Self Learning Material

M.Com - 101(1st Semester)

BUSINESS ENVIRONMENT

COMMERCE

Course : Business Environment

Block I : Introduction to Business Environment

Unit 1 : Business environment- Basics

1.0 Objective
1.1 Introduction
1.2 Concept of Business Environment
1.2.1 Internal Environment
1.2.2 External Environment
1.3 Significance of Business Environment
1.4 Indian Business Environment
1.5 Government and Business
1.6 Let us sum up

Unit 2 : Indian Economy: An overview

2.0 Objectives
2.1 Introduction
2.2 State of Indian Economy
2.2.1 Economic Indicators
2.2.2 External Indicators
2.2.3 Foreign investments & India
2.3 The progressive features of Indian economy
2.3.1 Sectoral overview
2.3.2 Indian Financial system
2.4 Development strategy in India
2.4.1 India's approach in the new millennium
2.4.2 The present day world
2.4.3 Indian public policies
2.5 Let us sum up

Block II : Government Controls and MNCs

Unit 1 : Controls and Industrial Policies

1.0 Objective
1.1 Introduction

1.2 Controls under Planning
1.3 Price Controls
1.4 Industrial Policy
1.5 Let us sum up

Unit 2 : MNCs and MRTP Act

2.0 Objectives
2.1 Introduction
2.2 Scenario of MNC's in India
2.3 MRTP Act
2.3.1 Restrictive Trade Practices
2.3.2 Unfair Trade Practices
2.3.3 Powers of the Commission
2.3.4 Remedies under the Act
2.4 Let us sum up

Block III : Policies and Mobilization of Resources

Unit 1 : Monetary & Price Policy in Developing Country

1.0 Objective
1.1 Introduction
1.2 Monetary Policy- meaning
1.3 Indian Monetary Policy
1.3.1 Features
1.3.2 Monetary Growth
1.3.3 Credit Policy
1.4 Price policy in developing economy
1.5 Let us sum up

Unit 2 : Mobilization of Resources Economy

2.0 Objective
2.1 Introduction
2.2 Mobilization of Resources through Fiscal Policy
2.2.1 Fiscal policy-meaning
2.2.2 Types of fiscal policy
2.2.3 Expenditure and Taxation
2.2.4 Borrowing

2.2.5 Economic & monetary effects
2.3 Indian Scenario
2.3.1 Mobilization of resources through taxation
2.3.2 Containment of current expenditure
2.3.3 Consequences of public borrowing
2.4 Public Enterprise savings
2.4.1 Central Government Public Enterprise
2.4.2 State Government Public Enterprises.
2.5 Household saving behaviours
2.5.1 Changing Structure of Private Savings
2.5.2 Policy incentives for private savings
2.6 Let us sum up

Block IV : Consumer Protection, Capital Market & Foreign Trade

Unit 1 : Consumer Protection

1.0 Objectives
1.1 Introduction
1.2 Consumer protection: Introduction and Definition
1.3 Objects of Consumer protection Act
1.4 Definition of Different terms under the act.
1.5 Redressal Machinery under the Act
1.6 Important Cases
1.7 Consumer rights and responsibilities
1.8 Let us sum up

Unit 2 : Indian Capital Market

2.0 Objectives
2.1 Introduction
2.2 Indian Capital Market- evaluation
2.3 Indian Stock Exchange
2.4 Institutional Investors
2.5 other issues
2.6 Let us sum up

Unit 3 : Direction of India's Foreign Trade

3.0 Objectives
3.1 Introduction
3.2 Trends in India's Foreign Trade
3.2.1 Trend in India's Export
3.2.2 Trend in India's Import
3.3 India's Foreign Trade: Recent trends
3.4 Foreign Exchange Management Act
3.4.1 Regulation and Management of Foreign Exchange
3.5 Let us sum up

Block V : Structural Reforms and IT Revolution

Unit 1 : Structural Reforms

1.0 Objectives
1.1 Introduction
1.2 Structural reforms in Indian economy
1.2.1 Impact on Terms of Trade and Prices
1.2.2 Impact on Household Income
1.2.3 Poverty and Food Security
1.3 India's foreign Policy (Globalization andTrade Promotion)
1.4 Let us sum up

Unit 2 : IT Revolution

2.0 Objectives
2.1 Introduction
2.2 Globalization
2.2.1 Indian stand in terms of Global Integration
2.3 Digital Cash
2.4 E-commerce
2.5 Impact of globalization, WTO,etc.
2.6 Let us sum up

BLOCK - 1 :
INTRODUCTION TO BUSINESS ENVIRONMENT

INTRODUCTION :

This block has been divided into two units so as to enable you to grasp the elementary idea of business environment in Indian scenario. These units have been designed to enable you to understand in details about:

The concept of Business Environment, which includes

- Study of Internal Environment
- Study of External Environment
- Significance of Business Environment, &
- Indian Business Environment
- The relationship between Government and Business
- State of Indian Economy
- The progressive features of Indian economy
- Development strategy in India

Unit 1 will focus on the basic concepts of Business environment and Unit 2 will enable you to know about Indian economy and its implication in business environment. In sum this block will equip you with the broad understanding of issues dimensions, systems comprising business environment under which one has to operate their businesses. The specific of these topics is going to be the focus of Blocks 2, 3, 4 and 5.

While going through these units you are suppose to answer the Self Assessment Questions provided within each of the units to assess yourself about your understanding of the subject matter. In order to update yourself, it is always better if you read business magazines, newspaper etc. regularly.

UNIT 1 : BUSINESS ENVIRONMENT- BASICS

Structure

1.0 Objective
1.1 Introduction
1.2 Concept of Business Environment
  1.2.1 Internal Environment
  1.2.2 External Environment
1.3 Significance of Business Environment
1.4 Indian Business Environment
1.5 Government and Business
1.6 Let us sum up

1.0 Objective

After going through this unit you will be able to:

- Define Business Environment
- Discuss the various components of Business Environment
- Analyze the significance of Business environment
- Critically evaluate the Indian Business Environment
- Establish relationship between Government and Business
- Design your own model for Business Environment

1.1 Introduction

As a commerce graduate, I believe that you might have learned about business in general, quite in details, till now. However, the business environment is such a topic; every time you go through; you will find quite a number of new dimensions. In today's dynamic business world, the study of business environment receives prudent consideration. This unit has been design in such a way that by going through the unit you can able to grasp the concept of business environment. Such conceptual clarity will enable you to learn the various topics in the coming units of this course. The relationship between the government and business is another aspect where special emphasis must be given in business environment. Go through this unit carefully as you will get enough input to make your further units easier to understand.

1.2 Concept of Business Environment :

Environment literally means the surroundings, external objects, influences or circumstances under which someone or something exists. Davis Keith defines the environment of business as "the aggregate of all conditions, events and influences that surround and affect it."

A business house is a part of the society and the business environment has a direct relationship with the rules and regulations as well as policies of the enterprise. The environment may have several impositions which in tern may have several constraints for the business enterprise. Though the environment can be broadly classified into two parts like internal environment upon whom the enterprise do have a control, the other part termed as external environment where the enterprise do not have any control and have to act according to the requirement.

A management system describes the organization and the set of significant interacting institutions and forces in the organization's complex and rapidly changing environment that affect its ability to serve its customers. The firm must continuously monitor and adapt to the environment if it is to survive and prosper. Disturbances in the environment may spell profound threats or new opportunities for the firm. The successful firm will identify, appraise, and respond to the various opportunities and threats in its environment.

1.2.1 Internal Environment :

The management system can be conceptualized on two levels. The first level involves the organization's internal environment. Internally, an organization can be viewed as a resource conversion machine that takes inputs (labour, money, materials and equipment) from the external environment (i.e., the outside world), converts them into useful products, goods, and services, and makes them available to customers as outputs. Some of the important factors affecting the internal business environment are :

- Ideology;
- Organizational values;
- Objectives;
- Rules and Conventions;
- Power;
- Functional aspects;
- Behavioural aspects, etc.

1.2.2 External Environment

The second level of the management system involves the organization's external environment. It consists of all the outside institutions and forces that have an actual or potential interest or impact on the organization's ability to achieve its objectives, e.g.: competitive, economic, technological, political, legal, demographic, cultural, and ecosystem.

Environmental forces create challenges and opportunities for the organization. Managers must react and adapt to changes in their internal and external environment. Globalization is an example of an opportunity for an organization. Improving technologies, such as transportation and communications, have enabled companies to expand into global or worldwide markets. Globalization affects how organizations are managed. Managers must learn to deal effectively with multiple cultures and political systems in the midst of rapidly changing markets and technology. They must be able to anticipate this changing environment and develop the vision and competencies at all levels in their organizations to embrace this dynamic future. Some of the important factors affecting the external business environment are:

- Market;
- Technology;
- Government;
- Economy;
- Power Structure;
- Local Community;
- Competition;
- Culture, etc.

Fig 1.A : Conceptual Model of Business Environment.

Now, let us do a simple exercise.

Self Assessment Question I

Attempt this question :

Fill up the blanks

(i) Environment literally means the ---------------.

(ii) A business house is a ------- of the society.

(iii) Any Business firm must continuously monitor and adapt to the -------------- if it is to survive and prosper.

(iv) Internally, an organization can be viewed as a resource conversion machine that takes inputs and -------- them into outputs.

(v) Environmental forces create ----------- and opportunities for the organization.

Check your answer with the one provided at the end of the unit.

