons for overruling will be recorded on paper.

The order is likely to bring greater order and transparency in transfers and posting

Money Laundering

Money laundering is the process of concealing the source of large amounts of money that have been gained through illegitimate means. Money evidently gained through crime is "dirty" money, and money that has been "laundered" to appear as if it came from a legitimate source is "clean" money. Money can be laundered by many methods, which vary in complexity and sophistication.

Money laundering happens in almost every country in the world, and a single scheme typically involves transferring money through several countries in order to obscure its origins. Money laundering, at its simplest, is the act of making money that comes from Source A look like it comes from Source B. In practice, criminals are trying to disguise the origins of money obtained through illegal activities so it looks like it was obtained from legal sources. Otherwise, they can't use the money because it would connect them to the criminal activity, and law-enforcement officials would seize it.

'Money Laundering' as an expression is one of fairly recent origin. The original sighting was in the newspapers reporting the Watergate Scandal in the United States in 1973.

The action of the US President Richard Nixon's "Committee to re-elect the President" that moved illegal campaign contributions to Mexico, and then brought the money back through a company in Miami. It was Britain's newspaper Guardian that coined the term, referring to the process as "laundering".

"Money laundering" is associated with Mafia in the United States. Gangsters there were earning huge sums in cash from extortion, prostitution, gambling and bootleg liquor. They needed to show a legitimate source for these monies. One of the ways in which they were able to do this was by purchasing outwardly legitimate businesses and to mix their illicit earnings with the legitimate earnings they received from these businesses.

Money Laundering as a crime attracted the interest in the 1980s, essentially within a drug trafficking context. It was from an increasing awareness of the huge profits generated from this criminal activity and a concern at the massive drug abuse problem in western society which created the impetus for governments to act against the drug dealers by creating legislation that would deprive them of their illicit gains.

Money Laundering is not an independent crime, it depends upon another crime (predicate offence), the proceeds of which is the subject matter of the crime in money laundering. Money Laundering has a close nexus with organized crime. It is well recognized that through the huge profits the criminals earn from drug trafficking and other illegal means, by way of money laundering could contaminate and corrupt the structure of the State at all levels, this definitely leads to corruption. Further, this adds to constant pursuit of profits and the expansion into new areas of criminal activity.

Through money laundering, organized crime diversifies its sources of income and enlarges its sphere of action. The social danger of money laundering consists in the consolidation of the economic power of criminal organizations, enabling them to penetrate the legitimate economy. In advanced societies, crime is increasingly economic in character. Criminal

associations now tend to be organized like business enterprises and to follow the same tendencies as legitimate firms; specialization, growth, expansion in international markets and linkage with other enterprises.

The amount of money laundered each year is in the billions (US dollars) and poses a significant policy concern for governments. As a result, governments and international bodies have undertaken efforts to deter, prevent and apprehend money launderers. Financial institutions have likewise undertaken efforts to prevent and detect transactions involving dirty money, both as a result of government requirements and to avoid the reputational risk involved. Issues relating to money laundering have existed as long as there have been large scale criminal enterprises. Modern anti-money laundering laws have developed along with the so-called modern "War on Drugs". In more recent times anti-money laundering legislation is seen as adjunct to the financial crime of terrorist financing in that both crimes usually involve the transmission of funds through the financial system (although money laundering relates to where the money has come *from*, and terrorist financing relating to where the money is going *to*).

Methods and Stages of Money Laundering

There are three stages involved in money laundering; placement, layering and integration.

leeway → The available amount of freedom to move or act

Discern → see or be aware of

Placement –This is the movement of cash from its source. On occasion the source can be easily disguised or misrepresented. This is followed by placing it into circulation through financial institutions, casinos, and other businesses, both local and abroad. The process of placement can be carried out through many processes including:

1. *Currency Smuggling* – This is the physical illegal movement of currency and monetary instruments out of a country. The various methods of transport do not leave a discernible audit trail
2. *Bank Complicity* – This is when a financial institution, such as banks, is owned or controlled by unscrupulous individuals suspected of conniving with drug dealers and other organised crime groups. This makes the process easy for launderers. The complete liberalisation of the financial sector without adequate checks also provides leeway for laundering.
3. *Asset Purchase* – The purchase of assets with cash is a classic money laundering method. The major purpose is to change the form of the proceeds from conspicuous bulk cash to some equally valuable but less conspicuous form.

Layering – The purpose of this stage is to make it more difficult to detect and uncover a laundering activity. It is meant to make the trailing of illegal proceeds difficult for the law enforcement agencies. For example, *Material assets bought with cash then sold* – Assets that are bought through illicit funds can be resold locally or abroad and in such a case the assets become more difficult to trace and thus seize.

Integration – This is the movement of previously laundered money into the economy mainly through the banking system and thus such monies appear to be normal business earnings. The known methods used are:

1. *Property Dealing* – The sale of property to integrate laundered money back into the economy is a common practice amongst criminals. For instance, many criminal groups use shell companies to buy property; hence proceeds from the sale would be considered legitimate.
2. *Front Companies and False Loans* – Front companies that are incorporated in countries with corporate secrecy laws, in which criminals lend themselves their own laundered proceeds in an apparently legitimate transaction.

3. *False Import/Export Invoices* – The use of false invoices by import/export companies has proven to be a very effective way of integrating illicit proceeds back into the economy. This involves the overvaluation of entry documents to justify the funds later deposited in domestic banks and/or the value of funds received from exports.

Harmful Effects of Money Laundering:
Money Laundering threatens national governments and international relations between them through corruption of officials and legal systems. It undermines free enterprise and threatens financial stability by crowding out the private sector, because legitimate businesses cannot compete with the lower prices for goods and services that businesses using laundered funds can offer. There are few specific challenges which is posed by Money-laundering activities throughout the world.