1.3 Significance of Business Environment :

The significance of business environment can be traced in the following lines:

(i) The Internal Environment :

- Organizational Resources: for an overall development, the organization first has to identify their available resources and then tries to develop strategies to utilize those resources to the maximum possible level. This optimal utilization can give lot of advantages like cost effectiveness, drawing utilities, etc.

- R& D and Technological capabilities: with the changes occurred in the technological sector and also any new break through R&D; if can be speculated in time and up to date one self to fit into the new situation by providing training to the employees and procuring the latest technologies, enables an organization to become a business leader in their respective segment.

- Financial capabilities: for procurement, utilization etc. of resources finance plays a major role. Therefore it is important to have a close eye on the position of financial health of the organization.

- Marketing capabilities: the ultimate success of the organization at the end of the day is how much revenue one has earned for the day. The marketing segment plays an important role in clearing the stocks, converts the inventory to revenue, creates a place to sale product or services, attains the customers' satisfaction and paves a way to earn more revenue.

- Operation Capabilities: the optimal utilization of resources can be attaining by way of proper management of their operations. This in turn will reduce the cost. Hence a close look is a must to have a smooth running of the operation processes in the organization.

(ii) The External Environment :

- Suppliers: Development of suppliers' environment have a substantial impact on the company's activity and marketing operations. Supply shortages or delays, labour strikes and other events can affect sales and customer's goodwill in the long run.

- Customers: Every business house is closely looking at the customer's needs, satisfaction level and expectations. As today's market is primarily determined by customers, so the players have no other option but to dance in the tune played by the customers.

- Competitors: the success of an enterprise depends on its ability to satisfy the needs and wants of the consumers better then its competitors. With the change of the world economy by and large the competition becomes very tough and hence every organizations tries to develop strategies to remain in the fray.

- Economic systems: the economic system adopted by a country has a large role to play in determining the future course of action of all the business enterprises in that country. The systems could be Open market economy, Centrally planned economy or Mixed economy. All these economies has certain advantages and disadvantages and accordingly the business houses has frame up their policies to sustain themselves in that economy.

- Political system: the ideology of the political parties in rule has a major role in determining the course of action of

business houses in that country. So the stabilities and efficiency of the political party has a positive impact on the business activities.

- Social & Cultural Factors: the socio-cultural environment encompasses the economic, political, legal or technological factors and at times the buying behaviours of customers, their preferences, attitudes, beliefs, life styles and social values are being made to change over a period of time. Hence the socio-cultural changes affect the business strategies of an organization.

In fine one can find the relevance of studying business environment because:

- It helps an organization to develop broad strategies and long term policies.
- Knowledge about the changing environment will keep the organization dynamic in its approach.
- It enables the organization to foresee the impact of the socio-economic changes at the national as well as international level.
- It enables one to understand their position of strength, weaknesses, opportunities and the threats.

Now, let us do a simple exercise.

Self Assessment Question II

Attempt this question:

Fill up the blanks -

(i) For an overall development, the organization first has to identify their available ---------------.

(ii) The success of an enterprise depends on its ability to satisfy the ----- and -------- of the consumers

(iii) The ideology of the political parties in rule has a major role in determining the ------------ of action of business houses in that country.

(iv) Knowledge about the changing --------- will keep the organization dynamic in its approach.

Check your answer with the one provided at the end of the unit.

1.4 Indian Business Environment :

A new spirit of economic freedom is at work in India, bringing with it great change. A series of ambitious economic reforms, aimed at deregulating the country and stimulating foreign investment have taken place.

India is a democracy of one billion people, and economic reform is a consensus shared by its many political parties. They have been quick to embrace free market enterprise, which has attracted a number of American corporations, including General Electric, General Motors, Hewlett-Packard, Johnson & Johnson, and Microsoft, to name a few.

Bangalore, the location of Acusis' Indian headquarters, is known as the "Silicon Valley of India." The city is a vast entrepreneurial haven, not only to the software engineering industry, but also hosting companies in a variety of other industries, including: aeronautical engineering, research & development, agriculture and biochemistry.

Companies across the globe are coming to realize the opportunity India presents, and are wasting no time in acting. Siemens of Germany, a company which produces and sells power plants, electric meters, hi tech medical equipment and mobile phones has big plans for India. According to CEO Heinrich Von Pierer, "We are going to make new investments in India to the extent of $500 million in the years to come."

The Siemens group in India has 12 subsidiaries employing 10,000 people with combined sales of $650 million, more than six times the sales recorded a decade ago. The company, which also deals in infrastructure projects like airports and highways, plans to build an airport in Bangalore. Siemens plans to set up more hardware and software development centers there.

With the phenomenal expansion of the country's software industry, many Indian policy makers are predicting significant growth rates in the years to come.

1.5 Government and Business :

With the growth of industrial revolution and its acceptance by the community, the entire social and economic structure of society and the concept of human relationship underwent a radical change. The application of science and technology in the industrial field not only crystallized and contracted the widespread and far flung world but also resulted in the concentration of economic and social power on an unprecedented scale. The tremendous power placed in the hands of a few individuals by the advent of technology and science was misused by some individuals which were detrimental to the community as a whole.

The state intervention in the economic and business activities is no longer a political taboo or an economic anathema. It is now regarded as an inescapable part of the obligation of present day governments to redress economic imbalances, to safeguard the interests and welfare of the community as a whole and to plan for overall progress and prosperity of the nation. There is hardly any country today in which the government is not engaged actively directly in the setting up and control the management of economic and industrial enterprises. State intervention or state control lies within two extremes. On one side there is 100 percent control and on the other side there is control according to state requirements. The first is adopted in communist countries which are becoming very rare in today's world and the second one is found in capitalist countries which are being redefined as have adopted the open market economy.

The interventions can be in nutshell attributed to:

- The social conflicts
- Private capitalism which causes the concentration of economic power in few hands.
- Trade union movement
- World wars
- Great depressions in Thirties
- Russian revolution
- Creation of large cities
- MNC's role, etc.

Now, let us do another simple exercise.

Self Assessment Question III

Attempt this question :

Fill up the blanks -

(i) State intervention or state control lies within -------- extremes

(ii) With the growth of industrial revolution and itsacceptance by the community, the entire social and ---------- structure of society and the concept of human relationship underwent a radical change.

Check your answer with the one provided at the end of the unit.

1.6 Let Us Sum Up :

Environment literally means the surroundings, external objects, influences or circumstances under which someone or something exists. A business house is a part of the society and the business environment has a direct relationship with the rules and regulations as well as policies of the enterprise. The two factors effecting business environment are: internal environment and external environment. In business the Government plays a crucial role. The state intervention in the economic and business activities is no longer a political taboo or an economic anathema. It is now regarded as an inescapable part of the obligation of present day governments to redress economic imbalances, to safeguard the interests and welfare of the community as a whole and to plan for overall progress and prosperity of the nation.

1.7 Key Words :

- **Environmental Analysis:** it is the process by which strategists monitor the economic, governmental/legal, market, supplier, technological, geographic and social settings to determine opportunities and threats to their firms.

- **Economic systems:** it is the system adopted by a country which has a large role to play in determining the future course of action of all the business enterprises in that country. The

systems could be Open market economy, centrally planned economy or Mixed economy.

- **R&D :** The Research and Development aspect which is very essential for growth both in Macro level and Micro Level.

1.8 Probable Answers :

SAQ I : (i) Surroundings (ii) Part (iii) environment (iv) converts (v) challenges / threats

SAQ II : (i) resources (ii) needs, wants (iii) course (iv) environment

SAQ III : (i) two (ii) economic

1.9 Reflective Questions:

- Define Business Environment. Discuss the various components of Business Environment.
- Analyze the significance of Business environment. Do you think that study of business environment becomes meaningless because of its high volatility?
- Critically evaluate the Indian Business Environment. Do you think that it is progressing at a right pace?
- Establish relationship between Government and Business. Bring out some justification as to why government has to enter into the business arena.
- Design your own model for Business Environment stating both the internal and external factors.

1.10 Suggested Readings for Unit I :

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.) (chapter 1&2)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004) (chapter 1 & 3)

UNIT 2 : INDIAN ECONOMY :OVERVIEW

Structure

2.0 Objectives
2.1 Introduction
2.2 State of Indian Economy
2.2.1 Economic Indicators
2.2.2 External Indicators
2.2.3 Foreign investments & India
2.3 The progressive features of Indian economy
2.3.1 Sectoral overview
2.3.2 Indian Financial system
2.4 Development strategy in India
2.4.1 India's approach in the new millennium
2.4.2 The present day world
2.4.3 Indian public policies
2.5 Let us sum up

2.0 Objectives :

After going through this unit you will be able to

- List the economic indicators
- Discuss the role of MNC's in India
- Critically evaluate the progressive features of Indian Economy
- Argue on the development strategies adopted by India.

2.1 Introduction :

In the last unit you have learned about business environment and its significance in Indian economy. However, the business environmental study would be meaning less if one is unaware of the economic development of the country and since the subject demands for such background, hence the material has been prepared by taking India as a reference. This unit mainly highlights the progressive features of Indian economy and its development strategies in length.

Apart from this material, it is always better if you read economic dailies to update yourself regarding the progressive features of Indian economy.

2.2 State of Indian Economy :

India is today one of the six fastest growing economies of the world. The country ranked fourth in terms of Purchasing Power Parity (PPP) in 2001. The business and regulatory environment is evolving and moving towards constant improvement. A highly talented, skilled and English-speaking human resource base forms its backbone.

The Indian economy has transformed into a vibrant, rapidly growing consumer market, comprising over 300 million strong middle class with increasing purchasing power. India provides a large market for consumer goods on the one hand and imports capital goods and technology to modernize its manufacturing base on the other.

An abundant and diversified natural resource base, sound economic, industrial and market fundamentals and highly skilled and talented human resources, make India a destination for business and investment opportunities with an assured potential for attractive returns.

Far-reaching measures introduced by the government over the past few years to liberalise the Indian market and integrate it with the global economy are widely acknowledged.

The tenth five year plan document targets a healthy growth rate of 8% for the Indian economy during the plan period 2002 - 07.

2.2.1 Selected Economic Indicators :

India remained relatively unscathed from the 1997-98. Asian financial sector crisis and has maintained a healthy growth rate of over 5 per cent despite recession in major world economies over the past two years. This demonstrates the size, strength and resilience of the Indian economy.

India's GDP for the year 2001-02 was US$ 422 billion. The real GDP growth varied between 6 to 8 per cent per annum (average 6.5 per cent per annum), during the 1990s.

Were it not for the resilience of China and India, the world economy would have been in deep recession in 2002.[1]

The sectoral composition of GDP reflects a transition. While the agricultural and industrial sectors have continued to grow, the services sector has grown at a significantly higher pace - it currently contributes nearly half of India's GDP.

On the external front, cumulative foreign investment inflows have been US$ 50 billion since 1991. This includes over US$ 28 billion of Foreign Direct Investment (FDI) and about US$ 22.6 billion in portfolio investment.

Licensing has been removed from all but six sectors. The Indian government is determined to remove any remaining road blocks, real or perceived. India has one of the most transparent and liberal FDI regimes among the emerging developing economies. The Union government has been continuously opening up new sectors to foreign investment, while enhancing FDI limits in others. The year 2002 saw the opening up of the defence, print media, housing and real estate and urban mass transportation sectors. Some of the key aspects of FDI in the country include:

- 100 per cent FDI is allowed in most sectors except telecommunications (49 per cent), insurance (26 per cent), banking (49 per cent), aviation (40 per cent) and small scale industries (24 per cent). FDI in excess of 24% is permitted in SSI sector on 50% export obligation.
- FDI inflows grew by 65 per cent over the previous year to reach US$ 3.91 billion during 2001-02. The growth of 65 per cent is encouraging at a time when global FDI inflows have declined by 40 per cent.
- The upward trend in FDI inflows has been sustained with FDI inflows during April-June 2002 being double that of the corresponding period in 2001.
- An Economist Intelligence Unit (EIU) report on 'World investment prospects 2002' projects an annual average FDI inflow of US$ 5.3 billion into India during 2002-2006.

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[1]***Source: Morgan Stanley Dean Witter report.***

2.2.2 External sector :

India's external sector posted significant gains during 2001-02, despite the deepening of the global slowdown and uncertainties owing to September 11, 2001 terrorist attacks. The current account registered a surplus after a period of more than two decades. The buoyancy in capital flows bolstered the foreign exchange. Indicators of liquidity and sustainability of external debt improved further. The exchange rate of the rupee remained broadly stable during the year.

"Worldwide FDI flows will decline this year - 25 per cent in developing and 31 per cent in developed countries - but India is one of the few countries where it will go up," Karl Sauvant, Director, UNCTAD told UNI.[2]

According to a recent report on global foreign direct investment inflows, India has been rated the seventh most attractive destination in the world for FDI for 2001.

Weak external demand adversely affected India's export performance during 2001-02. This was counterbalanced by the listless domestic demand for imports and the softness in international oil prices for a greater part of the year. As a result, the trade deficit, on balance of payments basis, declined from US$ 14.4 billion during 2000-01 to US$ 12.7 billion during 2001-02. The invisible account continued to provide support to the balance of payments with the surplus increasing from US$ 11.8 billion during 2000-01 to US$ 14.1 billion during 2001-02. The current account recorded a surplus of US$ 1.4 billion. Net capital flows were higher at US$ 9.5 billion during 2001-02.

2.2.3 Foreign Investments & India

"...A survey on FDI conducted by FICCI shows that the performance of 385 foreign investors operating in India was satisfactory, with 61 per cent reporting profits or break-even. And around 51 percent of the respondents have expansion plans on the cards. Despite the overall conditions of slowdown, over 71 per cent respondents reported a capacity utilization of 50-75 per cent.

As many as 93 per cent of the respondents find the handling of approvals and applications at the Centre to be good to average. The

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[2]*Source: News reports, 25 November 2002.*

simplification of the approval procedure at the Centre can be gauged by the fact that the number of applications going through the automatic route has raised from 16 per cent in 2000 to 29 per cent in 2001. Also the ratio of FDI inflows to approvals had gone up to 52.8 per cent in 2000 compared to 29 per cent in 1996.

Around 63 percent find the overall policy framework to be good to average. "The apparent increase in the FDI inflow shows that the improved policy environment is having a positive impact," says a senior official at FICCI. FDI this year has risen by 61 per cent to US$ 2.37 billion in April- November 2001 compared to US$ 1.47 billion in the corresponding period last year. Besides 70 per cent feel that bringing funds into the country is relatively easy and 69 per cent say that funds repatriation can be carried out fairly easily..."[3] India's foreign exchange reserves have risen significantly to over US$ 68 billion by the end of December 2002. This has provided the much needed stability to the exchange rate and strengthening of the rupee.

The external debt to GDP ratio of the country has improved significantly from 38.7 per cent in 1992 to around 22.3 percent in 2001. Among developing countries, India has one of the lowest external debts to GDP ratios.

The value of foreign trade has increased substantially. Both exports from and imports into India are increasing. The total volume of foreign trade in 2001-02 was over US$ 95 billion. In order to boost exports and attract foreign investments, the government had announced in April 2000 the establishment of Special Economic Zones (SEZs) policy. The SEZs would offer world class infrastructure, attractive financial and tax incentives and procedural ease of a duty-free trading area. For all practical purposes, units located in the SEZs are given deemed foreign territory treatment.

A unique feature of the transition of the Indian economy has been an element of high growth with stability. Both at the central and state levels and across political affiliations of the Indian federal and state polity, there is consensus on further economic liberalisation. The reforms programme and the market oriented policies of the government are irreversible.

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[3]***Source: India Business World, April 2002.***

Now, let us do a simple exercise.

Self Assessment Question I
Attempt this question:

State whether the following statements are true or false:

(i) India is today one of the four fastest growing economies of the world.

(ii) The Indian economy has transformed into a vibrant, rapidly growing seller's market.

(iii) India's GDP for the year 2001-02 was US$ 422 billion.

(iv) Licensing has been removed from all but five sectors.

(v) The current account registered a surplus after a period of more than two decades.

(vi) For all practical purposes, units located in the SEZs are given deemed foreign territory treatment.

Check your answer with the one provided at the end of the unit.

2.3 Progressive Features :

2.3.1 Sectoral overview :

- **Agriculture**

Two thirds of India's population lives in rural areas. Agriculture and related activities are the main source of livelihood for them. The performance of the agricultural sector has continuously been improving (over many decades), helping the country achieve a surplus in food grains production. This has been facilitated through new agricultural techniques and tools acquired by Indian farmers, mechanization, use of high yielding varieties of seeds, increasing use of fertilizers and irrigation facilities, on-going operational research in the country's numerous agricultural universities and colleges, etc. With liberalisation of trade in agricultural commodities, India enjoys a competitive advantage in a number of agricultural and processed food products exports.

An overview of Indian Agriculture
(Production side)

<u>Comparative advantages:</u>

- Second largest arable land in the world
- Diverse agro-climatic zones across the country,
- Round the year sunshine
- Potential to cultivate a vast range of agricultural products
- Large marketable surpluses and abundant raw material for processing
- Vast pool of skilled manpower in research and extension

These advantages being leveraged, for India to be a leading food supplier to the world.

While the share of agriculture in GDP (26.6 per cent in 2000-01) is declining because of faster growth of the services sector, production in absolute terms has been steadily raising. Agriculture accounts for 62 per cent of total employment. Some other key highlights include:

- India had a buffer stock of food grains (wheat and rice) of nearly 50 million tonnes (Dec. 02) as against the target of 20 million tonnes at any given point in time. This has helped India enter the food grains export market in a significant way.
- India is the largest producer and consumer of tea in the world and accounts for 28 per cent of world production and 15 per cent of world trade.
- Agri-exports account for 13-18 per cent of total annual exports of the country. Agri-exports amounted to over US$ 6 billion in 2000-01.
- The value of agricultural imports of inputs like fertilizers, etc. are approximately one-fourth the value of exports.

Table 1.1 India's Rank in World Production

	India	India's Rank in World Production
Arable Land (Million ha)	151	2
Irrigated Land (Million ha)	55	1
Wheat	72	2
Rice, Paddy	124	2
Coarse grains (including maize)	29	3
Milk	91	1
Fruits	47	2
Vegetables	82	2
Edible Oilseeds	25	3
Pulses	15	1
Sugarcane	245	2
Tea	0.85	1
Cattle (million)	186	2

- **Manufacturing**

India has moved from an agrarian to a manufacturing and services led economy. The manufacturing sector contributes around one-fourth of the total GDP. The country has built a diversified industrial base comprising traditional handicrafts, small, medium and large manufacturing companies and high technology-oriented products. The industrial output has grown to approx US$ 65 billion. The country has emerged as an important global manufacturing hub - many multinational corporations (MNCs) like Pepsi, General Electric (GE), General Motors (GM), Ford, Suzuki, Hyundai, Gillette, LG, etc. have followed India's economic liberalisation process from close quarters and set up successful operations in the country in recent years. They have been able to leverage cost advantages while adhering to global manufacturing facilities.