Terrorism – Terrorism is an evil which affects each and everybody. Now and then we can find terrorist attacks being made by terrorists. These attacks definitely cannot be done without the help of money. Money Laundering serves as an important mode of terrorism financing. Terrorist organizations raise funding from legitimate sources, including the abuse of charitable entities or legitimate businesses or selffinancing by the terrorists themselves. Terrorists also derive funding from a variety of criminal activities ranging in scale and sophistication from low-level crime to organised fraud or narcotics smuggling, or from state sponsors and activities in failed states and other safe havens. Terrorists use a wide variety of methods to move money within and between organisations, including the financial sector, the physical movement of cash by couriers, and the movement of goods through the trade system. Charities and alternative remittance systems have also been used to disguise terrorist movement of funds.

Threat to Banking System – Across the world, banks have become a major target of Money Laundering operations and financial crime because they provide a variety of services and instruments that can be used to conceal the source of money. Though norms for record keeping, reporting, account opening and transaction monitoring are being introduced by central banks across the globe for checking the incidence of Money Laundering and the employees of banks are also being trained to recognise suspicious transactions, the dilemma of the banker in the context of Money Laundering is to sift the transactions representing legitimate business and banking activity from the irregular / suspicious transactions. Launderers generally use this channel in two stages to disguise the origin of the funds first, when they place their ill gotten money into financial system to legitimize the funds and introduce these funds in the financial system and second, once these funds have entered the banking system, through a series of transactions, they distance the funds from illegal source. The banks and financial institutions through whom the 'dirt money' is laundered become unwitting victims of this crime. Also the loss to bank is found the money in deposits are illgotten

Threat to Economic and Political Stability – the infiltration and sometimes entry of dirty money into legitimate financial sectors and national accounts can threaten economic and political stability. An IMF working paper concludes that money laundering impacts financial behaviour and macro-economic performance in a variety of ways including policy mistakes due to measurement errors in national account statistics; volatility in exchange and interest rates due to unanticipated cross border transfer of funds; the threat of monetary instability due to unsound asset structures; effects on tax collection and public expenditure allocation due to misreporting of income and many more such ways.

Sift → Examine carefully to select what is

Macroeconomic Consequences of Money Laundering

The integrity of the banking and financial services marketplace is heavily reliant on the perception that it functions within a framework of high legal, professional and ethical standards. A reputation for integrity is perhaps one of the most valuable assets of a financial system and institution. Therefore, on a macro level, money laundering poses a risk to confidence in the financial system and its institutions. *"The soundness and confidence in the financial system as a whole could be seriously jeopardised thereby losing the trust of the public..."* if the financial system is caught laundering criminal proceeds.

Other potential macroeconomic consequences of unchecked money laundering have been cited by the International Monetary Fund as inexplicable changes in money demand, contamination effects on legal financial transactions and increased volatility of international capital flow and exchange rates owed to unanticipated cross-border asset transfers. The latter point is especially important and poses a big risk to financial system as money laundering has a direct effect on the Foreign Exchange Market (FOREX) of an economy. The FOREX market is vulnerable owed to the volume of cash involved in the trade. The apparent fund movement, especially from illegal sources, from one jurisdiction to another is capable of exacerbating the exchange rate volatility. This can be devastating especially when there is no corresponding increase in production: hence the domino effect on regulating cash flow and inflation.

Social and Political Costs

There are also social and political costs of money laundering, which have the capacity to be serious if left unchecked or dealt with ineffectively.. Organised crime syndicates can infiltrate financial institutions and acquire control of large sectors of the economy through investment. Organised crime syndicates are in an opportune position to offer bribes to public officials and indeed governments. This implies corruption and laundering go hand in hand. The influence of organised crime syndicates in the economic and political sphere can weaken the social fabric, collective ethical standards and ultimately the democratic institutions of society.

inextricable → impossible to separate

However, what is probably of most importance is the fact that money laundering is inextricably linked to the underlying criminal activity that generated it. Laundering enables criminal activity to continue. It is the dynamic that allows criminal activity of all descriptions to grow and expand. This process –the delivery channel of clean funds –is now so embedded in the 'normal' business environment that chances of controlling it are small and therefore chances of eradicating it are slim to nothing.

There are lots of money-laundering **techniques** that authorities know about and probably countless others that have yet to be uncovered. Here are some of the more popular ones:

- **Structuring deposits** Also known as **smurfing,** this method entails breaking up large amounts of money into smaller, less-suspicious amounts. The money is then deposited into one or more bank accounts either by multiple people (smurfs) or by a single person over an extended period of time.
- **Overseas banks** Money launderers often send money through various "offshore accounts" in countries that have bank secrecy laws, meaning that for all intents and purposes, these countries allow anonymous banking. A complex scheme can involve hundreds of bank transfers to and from offshore banks. According to the International Monetary Fund, "major offshore centers" include the Bahamas, Bahrain, the Cayman Islands, Hong Kong, Antilles, Panama and Singapore.
- **Underground/alternative banking** Some countries in Asia have well-established, legal alternative banking systems that allow for undocumented deposits, withdrawals

and transfers. These are trust-based systems, often with ancient roots, that leave no paper trail and operate outside of government control. This includes the *hawala* system in Pakistan and India and the *fie chen* system in China.

Hawala – Hawala is an alternative or parallel remittance system. It exists and operates outside of, or parallel to 'traditional' banking or financial channels. It was developed in India, before the introduction of western banking practices, and is currently a major remittance system used around the world. In hawala networks the money is not moved physically. A typical hawala transaction would be like a resident in USA of Indian origin doing some business wants to send some money to his relatives in India. The person has option either to send the money through formal channel of banking system or through the hawala system. The commission in hawala is less than the bank charges and is without any complications for opening account or visit the bank, etc. The money reaches in to the doorstep of the person's relative and the process is speedier and cheaper. Cyber Crime – Now one has to confront with hybrid crimes, the crimes with many attributes. According to Capt. Raghu Raman, "Five types of crimes are now converging. Cyber crimes such as identity theft, illegal access to e-mail, and credit card fraud are coming together with money laundering and terrorist activities. Large amounts of money is now stored in digital form. Now you can transfer money through electronic and online gateways to multiple accounts." This convergence leads to a greater problem of tackling of different issues at one time. (Read ahead)

Shell companies These are fake companies that exist for no other reason than to launder money. They take in dirty money as "payment" for supposed goods or services but actually provide no goods or services; they simply create the appearance of legitimate transactions through fake invoices and balance sheets.