Companies in the manufacturing sector have consolidated around their area of core competence by tying up with foreign companies to acquire new technologies, management expertise and access to foreign markets. The cost benefits associated with

manufacturing in India, have positioned India as a preferred destination for manufacturing and sourcing for global markets.

- **Services**

The services sector currently accounts for almost half of the country's GDP. Expanding at a rate of 8-10 per cent per annum, services is the fastest growing sector in the Indian economy. In fact, the growth in India's GDP, despite the global slowdown, is attributed largely to its strong performance.

Availability of highly skilled workers has encouraged many international companies to carry out their research and development activities in India. IT, biotech, tourism, health, financial services and education hold the promise of sustainable high growth. To give a perspective:

- The Indian IT industry has grown from US$ 0.8 billion in 1994-95 to US$ 10.1 billion in 2001-02. Domestic software has grown at 46 per cent while software exports have grown at 62 per cent over the last 5 years.

- The last decade has seen the Indian entertainment industry grow exponentially. The key drivers for this have been technology and the government's recognition of the importance of the sector. The industry is expected to grow at a compound annual growth rate (CAGR) of 27 per cent. Revenues are projected to increase from US$ 3 billion in 2002 to US$ 10 billion in 2005.

- Information Technology enabled Services (ITeS) with elements like call centers, back office processing, content development and medical transcription are key to rapid growth. The sector has an employment potential of 1.1 million by 2008.

- **Infrastructure**

The infrastructure sector in India, traditionally reserved for the government, is progressively being opened up for private sector participation.

- **Ports**

The country has a 7500 km long coastline dotted with numerous major and minor ports. The areas that have been identified for participation and investment by the private sector include leasing

out existing assets of the ports, construction of additional assets such as container terminals, cargo berths, handling equipment, repair facility, captive power plants and captive facilities for port based industries. Foreign investment up to 100 per cent equity participation is permitted in ports through the automatic route for construction and maintenance of ports and harbours.

A number of private companies have already set up port facilities in the country. have been able to compete with existing major ports. Many multinational and Two greenfield ports i.e. Pipavav and Mundra in Gujarat have been set up through private participation and these domestic players have taken over existing port facilities and are operating them. Recently the container terminal at Chennai port has been taken over by an Australian port major.

- **Roads**

India has the second largest road network in the world, spanning 3.3 million kilometers. Most of the private investment in this sector has traditionally been through the build-operate-transfer schemes. However, now many new projects are being bid out on toll collection mechanism.

Currently, the National Highways Authority of India (NHAI) is implementing the National Highways Development Project (NHDP). NHDP is the largest ever highway development project to be undertaken in the country. The project involves widening of over 13,000 km of highways in the country. The investment for this project is estimated at US$ 13.2 billion at 1999 prices. The project has been broken up into a large number of smaller segments, many of which have been commissioned. Currently work has been completed on 1976 kilometers and another 5222 kilometers of length is under construction.

- **Airports**

India has 122 airports, controlled by the Airports Authority of India (AAI). The total passenger traffic handled by these airports in 2001-02 was over 40 million, while the cargo traffic handled was around 854,000 tonnes. The government is in the process of leasing out the four major international airports at Delhi, Mumbai, Chennai and Kolkata to private operators.

● **Power**

Power Sector, hitherto, had been funded mainly through budgetary support and external borrowings. But given the budgetary support limitation due to growing demands from other sectors, particularly social sector and the severe borrowing constraints, a new financing strategy was enunciated in 1991 allowing private enterprise a larger role in the power sector.

The all India installed capacity of electric power generating stations under utilities was 104917 MW as on March 2002 consisting of 26261 MW hydro, 74428 MW thermal, 2720 MW nuclear and 1507 MW wind. A capacity addition target of 4764 MW consisting of 1536 MW of Hydro and 3228 MW of thermal was envisaged for the year 2001-02 of which 3115 MW consisting of 1106 MW of hydro and 2009 MW of thermal was achieved.

Presently, restructuring and regulatory reforms include bringing about reforms in the State Electricity Boards (SEBs) through establishment of the State Electricity Regulatory Commissions. Reforms are progressing steadily in the sector and privatisation of SEBs have already begun. The government is also planning a massive restructuring of the finances of SEBs and is looking at a one-time settlement of dues of SEBs. In effect, a large amount of liquidity will be injected in the sector.

The Ministry of Power has also formulated a Blue Print to provide reliable, affordable and quality power to all users in the country i.e. power on demand by 2012. This requires huge increase in generation capacity, upgradation of existing generation facilities and also the transmission and distribution network.

● **Telecommunications**

India's telecommunications network ranks among the top ten countries in the world. One of the world's largest and fastest growing telecom markets, the country has an investment potential estimated at US$ 39 billion by 2005 and US$ 69 billion by 2010.

Despite a strong base of a billion people, the country has a low telephone density of approximately 5 per cent, estimated to grow to 7 per cent by 2005 and 15 per cent by 2010. The government had allowed private participation in cellular services in 1992. The sector witnessed partial de-regulation between 1994 and 1999. The

government announced the New Telecom Policy (NTP) in 1999 to further de-regulate the sector with respect to services like basic, international long distance (ILD), national long distance (NLD) and Wireless in Local Loop (WLL) among others.

● **Financial sector**

The Indian financial sector reforms aim at improving the productivity and efficiency of the economy. It remained stable, even when other markets in the Asian region were facing a crisis. The opening of the Indian financial market to foreign and private Indian players, has resulted in increased competition and better product offerings to consumers.

The financial sector has kept pace with the growing needs of corporates and other borrowers. Banks, capital market participants and insurers have developed a wide range of products and services to suit varied customer requirements. A trend towards mergers and acquisitions is expected in the near future due to the compulsions of size and limitations of growth of business on its own vis-à-vis growth through acquisitions. The recent favourable government policies for enhancing limits of foreign investments in the banking sector have generated interest from global banking majors.

The Reserve Bank of India (RBI) has ushered in a regime where interest rates are more in line with market forces. This has increased the credit disbursements in the economy which, in turn, will boost industry. Banks and trade financiers have also played an important role in promoting foreign trade of the country.

The potential of the sector is evident from existing and projected estimates:

- Presently the total asset size of the Indian banking sector is US$ 270 billion while the total deposits amount to US$ 220 billion in a banking network of over 66,000 branches across the country.
- The size of the insurance market with only 20 per cent of the insurable population currently insured, presents an immense opportunity to new players. Foreign insurance majors have entered the country in a big way and started joint ventures in both life and non-life areas.

● **Disinvestment**

The government over the past decade has been increasingly redefining its role from being a provider of goods and services to that of a policy maker and facilitator. Towards this objective, the government has been consistently divesting its stake in various public sector undertakings (PSUs).

- Between 1991 and 2002, the government divestment process had yielded US$ 6.3 billion to the national exchequer.

● **Policy Initiatives**

- There has been a paradigm shift in the government's approach to selling its stake since 31 March, 2000. From selling minority stakes, the government has started divesting majority holdings and transferring management control to strategic investors in profitable undertakings.
- The government had set up a separate ministry in late 1999 to facilitate the divestment process. It has also set up a cabinet committee and an inter-ministerial group to consider and facilitate specific divestment proposals.
- Some of the key highlights of the disinvestment policy are:
- The 1991-92 budget considered divestment of 20 per cent government equity in select PSUs in favour of public sector institutional investors, mutual funds and workers.
- The Disinvestment Commission (1997-99) made specific recommendations on 58 specific PSUs with respect to disinvestment feasibility and the methodology to be adopted.
- The second phase of disinvestment started in 1998-99. Each year since 1999, the government is pushing ahead with reforms and disinvestments. The government has now declared its willingness to reduce its stake below 26 per cent in non-strategic PSUs.

● **Opportunities**

The successfully privatized projects during 2002-03 include the long-distance international telecom carrier - Videsh Sanchar

Nigam Limited (VSNL); petroleum marketing company - IBP; petrochemical company - Indian Petrochemicals Limited (IPCL); metal manufacturing companies - Hindustan Zinc Limited and Bharat Aluminium Company; hotels belonging to India Tourism Development Corporation (ITDC) and the country's largest small and medium car manufacturing company - Maruti.

The government is now considering disinvestments of the Shipping Corporation of India and two state trading corporations (STC and MMTC) among others. One of the biggest privatisation projects that the government has initiated is the leasing of international airports at the four metropolitan cities of Delhi, Mumbai, Chennai and Kolkata. The privatisation mandates will provide a good opportunity to both domestic and foreign investors to pick up stakes in well-performing assets.

2.3.2 The Indian Financial System :

India has a large, sophisticated financial system including private and public, formal and informal actors. In addition to formal financial institutions, informal institutions such as family and moneylenders are important sources of capital. India has substantial capital resources, but as Table 1 indicates, the bulk of this capital resides in the banking system. In the formal financial system, lending is dominated by retail banks rather than the wholesale banks or the capital markets for debt. The primary method for firms to raise capital is through the public equity markets, rather than through private placements.

● The banking system

Prior to independence from Britain, the banking system was entirely private and largely family-operated. In the pre-war period, the family-run banks often invested in new ventures. After Independence, the Reserve Bank of India (RBI) and the State Bank of India were nationalized, with the State Bank of India continuing to play the role of banker to government agencies and companies. Then, in 1969, the next 14 largest banks were nationalized. With the State Bank of India, the state controlled 90% of all bank assets. The nationalized banking system became an instrument of social policy. During 1969-91, the financial position of the banks progressively weakened, due to loss-making branch expansions, ever-

strengthening unions, over standing, and politicized loans. Until 1991, depositors were reluctant to use banks because although their savings were safe, the government set deposit interest rates below the rate of inflation.

By 1991, the entire bank system was unprofitable and nearing collapse. The socialized banking system had other perverse effects. For example, although the bank managers were civil servants and very risk-averse, they could offer below-market interest rates. This created excessive demand for funds, but, quite naturally, bankers extended the loans to their safest customers. These were primarily the large firms owned by the government, which operated the largest steel, coal, electrical, and other manufacturing industries. The other large bank borrowers were the giant family conglomerates such as the Tata and Birla group. This increased the group's economic power, but did not lead to economically efficient decisions about how to deploy capital. Small firms were starved for capital. Thus the Indian banks provided no resources for entrepreneurial firms.

● Equity markets

The first Indian stock markets were established during the British Raj era in the 19th century. During the early part of the 20th century, Indian equity markets actively financed not only banking, but also the cotton and jute trades (Schrader, 1997). In 1989 there were 14 stock markets in India, though Bombay was by far the largest (World Bank, 1989). The socialization of the economy and particularly banking after independence reinforced the strength of the stock markets as a source of capital, and by the 1960s, India had one of the most sophisticated stock markets in any developing country.

There were several reasons for the growth of the Indian stock market. Motivated by its egalitarian principles, the government supported the stock markets as an instrument for reducing the concentration of ownership in the hands of a few industrialists (an outcome of the government policy of providing below-market interest loans to the large family conglomerates).

Second, the government industrial licensing policy instituted in 1961 meant that businesses had to apply for government permission to establish new ventures. Permissions were given only

in the context of the Soviet style national plans for each sector. There was a strong element of favoritism in where one receives permission. Most important, due to government central planning controls, shortages were endemic, and thus, permission to produce was a guarantee of profits. The distortion these policies created by encouraging concentration were meant to be offset by RBI stipulation that private sector borrowers could not own more than 40% of the firm's equity if they wished to receive bank finance. In 1973 the government required all foreign firms to decrease ownership in their Indian subsidiaries to 40%. Faced with a choice between selling stakes privately and listing on the stock exchanges, most firms chose the latter and issued new stock, which led to a large increase in public ownership of such companies. So, to raise money the private sector became reliant on stock markets. Investors, large and small, readily financed ventures since the shortages induced by the planning system guaranteed a ready market for anything produced.

Curiously, the retention of 40% of the equity by the core investors meant that in reality they controlled the firm. The 40% regulation did not liberalize the markets as much as one might expect. Because loans were also necessary for firms and this required collateral in fixed assets, new entrepreneurs were restricted to sectors with asset heavy projects. This disadvantaged the service sector, resulting in even greater concentration, and equity markets focused on financing low risk projects. Moreover, the public's enthusiasm for firms operating within a licensed industry meant that it was difficult for other new firms to secure capital through listing on the stock exchanges.

In 1991, as part of a large number of financial reforms, the Securities and Exchange Board of India (SEBI) was created to regulate the stock market. At the time, there were 6,229 companies listed on all the stock exchanges in India (RBI, 1999, p. 16). The reforms and loosening of regulations resulted in an increase in the number of listed companies to 9,877 by March 1999, and daily turnover on the stock exchanges rose to 107.5 billion rupees (US$2.46 billion) by December 1999. One reform was the removal of a profitability criterion as a requirement of listing. To replace the profitability requirement, it was stipulated that a firm would be de-listed if it did not earn profits within three years of listing. This reform meant unprofitable firms could be listed, providing an exit

mechanism for investors. Not surprisingly, there was a dramatic increase in the listings of firms, many of which could be considered as high technology. In terms of experience, India contrasted favorably with most developing countries, which had small, inefficient stock markets listing only established firms. Even in Europe, until the creation of new stock markets in the mid-1990s, it was extremely difficult to list small high technology firms (Posner, 2000). But, although these stock markets provided an exit opportunity, they did not provide the capital for firm establishment. Put differently, accessible stock markets did not create venture capital for startups; they merely provided an opportunity for raising follow-on capital or an exit opportunity.

● Other institutional sources of funds

India has a strong mutual fund sector that began in 1964 with the formation of the Unit Trust of India (UTI), an open-ended mutual fund, promoted by a group of public sector .financial institutions. Because UTI's investment portfolio was to consist of longer-term loans, it was meant to offer savers a return superior to bank rates. In keeping with the risk-averse Indian environment, initially UTI invested primarily in long-term corporate debt. But, UTI eventually became the country's largest public equity owner as well. This was because the government controlled interest rates in order to reduce the borrowing costs of the large manufacturing firms that it owned. These rates were usually set well below market rates, yet UTI and other institutional lenders were forced to lend at these rates. In response, firms started issuing debt that was partially convertible into equity in order to attract institutional funds. By 1985, the conversion of these securities led to UTI becoming the largest owner of publicly listed equity (UTI Annual Report, 1985). By 1991, the equity portion of the UTI portfolio had grown to 30% (UTI Annual Report, 1991). In 1992, in tandem with banking sector reform, permission to form privately-owned mutual funds (including foreign-owned funds) was granted, leading to gradual erosion in UTI's then-dominant market share. Until April 1999, mutual funds were not allowed to invest in venture capital companies. Since then, the mutual funds have been allowed to commit up to 5% of their funds as venture capital, either through direct investments or through investment in venture capital firms.

But, the mutual funds have not yet overcome their risk-averse nature and invested in venture capital, either directly or indirectly through investment in venture capital funds. Certainly, should the mutual funds decide to invest directly in firms, there would be operational issues regarding the capability of mutual funds to perform the venture capital function. The largest single source of funds for US venture capital funds since the 1980s has been public and private sector pension funds. In India, there are large pension funds but they are prohibited from investing in either equity or venture capital vehicles, thus closing of this source of capital. In summation, prior to the late 1980s, though India did have a vibrant stock market, the rigid and numerous regulations made it nearly impossible for the existing financial institutions to invest in venture capital firms or in startups. Nearly all of these institutions were politicized, and the government bureaucrats operating them were risk-adverse. On the positive side, there was a stock market with investors amenable to purchasing the equity in fairly early stage companies. It was also possible to bootstrap a firm and/or secure funds from friends and family-if one was well connected. But, no financial intermediaries comfortable with backing small technology-based firms existed prior to the mid-1980s.

Now, let us do a simple exercise.

Self Assessment Question II

State whether the following statements are true or false:

(i) India enjoys a competitive advantage in a number of industrial and processed food products exports.

(ii) Information Technology enabled Services (ITeS) with elements like call centers, back office processing, content development and medical transcription are key to rapid growth.

(iii) Two Greenfield ports i.e. Pipavav and Mundra in Gujarat have been set up through government participation.

(iv) The government had set up a separate ministry in late 1999 to facilitate the divestment process.

(v) By 1991, the entire bank system was unprofitable and nearing collapse.

Check your answer with the one provided at the end of the unit.

2.4 Development Strategy in India :

In managing the process of economic integration that is driven by several forces, developing countries face challenges from a world order that is particularly burdensome on them. Yet, it is necessary for the public policy to manage the process with a view to maximizing the benefits to its citizens while minimizing the risks; but the path of optimal integration is highly country-specific and contextual. On balance, there appears to be a greater advantage in achieving a well-managed and appropriate integration into the global process, which would imply more effective - but not necessarily intrusive or extensive - interventions by governments.

Globalisation, is seen to be the world's "mega-trend" over the next 15 years, causing the global economy to grow by about 80% compared with 2000, and raising average income per head worldwide by about 50% over the same period. The benefits will be unevenly distributed but there will be a much richer world.

Economists world over believe, that most of this growth will be in Asia, especially in China and India, driving Asia to displace the west over the next 15 years as the focus of global economic dynamism. The impact of that shift will be economic and political, pulling Washington's attention away from Europe and the Middle East and towards the emerging 21st century superpowers. In this backdrop, it is important to carefully examine the issues underlying India and the global economy to draw strategies.

If we look at the Indian experience since independence, we find that export pessimism permeated the policy stance throughout the early decades of our planning. Import substitution was the principal instrument of trade policy and was regarded in the early years as not only the correct strategy but also inevitable in a continental economy like India. The gulf crisis and its impact on India provided several lessons for us, and one of them was that a relatively closed economy does not provide immunity from a foreign exchange crisis. Incidentally, India excelled in managing the crisis and emerged as one of the very few countries in the world, amongst both the developed and the developing, to have never defaulted on its external obligations. In the aftermath of the Gulf crisis, policy actions were initiated as part of the overall macroeconomic management well coordinated to simultaneously achieve stabilization

and structural change. External sector policies designed to progressively open up the Indian economy formed an integral part of the strategy for structural reforms.

In this context, improvement in exports, both merchandise and invisibles were recommended. Suggestions were made regarding modulation of import demand on the basis of the availability of current receipts to ensure a level of current account deficit consistent with normal capital flows. Further, Indian policy makers took up measures to enhance non-debt creating flows to limit the debt service burden. A switch over to market-determined exchange rate; building up the foreign exchange reserves to avoid liquidity crises and elimination of the dependence on short-term debt were some of the most important changes that were suggested. It is evident that these changes in the external sector policies of the 1990s, paid rich dividends in terms of growth and resilience to a series of external and domestic shocks.