Investing in legitimate businesses Launderers sometimes place dirty money in otherwise legitimate businesses to clean it. They may use large businesses like brokerage firms or casinos that deal in so much money it's easy for the dirty stuff to blend in, or they may use small, cash-intensive businesses like bars,car washes, strip clubs or check-cashing stores. These businesses may be "front companies" that actually do provide a good or service but whose real purpose is to clean the launderer's money. This method typically works in one of two ways: The launderer can combine his dirty money with the company's clean revenues -- in this case, the company reports higher revenues from its legitimate business than it's really earning; or the launderer can simply hide his dirty money in the company's legitimate bank accounts in the hopes that authorities won't compare the bank balance to the company's financial statements.

Most money-laundering schemes involve some combination of these methods, although the Black Market Peso Exchange is pretty much a one-stop-shopping system once someone smuggles the cash to the peso broker. The variety of tools available to launderers makes this a difficult crime to stop, but authorities do catch the bad guys every now and then. In the next section, we'll take a look at two busted money-laundering operations.

International efforts to control

Money laundering is a crucial step in the success of drug trafficking and terrorist activities, not to mention white collar crime, and there are countless organizations trying to get a handle on the problem. Because global financial systems play a major role in most high-level laundering schemes, the international community is fighting money laundering through various means, including the Financial Action Task Force on Money Laundering (FATF),

which as of 2014 has 34 member states and organizations. The United Nations, the World Bank and the International Monetary Fund also have anti-money-laundering divisions. India is a member.

The United Nations Office on Drugs and Crime maintains the *International Money Laundering Information Network*, a website that provides information and software for anti-money laundering data collection and analysis. The World Bank has a website in which it provides policy advice and best practices to governments and the private sector on anti-money laundering issues.

- Basel Committee on Banking Regulations and Supervisory Practices The Basel Statement of Principles on the prevention of criminal use of the banking system was a significant breakthrough on the financial front to have some controlling mechanism for money-laundering on an international plane.
- UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances: This UN Convention was one of the historic conventions inasmuch as the parties to the Convention recognized the links between illicit drug traffic and other related organised criminal activities which undermine the legitimate economies and threaten the stability.
- GPML – The Global Programme against Money Laundering was established in 1997 GPML mandate was strengthened in 1998 by the United Nations General Assembly Special Session (UNGASS) Political Declaration and Action Plan against Money Laundering which broadened its remit beyond drug offences to all serious crime. Three further Conventions have been adopted / specify provisions for AML/CFT related crimes:
- International Convention for the Suppression of the Financing of Terrorism (1999)
- UN Convention against Transnational Organized Crime (2000)
- UN Convention against Corruption (2003)
- FTAF: The **Financial Action Task Force (on Money Laundering) (FATF)** is an intergovernmental organization founded in 1989 on the initiative of the G7.The purpose of the FATF is to develop policies to combat money laundering and terrorism financing. The FATF Secretariat is housed at the headquarters of the OECD in Paris.
- International Money Laundering Information Network (IMoLIN): IMoLIN is an Internet-based network assisting governments, organizations and individuals in the fight against money laundering and the financing of terrorism
- Wolfsberg AML Principles: This gives eleven principles as an important step in the fight against money laundering, corruption and other related serious crimes.

Egmont Group of Financial Intelligence Units:The Egmont Group is the coordinating body for the international group of Financial Intelligence Units (FIUs) formed in 1995 to promote and enhance international cooperation in anti-money laundering and counter-terrorist financing.

Asia-Pacific Group on Money Laundering (APG):The Asia/Pacific Group on Money Laundering (APG) is an international organisation consisting of 38 member countries/jurisdictions and a number of international and regional observers including the United Nations, IMF and World Bank. The APG is closely affiliated with the FATF based in the OECD Headquarters at Paris, France. All APG members commit to effectively implement the FATF's international standards for anti-money laundering and combating financing of terrorism.

India

With its growing financial strength, India is vulnerable to money laundering activities even though the country's strict foreign exchange laws make it difficult for criminals to launder money. International Narcotics Control Strategy Report by Bureau for International Narcotics and Law Enforcement Affairs emphasizes India's Vulnerability to money-laundering activities in following words: "India's emerging status as a regional financial center, its large system of informal cross-border money flows, and its widely perceived tax avoidance problems all contribute to the country's vulnerability to money laundering activities. Some common sources of illegal proceeds in India are narcotics trafficking, illegal trade in endangered wildlife, trade in illegal gems (particularly diamonds), smuggling, trafficking in persons, corruption, and income tax evasion. Historically, because of its location between the heroin-producing countries of the Golden Triangle(Myanmar, Thailand and Laos) and Golden Crescent(Iran, Pakistan and Afghanistan), India continues to be a drug-transit country."

Money-laundering in India has to be seen from two different perspectives, i.e., Money laundering on international forum and Money-laundering within the country. As far as the cross-border money-laundering is concerned India's historically strict foreignexchange laws and reporting norms have contributed to a great extent to control money laundering on international forum. However, there has been threat from informal transactions like 'Hawala'. According to Indian observers, funds transferred through the hawala market are equal to between 30 to 40 percent of the formal market. The Reserve Bank of India (RBI), India's central bank, estimates that remittances to India sent through legal, formal channels in 2013 amounted to about U.S. $ 70 billion. Due to the large number of expatriate Indians in North America and the Middle East, India continues to retain its position as the leading recipient of remittances in the world.In India, before the enactment of the Prevention of Money Laundering Act 2002 (PMLA-02), the following statutes addressed scantily the issue in question:

- The Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974
- The Income Tax Act, 1961
- The Benami Transactions (Prohibition) Act, 1988
- The Indian Penal Code and Code of Criminal Procedure, 1973
- The Narcotic Drugs and Psychotropic Substances Act, 1985
- The Prevention of Illicit Traffic in Narcotic Drugs and Psychotropic Substances Act, 1988

However, this was not sufficient with the growth of varied areas of generating illegal money by selling antiques, rare animal flesh and skin and many such varied new areas of generating money which was illegal. Money-laundering was an effective way to launder the black money (wash it to make it clean) so as to make it white. The international initiatives as discussed above to obviate the threat not only to financial systems but also to the integrity and sovereignty of the nations and the recent Hawala episode in India triggered the need for an anti money-laundering law. In view of the urgent need for the enactment of a comprehensive legislation inter alia for preventing money laundering and connected activities, confiscation of proceeds of crime, setting up of agencies and mechanisms for coordinating measures for combating money-laundering etc., the PML Act 2002 came into force in 2005. The amended version came into force in 2013.

Money laundering and stock markets

Laundering of money through stock markets is not a new phenomenon globally. The Financial Action Task Force (FATF) on money laundering conducted a study in 2009 titled

"Money Laundering and Terrorist Financing in Securities Sector" which concludes that "use of securities market for money laundering is an actual threat, use of the same for terrorist financing poses a serious risk".

Fears about incidence of money laundering in the Indian stock markets have been confirmed by the statement made by the Indian Home Minister Mr. Sushil Kumar Shinde at the Interpol conference in Rome in November 2012. Mr.Shinde stated that "It is a cliché to say that terror-funding is the lifeblood of terrorism. Credible intelligence suggests terrorist outfits are investing in stock markets through spurious companies, setting up fictitious businesses and laundering money."

This is not the first time such a statement has been made. In 2007, Mr. M.K. Narayanan, the then National Security Advisor affirmed that terror outfits were reportedly using the Chennai and Mumbai stock exchanges for investing in stock markets through fictitious companies whose links were traceable to some terror outfits.

The Finance Ministry's "White Paper" on "Black Money", 2012 states that two topmost sources of the cumulative financial inflows from April 2000 to March 2011 are Mauritius (41.80 per cent) and Singapore (9.17 per cent). These inflows are not in proportion with the size of their individual economies, and are suspected to be funds of resident Indians which are routed through countries to avoid taxes by a process known as "round tripping" concealing the identity of the investor.

The report also states that "Investment in the Indian Stock Market through Participatory Notes (PN) is another way in which the black money generated by Indians is re-invested in India. The ultimate beneficiaries/investors through the PN route could be Indians and the source of their investment may be black money generated by them. It is at this juncture, that analyzing the possible role of Participatory Notes (PN) in the proliferation and as a conduit for money laundering in India becomes imperative.

In recent times, terror groups have evolved into hybrid organisations combining focus on terror attacks with a high level of financial skills which are seen with global criminal syndicates. Thus, there is a strong possibility that criminally laundered funds are routed back to India through the stock markets by groups linked to terrorism.

Causes of Increase in Money Laundering and Inability to Control

There are various causes for increase in Money Laundering and the few of them can be enlisted as follows which is popularly known as 'Features of an Ideal Financial Haven':

- No deals for sharing tax information with other countries –
- Corporate Secrecy Laws – as the corporate law of certain countries enables launderers to ide behind shell companies.
- Tight Bank Secrecy Laws
- A Government that is Relatively Invulnerable to Outside Pressures (Swiss government)
- Increase in sophistication and employment of professional people for doing the task

Liberty Reserve :-

In 2013, Liberty Reserve, a major global online cash transfer business run out of Costa Rica, has been shut down and its executives arrested to face U.S. charges of laundering $6 billion. According to U.S. Attorney, "Liberty Reserve has become a financial hub of the cybercrime world, facilitating a broad range of online criminal activity including credit card fraud,

identity theft, investment fraud, computer hacking, child pornography and narcotics trafficking." According to the indictment, it moved tens of millions of dollars through shell company accounts maintained in Cyprus, Russia, Hong Kong, China, Morocco, Spain and Australia, among other places.

Bitcoins

Bitcoin is a cryptocurrency that can be transferred through a computer or smartphone without an intermediate financial institution. The concept was introduced in 2008 It is a peer-to-peer, electronic cash system.The processing of Bitcoin transactions is secured by servers called bitcoin miners. These servers communicate over an internet-based network and confirm transactions Bitcoin is accepted in trade by merchants and individuals in many parts of the world. Like other currencies, illicit drug and gambling transactions constitute some of its commercial usage. Although the bitcoin is promoted as a digital currency, many commentators are worried about the bitcoin's volatile exchange rate, relatively inflexible supply, high risk of loss, tax evasion etc.

The Bitcoin industry is getting more eyeballs from authorities in various countries, who are seeking to understand the virtual currency's role in their economy and form regulations to govern the whole ecosystem — as a testimony to the rise of Bitcoin's popularity and the subsequent concerns that arise from using it.

After Thailand ruled Bitcoin as illegal and banned it in July 2013, the US has stepped into the fray as it announced plans to start investigating the virtual currency, seeking to understand and provide regulatory framework,".

At the same time, India's central bank has spoken up to say that it is "watching" Bitcoin, though it has no intention of regulating the currency now.

The Reserve Bank of India had previously acknowledged, however, that virtual currencies "pose challenges in the form of regulatory, legal and operational risks."

In June, US authorities were examining the use of virtual currencies such as Bitcoin amid fears that Americans were using them to evade taxes.

The growing use of digital currency will result in rise in cyber laundering as hacking attacks and online scams take centre stage on Internet, says a latest report. It said the Indian banks and authorities should be alert to money laundering using online black-money route and other techniques as they will expand with the use of digital currency.

"This new techniques of money laundering (using digital currency) includes opening accounts with low cost and little known payment gateways, buying digital currencies, purchasing stolen data, setting up online shops with payment gateways".

Digital-currency is the alternative to the traditional currency, which is used in online transactions.

"Traditional money laundering has often been a secondary process - preceded by an illegal activity, such as drug trafficking but the liberty reserve case(see above) shows that data thefts, hacking attacks and online scams are replacing the traditional crimes and the digital currency is now at the centre of the laundering operations.".