2.4.1 India's approach in the new millennium

In the 21st century, there has been a dramatic shift in India's approach to external sector management in tune with the changing circumstances. First, with the emergence of marginal current account surplus, the sustainability of India's current account deficit may not be a problem though the deficit on her trade account persists and has been increasing. Second, the main contributors to the positive outcome in India's current account are workers' remittances and export of software, both being a result of process of global integration. Third, the exchange rate regime as well as external debt management has served India well, especially the avoidance of sovereign debt through commercial borrowings. The new policy regime helped India withstand several global crises while maintaining a respectable growth. Fourth, the management of capital account has acquired the primary focus rather than the current account. Fifth, a judicious integration with the global trade regime has imparted some competitive efficiency and confidence to the domestic industry and perhaps, even to commercial agriculture though to a limited extent. Finally, it has become evident that the management of the external sector is closely linked to the domestic sector and the major thrust of Indian public policy is now on managing the integration.

In brief, India has moved from managing external sector to implementing an optimal integration of domestic and external sectors, and the global economy.

More recently, however, a debate in the rest of the world has been in evidence on the challenges likely to be faced by the global economy on account of progressively increasing global integration of the Indian economy. There is a need to have an ongoing appreciation of how the global economy is responding to the challenges of our integration while we move forward with our own agenda of securing an optimal integration.

2.4.2 The present day world :

Currently, the major issue in the global economy appears to be the significant build up of current account imbalances. The current account deficit of U.S.A. has been rising and is around 5% of GDP, while current account surpluses are noticed in Asia and to some extent in Latin America and Russia. The external financing of the US deficit moved away from equity in the late nineties to debt in the recent years, possibly reflecting a perception of productivity growth in the former period and fiscal stress in the latter. The official reserves played a greater role than in the past in financing the US current account deficit in recent years.

Further, the simultaneous emergence of China and India with significant competitive strengths in trade in goods as well as services will have to be accommodated by the global economy. Thus, the issue for the immediate future is that both, correcting current global imbalances and integrating the two Asian giants, may have to take place simultaneously in the global economy.

It is evident that China and India will have to give a high priority to generating employment. Both these emerging economies are poised for substantial increases in productivity. Consequently, the global economy will have to consider the implications of these developments on prices, exchange rates, wages and structures of employment in industrialised countries. Over the medium term, it is felt that outsourcing will grow in geometric progression, particularly to India, and may also cover high-end research and development. One sector where the industrialised economies continue to show

considerable strength and dominance is the financial sector, partly attributable to the confidence factor in financial markets that favours the industrialised economies and traditional international financial centres. It is essential for India to carefully monitor the developments in both real and financial sectors, and to modulate her policies in accordance with the global developments so that global integration continues to be a positive sum game for all the countries. Global economic integration is technology induced and policy-managed. While the economic integration of India with the global economy will continue to take place, a successful integration, with due regard to the interests of a vast majority particularly, the poor would be possible only through sound public policies - evolved and redesigned from time to time. The BRIC report reflects considerable confidence in the future of the Indian economy, though it is necessary to see the fine print to realize that while India would be a super power in 2050, "if development proceeds successfully", the per capita income would still not be at a high end. What is important to recognize is that the report leans on the demographic strength that India derives from its huge workforce. In order to harness the demographic advantages, the quality of labour force, (in terms of relevant skills which need to be sustained, reoriented and upgraded in a globally competitive era) and the physical health of the workforce become crucial. Education and health, therefore, provide the link between supply and demand for labour through increases in productivity.

2.4.3 An appraisal of the public policies in India :

RBI's Governor Y V Reddy in his speech emphasized on the priorities for public policy to ensure successful economic integration of India with global economy.

He mentioned in his speech that practical policies in the external sector, particularly in the management of capital account and exchange rate, contributed to growth, provided resilience to shocks and an overall stability. Thus, India must continue with pragmatic, cautious and, gradual approach in this regard, subject to improvements in fiscal arena and the progress in strengthening the domestic financial sector.

Second, the management of financial sector has been oriented towards gradual rebalancing between efficiency and stability and the changing shares of public and private ownership. Enhanced competition among diverse players, including from branches of foreign banks, has been encouraged. Considerable improvements have taken place in prudential governance as also in moving away from administrative measures to market-orientation. Hence, it will be advisable to follow the same path in the coming years.

Third, on the fiscal front, he expressed concern about the high ratio of public-debt to GDP, but the structure of public-debt displays characteristics that make India less vulnerable than other countries with similar debt magnitudes. Therefore, there is advantage in continuing the progress in public debt management keeping structural aspects in view. An effective and qualitative fiscal adjustment would enhance the scope for a more successful integration with the global economy.

Fourth, significant liberalisation of external trade has taken place smoothly, which has imparted competitive efficiency to the domestic sector almost upto the global best standards in many of the sectors. There has also been demand for credit and creation of employment due to this. However, there exist several trade restrictions within India even as there has been progress in liberalizing external trade. Eliminating trade restrictions can have adverse impact on vulnerable sections, but a straight forward subsidy to the poor might well serve as solution. There is another well recognized distortion, vestiges of which still continue, in the form of reservation for small scale industries. With liberalisation of external trade, it is anomalous to persist with such distortions, even if on a reduced scale. Thus, there is still an unfinished agenda on trade reforms especially in regard to domestic trade and a policy commitment to remove such distortions in a defined short time frame would be ideal.

Fifth, it is interesting to note that the two sectors where India is globally most competitive, namely, software and pharmaceuticals, are not power intensive and do not require bulky transportation. The competitiveness of the manufacturing industry is admittedly a function of the availability of reliable power supply at reasonable cost. The budget of 2004-05 has rightly emphasized the importance

of power, airports and seaports (apart from tourism, which has significant employment potential) but there is need for implementation at a pace significantly faster than we have ever witnessed in any sector so far.

Sixth, there is universal recognition of the need to improve both productivity and output in the agriculture and related activities to meet the objectives of growth and employment. Yet, despite the best of efforts and excellent results achieved in that direction, there will have to be a massive shift of the workforce from agriculture to non-agricultural avocations. The quality of urban infrastructure even in the metropolitan cities is not conducive to globally competitive economic activity. The inevitable large scale redeployment of the migrating workforce would, therefore, need institutional arrangements, be they in public or private sector, for skill-imparting and skill up gradation.

Seventh, improvements in institutional infrastructure in matters relating to administrative, judicial and other systems of governance are admittedly important.

Eighth, the quantity and quality of water, education and health care infrastructure are far from adequate, and are not even at the minimum level consistent with a modern society. These fall under the ambit of delivery of public services and the Prime Minister has already accorded a high priority to this issue. Any tangible reform in this area would require action on several fronts, i.e., legislative executive and judicial and at several levels, Centre, State and local. Ninth, there are regional inequalities in growth. One should hope that the demonstration effect of a few high-performing States will spur the other States, in the medium term, to compete for better governance and economic performance.

Finally, enhanced investment activity, particularly in the infrastructure area, would necessitate higher domestic savings, especially in the public sector coupled with efficient financial intermediation. In addition, foreign savings need to be attracted and absorbed with a strong preference to Foreign Direct Investment in all sectors though in some sectors like banking, a calibrated approach may be warranted. At the same time, our enterprises should be enabled to attain a strong global presence in all sectors.

Now let us do another simple exercise :

SELF ASSESSMENT QUESTION III

State whether the following statement are true or false:

(i) External sector policies designed to progressively close the Indian economy formed an integral part of the strategy for structural reforms.

(ii) It is essential for India to carefully monitor the developments in both real and financial sectors

(iii) There is universal recognition of the need to improve both productivity and output in the agriculture and related activities to meet the objectives of growth and employment.

Check your answer with the one provided at the end of the unit.

2.5 Let Us Sum Up

Here instead of summing the unit by me, I would like you to sum up the entire unit within 150 words. You can use the available space provided below to write the same.

2.6 Annexure

Annexure I :

India's Position in terms of :

Per Capita Income/GDP (upto 31st March 2006)

- India :USD 520
- USA :USD 50,000

Annexure II :

Where India Will Be:

(BRIC Report: Goldman Sachs)

[Global Economic paper No.99]

Year Roughly where :

2010 UKRAINE is today

2015 PARAGUAY is today

2020 IRAN is today

2025 DOMINICAN REPUBLIC is today

2030 LATVIA is today

2035 HUNGARY is today

2040 SOUTH KOREA is today

2045 GREECE is today

2050 ITALY is today

Annexure III :

Human Development Category:

(2002)

Place	Life Expectancy in Yrs.)	A.L.R. (Percent)	G.D.P. (PPP)	USD Edu.Index	HD Index (2002)
USA	78.9	0.99	35,750	0.97	0.939
UK	78.1	0.99	26,150	0.99	0.936
RP.Korea	75.4	0.979	16,950	0.97	0.888
Japan	81.5	0.99	26,940	0.94	0.936
India	63.7	0.613	2,670	0.59	0.595
B'desh	61.1	0.411	1,700	0.45	0.509

2.7 Key Words

- ***Economic Indicators :*** The indicators which has an impact on the economic activities.

2.8 Probable Answers :

SELF ASSESSMENT QUESTION I : (i) False (ii) false
(iii) true (iv) false (v) true (vi) True

SELF ASSESSMENT QUESTION II: (i) False (ii) true
(iii) false (iv) true (v) true

SELF ASSESSMENT QUESTIONIII: (i) False (ii) true
(iii) true

2.9 Reflective Questions :

- What do you mean by economic indicators? List some of the economic indicators affecting India.
- Discuss the role of MNC's in India with some practical examples.
- Critically evaluate the progressive features of Indian Economy. Do you think that the progress is adequate? Justify.
- Argue on the development strategies adopted by India with suitable justification.

2.10 Suggested Readings for Unit 2 :

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.) (chapter 1 & 3)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004) (chapter 1 to 6)

BLOCK - 2 : GOVERNMENT CONTROLS AND MNCS

INTRODUCTION

In the last block you have learned about the basic concepts of Business environment and as I believe, you are all set to venture deep into the subject. This block has been divided into two units so as to enable you to grasp the elementary idea of various control measures adopted by India to check on the price, inflation etc. and also the conceptual idea of industrial policies in India. These units aim at the students to understand in details about:

- The concept of Control which includes
- Need, types, aims of control
- Limitations of control
- Significance of Industrial policies adopted by India.

Unit 1 will focus on the industrial policies in details and also the various controlling measures and Unit 2 will enable you to know about Monopoly and Restrictive Trade Practices (MRTP) Act and also the activities of Multi National Companies (MNCs). In sum this block will equip you with the broad understanding of issues dimensions, systems comprising Industrial policies in India along with various controls like price controls and also the legal environment under which one has to operate their businesses including MNCs.

While going through these units you are suppose to answer the Self Assessment Questions provided within each of the units to assess yourself about your understanding of the subject matter. In order to update yourself, it is always better if you read business magazines, news paper etc. regularly and also visit websites.

UNIT 1 : CONTROLS AND INDUSTRIAL POLICIES

Structure :

1.0 Objective
1.1 Introduction
1.2 Controls under Planning
1.3 Price Controls
1.4 Industrial Policy
1.5 Let Us Sum Up

1.0 Objective :

After going through this unit you will be able to:

- Define Control & Industrial Policy
- Discuss the various components of Control
- Analyze the significance of Industrial policy.

1.1 Introduction :

You must by now understand that several economic activities have an impact on the business environment. Control mechanism is one of such devise to control the activities of business houses. At the same time a clear cut policy of industries lead to a growth in the economy. This unit will focus on the control mechanism and also the significance of industrial policies of India.

1.2 Controls under Planning :

The price system can be used as a steering mechanism to secure the desired allocation of consumption and production, and thereby the interpersonal and inter-sectoral distribution of income. Hence, it is essential to have a price policy that is comprehensive enough to help achieve the various socio-economic aims. Today, the price polices of various nations aim, in general, at avoiding wide

fluctuations in the price behaviour, mobilization and optimum utilization of resources by bringing about their rational allocation, providing price incentives for increasing production and redistribution of income in favour of the poor. The nature of price policy a nation should adopt, however, depends on the nature of the economy, objectives of development, the institutional framework, trade and commercial patterns and the overall market behaviour.

When the First Five- Year Plan of India was formulated, the planners did not appear to have bothered much about the prices. As the First Plan experienced comparative price stability, the issue of prices was not a major concern while formulating the Second Plan also. But, during the Second Plan period, prices exhibited a disturbing trend and this became a matter of major concern. Hence, a separate chapter on price policy was incorporated, for the first time, in the Third Plan document.

The chapter on Price Policy for the Third Plan mainly dealt with the scope and limitations of the price policy and the constituents of the price policy. It stated that the price policy in a developing economy should concentrate on two main objectives:[a]it must ensure that the movements of relative prices accorded with priorities and targets that had been set in the plan; and [b] it must prevent any considerable rise in prices of essential goods that entered into the consumption of low income groups.

Fiscal and monetary discipline was conceived as the major constituent of price policy. It pointed out that fiscal policy must be directed to mopping up the excess purchasing power which tended to push up demands above the level of available supplies. The quantum of taxation must, in other words, be adequate to keep down consumption to the limits provided for in the plan. The requirements of public sector investment programme must be met by the transfer of real resources from the public rather than by creation of fresh purchasing power. In other words, fiscal policy in all its aspects must aim at restraining consumption and mobilizing saving more effectively.

It was stressed that monetary policy should go hand in hand with fiscal policy. Just as the latter should avoid the creation of excess purchasing power through government operations, the former should regulate the pace of credit creation through banks.

The policy also recognized the scope and limitations of the commercial policy in imparting stability to the economy.

While stressing that without adequate fiscal and monetary discipline, other regulatory measures would not have the desired effect, the policy recognized that fiscal and monetary policies by themselves might also not suffice to secure the right relationship between various prices or to prevent undue hardship to low and fixed income groups. "It may be necessary, then to have physical allocation and direct controls in certain sectors. It will be agreed, for instance, that so long as steel is scarce, it should be distributed between competing uses on the basis of agreed priorities. It may, of course, be essential to raise the price of any commodity that is scarce; but it may not be desirable from an overall point of view to get the highest bidder to get the bulk of the available supplies, leaving the rest to their own devices. If, similarly, there is a shortage of an essential drug, control of prices and distribution at a fair price to genuine users would be the appropriate course of action to adopt. The same reasoning applies to essentials of life like food or cloth. The prices of what may be called basic essentials must be held reasonably stable; in regard to commodities that are less essential, or may be classed as comforts or luxuries, a rise in prices may have to be tolerated. In the case of comfort and luxuries, in fact, an important factor in policy is the need to raise more resources; arise in their prices does not affect the common man. The techniques of price regulation may vary from commodity to commodity; in some cases, an increase in production may be the only way to secure a reasonable level of prices. In other cases, buffer stocks, reorganization of distribution arrangements and some direct controls may be inescapable."

Thus, the Price Policy recognized the importance of fiscal and monetary policies, commercial policy, physical controls, enhancement of supply, etc., in achieving its objectives.

Successive plans have emphasized the need for achieving price stability and distributive justice. However, the basis objectives and approach enunciated in the Price Policy formulated in the Third Plan have been continued in the successive plans without any remarkable change. More and more measures have been taken by the government to realize the objectives.

Now, Let us do a simple exercise

SELF ASSESSMENT QUESTION I

State whether the following are true or false:

(1) The price system can not be used as a steering mechanism

(2) The price polices of various nations aim, in general, at avoiding wide fluctuations in the price behaviour, mobilization and optimum utilization of resources by bringing about their rational allocation.

(3) Fiscal and monetary discipline was conceived as the major constituent of product policy.

(4) Successive plans have emphasized the need for achieving price stability and distributive justice.

Check your answer with the one provided at the end of the unit.

1.3 Price controls

A number of measures have been taken to control the prices. These measures include both indirect and direct controls.

- ***Indirect controls***

Indirect controls are exercised mainly through the monetary policy, fiscal policy and commercial policy.

The term monetary policy refers to the policy of the Central Bank of the country of the cost and availability of credit. The rationale of using the monetary policy to control prices is that there is a very strong direct relationship between money supply and prices. Ceteris paribus, an increase in money supply results in an increase in prices and vice versa. Hence, the price rise is sought to be arrested by monetary contraction and a fall in prices is dealt with by monetary expansion.

The Reserve Bank of India [RBI] has been employing the Bank [Discount] Rate Policy, open market operations variable reserve ratio requirement- and various methods of selective [Qualitative] credit control.

A policy that should go hand in hand with the monetary policy to make it effective is the fiscal policy. The fiscal policy refers to the policy of the government in respect of public revenue and public

expenditure. A fiscal policy can influence the price level by increasing or reducing the purchasing power of the public. Further, it can affect prices by imposing or removing or varying taxes on commodities or services, and by subsidies. Taxes, like excise duties and sales-tax, have a profound impact on the prices of commodities.

Commercial policy has also been used to a certain extent to stabilize the domestic economy. Prices can be kept under control by increasing the supply by importing goods which are in short supply. This has been done for such commodities as edible oils. Further, the government bans the export of certain items the supply position of which is not comfortable within the economy.

To prevent an unwarranted fall in the prices, the government may sometimes resort to the deliberate export of certain items.

There are other measures, too, such as buffer stock operations which can help avoid wide fluctuations in prices.

● ***Direct controls***

The Central and State Governments in India have armed themselves with a number of Acts to exercise direct control over the functioning of the economy. Laws like the Industries [Development and Regulation] Act, the Essential Commodities Act, the MRTP Act, the Companies Act, the Imports and Exports [Control] Act, etc., empower the Central Government to control production, supply, distribution and price in a large number of cases.

With the emergence of new problems and the aggravation of existing problems, the government has been arming itself, justified or not, with more and more powers of control. Today, the production, supply, distribution, and price of a number for commodities are subject to government control.

● ***Administered Prices***

Administered price, a term coined by Lord Keynes, refers to the price which is set consciously by a single decision-making body-like a monopoly firm, a cartel, or a government agency-rather than being determined by the free play of market forces.

When the market forces of supply and demand are free to interact, the price of a commodity rises when the demand for it increases relative to the supply, and the price falls when the demand declines. But under the administered price system, as the price is fixed at an artificial level, fluctuations in demand and supply do not cause any price fluctuation. In other words, the administered price is not an equilibrium price. Not only that, the administered price may not reflect the demand and supply conditions; sometimes it may not even absorb the full cost of production.