Currently, digital currencies are neither produced by government-endorsed central banks nor necessarily backed by the national currency.

Digital currency is decentralised, controlled by its users rather than the governments."This means it is anonymous, and that, unlike credit cards and PayPal, which block payments from a number of countries, it enables instant payments to anyone, from anywhere in the world."That's why criminals along with some online retailers love it. It is money without any sort of safety net underneath. There's no legislation to protect investment.

PMLA 2012

Prevention of Money laundering Act (PMLA) was enacted in 2002, but was amended thrice, first in 2005, then in 2009 and then 2012. The 2012 version of the amendment received president's assent on January 3, 2013 and the law became operational from February 15 on the notification of finance ministry.

Amendments

- The PMLA (Amendment) Act, 2012 has enlarged the definition of money laundering by including activities such as Concealment, acquisition, possession and use of proceeds of crime as criminal activities.
- Rigorous imprisonment of at least 3 years and up to 7 years
- No upper limit on Fines (earlier it was up to Rs 5 Lakh)
- It will also put the onus on banks, financial institutions, intermediaries or a person carrying on a specified business to report such instances by introducing the concept of a "reporting entity".
- The amendment will also link the provisions of Indian law with laws of other countries.
- It also proposes to make a provision for attachment and confiscation of the proceeds of crime even if there is no conviction, so long as it is proved that a specific property was involved in money-laundering.
- power of Indian courts restored over other foreign courts.
- to monitor money laundering through stock markets and trade. Only financial transactions above a certain level should be monitored to avoid over burdening of existing staff.

Amendments will help India bring its anti-money laundering legislation on par with international standards. It will also address the deficiencies in the present Act that have been experienced by the implementing agencies. It also provides for appeal against an order of the Appellate Tribunal directly to the Supreme Court.

Public Fund Utilisation

Intergovernmental transfers from the centre to the states take place through three channels: statutory and other transfers mandated by the Finance Commission, formula-based transfers for State Plan Schemes through the Planning Commission, and other discretionary transfers by the Planning Commission/ various central Ministries.

The entire tax sharing is a part of the Finance Commission transfers. In the rest of the transfers constituting of grants alone, grants other than those for State Plans now constitutes significant amount. These are generally not formula determined and for the bulk of the amount, are often conditional upon various actions at the state level including putting up the matching amounts. Thus, while the block grants (for State Plan and other block grants) by definition are unconditional transfers and therefore the issue of their utilisation is not a major concern, for the other grants the actual utilisation can be different from the allocations made; if the gap is large, then it can be a cause for concern.

As the extent of such utilisation has caused some concern in recent years, various aspects of this issue merit detailed examination. It is important to study two aspects concerned, namely the design of the schemes, and timing and structure of releases of funds with the objective of finding suitable changes that could contribute to better utilisation. It is done with the help of 16 selected schemes.

In terms of facilitating utilisation, a grantor agency has limited tools in its hands. These include the design of the scheme (to eliminate disincentives for utilisation), the actual transfer mechanism, and the timing. In terms of design, when one is considering conditional transfers which all the schemes under examination are, it shows that the more conditions there are, and the more difficult they are to meet, the less would be the utilisation. For example, a specific purpose transfer without any matching requirement is likely to be utilised to a higher extent than one with such a requirement. Similarly, the transfer mechanism can also influence utilisation; in times of resource constraints, grants on a reimbursable basis have less chance of high utilisation than those provided at least partly on advance basis.

The importance of timing of transfers hardly needs an explanation: it is sufficient to state that grants received at the fag end of the year have little chance of getting spent usefully within that year. In the selected special category states, there is also a seasonal dimension to the issue of timing. All the special category states in India have the problem of extreme weather; in the northeastern states it is the monsoon season that is characterised by heavy rainfall and in the states of Jammu & Kashmir (excluding the relatively lower areas of Jammu), Sikkim and northern parts of Arunachal Pradesh, it is the winter with heavy snowfall. During these months of extreme weather, developmental work is substantially hampered, and funds received cannot be gainfully employed.

When we examine available data with respect to the selected schemes to draw inferences about the suitability or otherwise of present arrangements, certain observations become necessary and they are given ahead.

Entitlement Program – · Demand
· Court can be approached

The Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) (Ministry of Rural Development)

This scheme is the largest rural employment programme designed in India, following up on and subsuming other rural employment programmes like SGRY with the ultimate objective of alleviating rural poverty through job creation. It entitles all persons – below poverty line or not – to at least 100 days of guaranteed wage employment. It was introduced through the notification of the Act first in 200 districts of the country, subsequently extended to another 130 districts. The Act is now applicable to the entire country except fully urban districts.

This is a cost sharing scheme with the centre bearing the full cost of wages of unskilled labour, 75 percent of the cost of material and wages for skilled/semi-skilled labour, and a part of the administrative expenses. The state governments have to bear the remaining costs of material and wages, and administrative costs, along with the costs of unemployment allowance payable to those who cannot be provided wage employment within 15 days of application.

As this is an entitlement programme, there is no predetermined amount of expenditure, either nationally or in any state. The nature of the scheme demands flexibility in the system of financing, and such flexibility is sought to be imparted through first release of the year based on an annual labour budget at the beginning of the year and subsequent release of funds on the basis of subsequent demand. The district level labour budgets and follow-up demands are channelled through the state government. Normally the releases are in two tranches, the first not more than 50 percent of the total approved labour budget. The first instalment is released subject to submission of the Audit report of the year before last.

Releases are subject to physical, financial, administrative and accountability conditions. Utilisation certificate for the previous year is due before second instalment is released, as also certificate regarding the release and receipt of the state share supported by authenticated bank statement.

The flow of funds hinges crucially on the labour budget, the preparation of which is an elaborate decentralised exercise. Starting from the village level, the proposed works have to be costed, checked for conformity with guidelines (e.g., permitted types of works, and approved ratio of materials and wages), conveyed for approval, and aggregated at the next higher level. The process is expected to start on October 2 every year and the state has to provide the detailed labour budget by end January.

Given the essential characteristic of the decentralised nature of this programme, this process of formulating the labour budget is perhaps ideal; however, the uneven administrative capacity of Panchayati Raj institutions (particularly at the block and village level) can create difficulties in the nature of trade-offs between timely submission and quality of the budget.

Data on releases show several types of departures from the expected pattern.
First, there are cases of releases larger than allocations. In a demand-driven programme, this is possible.
Second, there is a clearly noticeable tendency for the bulk of the funds to be released in the last quarter.

Data shows that utilisation was indeed low. States like Andhra Pradesh, Rajasthan, Uttar Pradesh, Uttarakhand, and West Bengal exhibit high levels of utilisation.

Notified wage – linked to CPI Agri labour
Min wage

As NREGA is a demand based scheme and as funds are released based on labour demands projected by the state, whatever slackness is there in the system is due mainly to the incapacity of the states to prepare the labour budget in line with Government of India guidelines in a comprehensive way in time and providing the matching amounts in time. Perhaps greater attention may have to be paid to the capacity building of the state officials to prepare labour demand budget etc. Further, allowing additional categories of work – specific to the state/region – may improve the scope of the project.

Some of the problems associated with claims of State Governments and release by the centre will be minimized once the online system of releases of funds is introduced. Integration of MNREGA with IAY & PMGSY.

Pradhan Mantri Gram Sadak Yojana (PMGSY) (Ministry of Rural Development)

This is a fully centrally funded transfer scheme designed to provide connectivity to rural habitations through construction of upgradation to all-weather roads. The eligible habitations are defined as with population of at least 250 in hill states, desert and tribal areas, and of at least 500 in other areas. Recipient states have to identify or set up an autonomous agency with a distinct legal status under its control that would be designated as the State Rural Roads Development Agency (SRRDA). The SRRDA is the actual recipient of the funds transferred by the central government and is the executing agency at the state level.

Vetted → make careful & critical examination

The administrative setup includes a state level Standing Committee chaired by the Chief Secretary and an Empowered Committee at the central Ministry level. The scheme is a project-based one, with states submitting project proposals as perguidelines and vetted by the Standing Committee, and approved by the Empowered Committee. PMGSY is funded mainly from the accruals of diesel cess in the Central Road Fund.

The state government has the responsibility of providing funds for the proper functioning of the SRRDA, funds for administration of maintenance contracts of PMGSY roads, funds to meet works related expenses not found eligible to be funded by the Ministry under the PMGSY, and to meet cost escalation and other programme expenses.

The transfers are made available to the SRRDAs normally in two instalments. However, the entire annual assistance may be provided in a single tranche for some specified districts (Lahaul-Spiti, Leh and Kargil). Otherwise, the first instalment amounts to 50 percent of the cleared value of projects or annual allocation, whichever is lower. Apart from meeting the general conditionalities of the programme, the release of the first instalment does not have any prerequisite. However, for single tranche releases and for the second instalment, several conditions regarding utilisation of available funds, physical progress, utilisation certificates, audited statement of accounts for the previous year, and certificate of the Bank Manager (where relevant accounts are maintained) have to be met. The second instalment is normally equal to the balance due on the approved cost of awarded works.

The conditionalities are by no means excessive and constitute normal precautions to prevent undue accumulation of funds at the state level and to ensure proper utilisation for the intended purposes.

The extent of utilisation of funds in the selected states do not reveal any major cause for worry and the figures do not indicate anything amiss in the design of the scheme. There is the aspect of timing of releases, however. Much of the releases is expected to be in the first quarter in this scheme.

Vet → Make a careful and critical examination of

Obviate → Remove a need or difficulty

Available data on timing of releases indicate considerable variability between the selected states, with extreme cases of the entire release for the year in the last quarter also noticed.

There are usually several difficulties that arise in the construction of roads in particular – land acquisition, forest clearances, seasonal stoppages and labour-related problems among them. The design of the programme tries to obviate these problems as far as possible by requiring necessary clearances at the proposal stage itself, but it appears that problems arise even after approval.

Indira Awaas Yojana (IAY) (Ministry of Rural Development)

IAY, the scheme for construction and upgradation of houses for the rural poor with special focus on SC/ST, is a cost-shared scheme between the centre and the states in the ratio of 75:25 (90:10 for the North-Eastern states and Sikkim). It is implemented through the District Panchayat or District Rural Development Agency (DRDA)(DRDAs were abolished in 2013), and central funds are made available directly to the district-level agencies. It is designed to provide cash assistance and a (optional) loan at a low rate of interest to each of the beneficiaries.

The beneficiaries receive the assistance on a staggered basis linked to progress of construction. The centre releases the assistance allocated to the district level agencies in two instalments except in the cases of districts with special problems like limited working season; in the latter cases, the entire annual assistance is released in one go. Single instalment releases are conditional upon at least 60 percent utilisation of available funds in the previous year, actual disbursement of the state share in the previous year, audited accounts for the year before last, bank reconciliation statements, and blockwise expenditure statements (or certificate from a Chartered Accountant that funds are directly transferred to beneficiaries' bank accounts from the DRDA). In other cases, 50 percent of the annual allocation is released in the first instalment provided conditions imposed while releasing second instalment of the previous year, if any, are met. Release of the second instalment is conditional upon a proposal for the same and fulfilment of several other conditions including at least 60 percent utilisation of total available funds, full release of state share in the previous years and due for the current year to date, appropriate budget allocation in the current year for the matching state share, submission of audit report for the last year along with action taken report, utilisation certificates for the previous year, approved Annual Plan and all pending progress/monitoring reports. The proposals have to be submitted latest by December 31 every year. Late submission invites progressive cuts in allocated amount.

The provisions summarised above indicate that the conditions imposed are primarily at the time of the second instalment and hence there ought to be little delay in releasing the first instalment. However, in the cases where the decentralised system is fully articulated, the sheer number of agencies involved increases the probability of default in providing some document or the other, which can hold up the proposals.

Block-wise expenditure statements are called for, but it is an enormous task to actually sift through this large number of statements with any degree of necessary attention at the central level. Some of these requirements may perhaps be curtailed and the task of monitoring may also be decentralised to some extent.

National Rural Drinking Water Programme (NRDWP) (Ministry of Rural Development)

The basic objective of this programme is to ensure safe drinking and cooking water for all rural citizens in a sustainable manner through judicious combination of the use and development/improvement of existing water sources, surface water, ground water sources, and rain water harvesting. The coverage also includes all rural schools and Aanganwadis. The scheme focuses on the quality of drinking water and universal coverage, encouraging local government involvement (along with state level organisations) with beneficiaries and other stakeholders, and the introduction of user charges in the interest of financial sustainability.

In the beginning of the financial year, Govt. of India releases 50% of the allocation under NRDWP to each State. The remaining 50% of the allocated funds are released to States based on receipt of specific proposals from the State Governments. after attaining a minimum of 60% expenditure on available funds. Except North-East and J&K, all States are mandatorily required to provide 50% matching State share. North-East and J&K are required to contribute 10% of the central release. State Water & Sanitation Missions (SWSM) in States further release funds to the public health engineering offices of various districts for meeting the expenditure of drinking water schemes in their districts.

Central funds for this programme are transferred directly to the bank accounts of State Water and Sanitation Mission (SWSM), the apex state-level body to be set up, supported by an elaborate institutional structure including district and village level structures. Planning for water is expected to be carried out in bottom-up manner, with priorities for various projects/activities Overall utilisation with respect to this particular programme is not very encouraging. And a part of the reason is to be found in the relatively small first quarter releases, although this alone cannot explain fully the low actual utilisation levels. It is possible that adequate and timely state releases were not forthcoming. Also, there might have been delays in the submission of necessary documentation from the states required for the release of the second instalment in particular. While the centre can only provide incentives to the states to put up the matching amounts, it can try and simplify the conditions for releases of funds to speed up the flow of funds and perhaps thereby improve utilisation.

Rashtriya Krishi Vikas Yojana (RKVY) (Ministry of Agriculture)

The main objective is to provide a boost to the agriculture and allied sector by incentivising the states to maintain and raise their investment in agriculture. The scheme is based on comprehensive district level agricultural plans (C-DAP), which are expected to take into consideration local needs and preferences, as well as constraints (agro-climatic and technical). It encourages convergence with other schemes wherever possible.

The system is driven by eligibility (conditional upon at least maintaining baseline allocation to agriculture and allied sectors in state plan) and formula-based allocations. Fixed proportions of allocations are available for funding specific projects and for supplementary funding in existing schemes/projects.

In the case of this scheme, there is no matching requirement and the system is allocation-based, although project proposals are needed to obtain releases. The first feature should aid utilisation. Fund utilisation was not very good in some states. Clearly, either the states were unable to submit acceptable proposals well in time to take full advantage of the scheme, or the concerned central Ministry was unable to process them in time to make the releases, or both.

Analysis

The review of the individual schemes and their functioning provides us the necessary background to undertake an assessment with a view to improving their effectiveness and utilisation. The following discussion is undertaken in that spirit. To structure the discussion, two main aspects of the schemes are covered: design of the scheme including administrative features, and flow of funds.

Design of the Schemes

The first design feature to be discussed would be the matching requirement of the scheme. Conceptually, the difference between a matching and non-matching grant is that a matching requirement can change budget priorities for expenditures on other heads of expenditure too, since the matching amount has to be taken out of the overall expenditure ceiling, affected one or more of unrelated expenditure heads. A nonmatching grant simply makes more funds available for expenditure in the specified category, in contrast. This is sometimes interpreted to contend that matching central grants to states can 'distort' the priorities of states. The strength of this 'distortion' naturally depends on the matching ratio. Thus, a matching grants are called for when the grantor agency wants to change the pattern of grantee agency's budgetary allocations in favour of the supported service. Too many matching grants in the system of intergovernmental transfers can cause conflicts of interest in the states with only small amounts of free resources; it may become difficult for a state to accommodate so many demands on its meagre resources that remain after meeting contractual obligations.At a more practical level, a matching ratio that cannot be afforded by several states can easily explain lukewarm response of the states to a scheme.

There have been some suggestions of reducing matching requirement further for better off take of funds, but we find no evidence that such reduction is either necessary or sufficient to achieve that. A uniform matching requirement for all states may actually be problematic since the fiscal strength of the states in the group varies widely. However, this a question that has been debated since long and the perceived arbitrariness implicit in a system of varying matching ratios has made such a system politically/administratively unpalatable.

The second design feature that could be important is the basis of the determination of transfers. The schemes can be divided into broadly two types: those based on proposals/plans to be submitted for approval and those based on allocations. Some of the schemes may have elements of both, but the distinction is still valid . MGNREGA is a different category by itself since it is an entitlement programme, although it is based to some extent on annual plans submitted by states. Conceptually, allocation-based programmes should have an edge in terms of utilisation simply because they do not involve the additional effort on the part of the states to prepare credible proposals/plans that may conceivably strain the administrative capabilities of some of the states.

The third, and probably most important, issue is that of delivery mechanism of the scheme. Most of the schemes reviewed, including the some of the flagship-schemes, have two features in common: **(a)** they are expected to be implemented in a decentralised manner, and **(b)** the

state level coordination is entrusted to an agency created for the purpose, with state government participation but autonomous. Many schemes expect the state level agency to be literally only a co-ordinating body, with the focus at the district level or at a further decentralised level. The decentralised structure is expected to cover the whole spectrum of the implementation process starting from preparation of project proposals/plans to actual expenditure, and the flow of funds is designed to percolate down for actual expenditures to be incurred at the most decentralised level. While this is a structure that obviously has an appeal in terms of decentralisation, it can, and probably does, create serious problems of administration and effective delivery. This creates a trade-off between accountability and utilisation. Even in a conceptual sense, the main problems with respect to a decentralised structure of a scheme administered from the central government level in a country like India is: **(i)** the inability to build in enough flexibility to accommodate necessary state-level variations, particularly for the North-eastern states, **(ii)** lack of information and time to assess really decentralised detailed proposals/plans, **(iii)** creating a large number of agencies that have to ensure delivery without the authority or the constitutional back-up that the state governments enjoy, and which add to the costs of governance, and **(iv)** not getting the state governments – without whose involvement, the schemes cannot succeed anyway – fully on board. For these reasons, as also administrative reasons elaborated below, it would be better to involve the state governments fully in the delivery of the schemes and leave it to their choice as to whether a dedicated agency for the scheme is required or not(as under RKVY).

Ensuring a smooth flow of funds under any scheme is absolutely essential to the success in meeting the ultimate objectives of the scheme. This is where the administration of the scheme is tested, and more often than not, this is what determines effective utilisation of the scheme. The review of the structure of the schemes, unfortunately leads one to the conclusion that there is perhaps too little delegation in the system that is creating bottlenecks in the flow of funds, which is also impacting on the effectiveness of the scheme and utilisation of available funds, defeating the objectives to varying extents. To begin with, approval of the project proposals/DPRs/plans is almost invariably at the central level. Given the sheer volume of the job, and the details that have to be gone into, there is a high probability of a trade-off between doing a good job of evaluation and doing so within a reasonable period of time. Unfortunately, slippage in either has negative impact on the scheme. As such, the only way out is to reduce the number of approvals necessary at the central level or eliminate this requirement altogether through delegation of this responsibility to the state government, or an agency designated by it.

Another cause of disruption in the flow of funds is the detailed documentation necessary to obtain the second and subsequent instalments of approved amounts of transfers, including audited accounts and utilisation certificates. With a decentralised system of implementation, default by some lowest level implementation agencies can penalise many such agencies (or delay on the part of a few can cause delay for a larger number), if the documentation (particularly utilisation certificates) has to be consolidated at a higher level for submission. This is where the trade-off between accountability and utilisation shows up. Here again, the solution can only be through delegation – the central Ministries should require utilisation

certificate and audited accounts from the respective state governments only (with a little more time allowed –these should be allowed to be submitted by end-December of a year for the previous year, with second instalments released on the basis of simple statements of expenditures at the state level). Any discrepancy between expenditure statements and utilisation certified can be adjusted while releasing the first instalment of the following year.

The above changes should help significantly in maintaining the time schedule of releases, which can impact on the schedule of implementation. For the special category states, it is particularly important to provide the bulk of funds in the first instalment, so that seasonal constraints can be worked around. Thus it would help these states if 80 percent of the approved funds are released in the first instalment by May 15 of every year, after necessary adjustments. For other states, the normal procedure may be followed.

Sunita Narain on MDM

The tragic loss of 23 young lives because of contaminated food in a Bihar school is unacceptable. But it is also a fact that the Mid Day Meal Scheme, under which cooked food is compulsorily provided to children in government schools, is too important and critical to give up on. The only questions that matter are: why does the scheme not work as well as it should and what can be done to fix it?

Providing nutritious food to children in schools helps address two key problems; hunger and education. In 1982, M G Ramachandran, the then chief minister of Tamil Nadu, set up the nutritious meal programme. In the mid-1990s, the Central government adopted these ideas coming from different states and framed a national midday meal scheme. In 2001, the Supreme Court directed all governments to provide cooked food to all children in primary schools. Since then the scheme has evolved. The Central government agreed to provide free grain (rice and wheat) and funding for transport, cooking cost and recently even an honorarium for the cook. The state government is required to top up this funding; pay for vegetables and pulses; provide infrastructure in schools and manage affairs.

It is estimated that some 117 million children studying up to standard 8 are fed cooked meals every day in some 1.26 million schools and other such centres. The scheme, according to government figures, provides employment to some 2.6 million cooks and helpers. The operations are complicated. Money comes from the Centre in four instalments to states; it then reaches districts and individual schools based on enrolment, off-take and spending. Grain is procured from the storehouse of the Food Corporation of India, transported to districts and then to schools. There are detailed guidelines on how this will work and who will oversee it and even taste the food before serving. It would be difficult to find a parallel in the world for the scale and deployment under this scheme.

But the question remains. Children died in Bihar. There is evidence from many other places that food is not hygienic or nutritious. More seriously, persistent malnutrition continues to shame the country. So what is wrong?

Let me point out the directions in which we should not look for answers. One, we should not look for more schemes or new schemes to replace the old. Two, we should not stop cooking food and replace it with what is considered to be more feasible to supply—biscuits and packaged food that comes from large and small corporates. There is a big push for this. It is not surprising since many eye the Rs 10,000 crore annual budget for meals under the scheme. The solution is to get down to fixing what is broken. It is clear from the states where the programme is working successfully that it requires attention to detail; it needs involvement of those placed the highest in the land—surprise visits, inspections and reports. This will send the signal to the system that food for children is priority.

Second, focus on the paraphernalia of delivery. We put every conceivable scheme in the hands of the hapless (and now increasingly corrupt) local panchayats—each sarpanch manages some 80 different accounts and some 150 different schemes. But there is absolutely no effort to invest in the management support functions of these bodies. If we believe—as we must—that the best institutions for governance are communities then it is time to fix their office. Stop thinking that it is low-cost and voluntary. Management takes money and people. Invest there.

Third, focus on money itself so that we can achieve the change we desire. The Central government pays close to Rs 3 for each primary school child and a little more than Rs 4 for older kids. This is in addition to transport costs (at 2006 rates) and Rs 1,000 per month for cooks and helpers. In Tamil Nadu, the midday meal organiser gets Rs 7,000 per month and the cook and helper are paid Rs 5,000 each. Clearly, this is what it takes.

Chaturvedi Committee on centrally sponsored schemes -

- Bunch the schemes
- 10% fund flexibility to states.

Centre's argument -

- Integration of states → 80 common schemes in all states from centre