In India, the price of a number of key commodities are administered by the government. Some key commodities and services such as steel, coal, fertilizers, aluminium and electricity, whose prices are administered, account for about one-fifth of the total weight in the wholesale price index. Thus, the administered price has become an important factor affecting the general price level in India. Over 70 percent of the goods and services sold by the public sector enterprises are subject to administered prices. These are indicative of the importance of the administered price in the Indian economy.

Administered prices are generally fixed on the recommendations of an expert body like the Bureau of industrial costs and prices [BICP] or, in the case of certain public enterprises, on those of specially constituted Inter Ministerial Committees or groups. While recommending prices, the BICP normally goes by the guidelines for price fixation prescribed by the government and, inter alia, takes into account the cost of most efficient firms which account for a large percentage of the total output [to ensure a certain level of efficiency in production], the optimal noms of consumption of raw materials and energy as well as capacity utilization, and provides a fair rate of return which has generally ranged between 10 and 14 percent on net worth, depending on the differences with respect to factors such as risk, priority, growth prospects, etc. In order to reconcile the interests of consumers as well as producers, a system of retention prices for different producers on the basis of cost of production on the one hand and uniform sale prices for consumers on the other has been recommended, and was in operation in several cases such as steel, fertilizers, cement, etc. Price adjustments are

allowed for changes in major cost components from time to time, and a review in depth is undertaken after suitable intervals.

1.4 Industrial Policy :

The Industrial Policy Resolution of 1956 and the Statement on Industrial Policy of 1991 provide the basic framework for the overall industrial policy of the Government in regard to the manufacturing industries. In the initial stages of the country's development, growth of industry was regulated through the granting of industrial licences and other industrial approvals. The Industries (Development and Regulation) Act, 1951 was the principal legislation providing the legal basis for industrial licencing. The industrial policy announced on 24th July, 1991 substantially dispensed with industrial licensing, announced measures facilitating foreign investment and technology transfers, and threw open the areas hitherto reserved for the public sector.

● *Industries Reserved for the Public Sector*

The private sector can now operate in all areas except those of strategic concern such as defence, railway transport and atomic energy. The list of industries reserved for the public sector now stands reduced to 6. Private participation is permitted in some specific areas in this list as well, such as mining; oil exploration, refining and marketing; and parts of the railway transport sectors.

● *Industries Where an Industrial License is Required*

The requirement of obtaining an industrial license for manufacturing activity is limited to:

- ❑ Industries reserved for the pubic sector.
- ❑ 16 industries of strategic, social or environmental concern.
- ❑ Industries reserved for the small scale sector.

All other industries are exempt from licensing, and only subject to the locational restrictions of metropolitan areas.

Now, Let us do another simple exercise

SELF ASSESSMENT QUESTION II

State whether the following are true or false:

(1) Indirect controls are exercised mainly through the monetary policy, fiscal policy and business policy.

(2) The Reserve Bank of India [RBI] has been employing the Bank [Discount] Rate Policy.

(3) To prevent an unwarranted fall in the prices, the government may sometimes resort to the deliberate export of certain items.

(4) When the market forces of supply and demand are free to interact, the price of a commodity decreases.

(5) The Industrial Policy Resolution of 1956 and the Statement on Industrial Policy of 1991 provide the basic framework for the overall industrial policy of the Government in regard to the manufacturing industries.

Check your answer with the one provided at the end of the unit.

1.5 Let Us Sum Up

Several economic activities have an impact on the business environment. Control mechanism is one of such devise to control the activities of business houses. During the five year plan period, when the First Five- Year Plan of India was formulated, the planners did not appear to have bothered much about the prices. As the First Plan experienced comparative price stability, the issue of prices was not a major concern while formulating the Second Plan also. But, during the Second Plan period, prices exhibited a disturbing trend and this became a matter of major concern. Hence, a separate chapter on price policy was incorporated, for the first time, in the Third Plan document.

The Industrial Policy Resolution of 1956 and the Statement on Industrial Policy of 1991 provide the basic framework for the overall industrial policy of the Government in regard to the manufacturing

industries. In the initial stages of the country's development, growth of industry was regulated through the granting of industrial licences and other industrial approvals. The Industries (Development and Regulation) Act, 1951 was the principal legislation providing the legal basis for industrial licencing. The industrial policy announced on 24th July, 1991 substantially dispensed with industrial licensing, announced measures facilitating foreign investment and technology transfers, and threw open the areas hitherto reserved for the public sector.

1.6 Key Words

Price Control means control of price hikes in case of essential commodities and other services where the interest of the common men is associated with.

Industrial Policy means a system through which the government determines the industrial course of action in a country having an objective of industrial growth.

1.7 Probable Answers:

SAQI : (i) False (ii) True (iii) False (iv) True

SAQII: (i)False (ii)True (iii) True (iv) False (v) True

1.8 Reflective Questions:

- Explain the meaning of Control and what are the types and limitations of Control?
- Discuss the various components of Control
- Define Industrial policy. Analyze the significance of Industrial policy.
- Critically argue the importance of Administrative pricing in a country like India.
- Develop a paper on control under the planning period of India.

1.9 Suggested Readings for Unit 1:

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.) (chapter 2 & 3)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004) (chapter 3 & 6)
- Dewett K.K., Verma J.D. & Sharma M.L., Indian Economics, S.Chand & Company Ltd., New Delhi (Chapter 31)

UNIT 2 : MNCS AND MRTP ACT

Structure

2.0 Objectives
2.1 Introduction
2.2 Scenario of MNC's in India
2.3 MRTP Act
  2.3.1 Restrictive Trade Practices
  2.3.2 Unfair Trade Practices
  2.3.3 Powers of the Commission
  2.3.4 Remedies under the Act

2.0 Objectives :

After going through this unit you will be able to

- Define MRTP
- List the important provision of MRTP
- Discuss the role of MNC's in India
- Critically evaluate the restrictive and unfair trade practices under the Act.
- Argue on the powers given to the commission by the Act.

2.1 Introduction :

In the last unit you have learned about control mechanism and industrial policies in Indian economy. However, the study would remain incomplete if one is unaware of the MRTP act and also the present scenario of MNC's in India. This unit mainly highlights the progressive features of MRTP act and its various provisions along with the MNC scenario in India.

2.2 Scenario of Multinational Corporations in India

MNC's have a strong hold over the Indian economy. The Industrial licensing policy Inquiry Committee stated that there were 112 companies in India in 1966 with assets worth Rs.10 Cr. or more.

Of these, 48 companies were either branches of foreign companies or Indian subsidiaries of foreign companies. In addition, there were 14 Indian companies virtually controlled by foreign entities. These 62 companies had Rs.1, 370 crore worth of assets. In March 1977, there were 482 branches of MNC's operating in India. Of these 319 were branches of UK based companies. Next to UK; USA based companies had 88 branches in India.

It can be observed that the MNCs operating in India have raised the major portion of their financial resources from within the Indian economy. This fact goes against the argument that the MNCs bring in large amounts of foreign capital with them. The real position is that the MNCs raise most of their capital requirements within the country itself. The MNCs are operating mainly in the field of agriculture and allied activities, commerce, trade and finance, processing and manufacture, etc.

A common form of MNC participation in Indian Industry is through collaboration agreements. Between 1948 till 1988, 12,760 foreign collaboration agreements were approved in India. Of these, 6,165 were approved during the period between 1981 and 1988. As a result of liberalisation measures announced in the 1991 Industrial policy, there was a spurt in the number of foreign collaboration agreements. The Government had approved 8,137 foreign collaboration proposals during the period 2001-2005.

In India, the MNCs are controlled by the Government agencies such as the Ministry of Company affairs, the RBI, the Ministry of Industrial Development and the Ministry of Finance. Since there are number of agencies, there are no objective criteria for approving proposals.

2.3 MRTP Act :

The Monopolistic and Restrictive Trade Practices Act, 1969, was enacted

- To ensure that the operation of the economic system does not result in the concentration of economic power in hands of few,
- To provide for the control of monopolies, and
- To prohibit monopolistic and restrictive trade practices. The MRTP Act extends to the whole of India except Jammu and Kashmir.

Unless the Central Government otherwise directs, this act shall not apply to:

(a) Any undertaking owned or controlled by the Government Company,

(b) Any undertaking owned or controlled by the Government,

(c) Any undertaking owned or controlled by a corporation (not being a company established by or under any Central, Provincial or State Act,

(d) Any trade union or other association of workmen or employees formed for their own reasonable protection as such workmen or employees,

(e) Any undertaking engaged in an industry, the management of which has been taken over by any person or body of persons under powers by the Central Government,

(f) Any undertaking owned by a co-operative society formed and registered under any Central, Provincial or state Act,

(g) Any financial institution.

2.3.1 Restrictive Trade Practice :

A restrictive trade practice is a trade practice, which

- Prevents, distorts or restricts competition in any manner; or
- Obstructs the flow of capital or resources into the stream of production; or
- Which tends to bring about manipulation of prices or conditions of delivery or effected the flow of supplies in the market of any goods or services, imposing on the consumers unjustified cost or restrictions.
- Inquiry into restrictive practices

The Commission may inquire into any restrictive trade practice

- Upon receiving a complaint from any trade association, consumer or a registered consumer association, or
- Upon a reference made to it by the Central or State Government or
- Upon its own knowledge or information
- Relief available.

The commission shall if after making an inquiry it is of the opinion that the practice is prejudicial to the pubic interest, or to the interest of any consumer it may direct that -

- The practice shall be discontinued or shall not be repeated;
- The agreement relating thereto shall be void in respect of such restrictive trade practice or shall stand modified.
- The Commission may permit the party to any restrictive trade practice to take steps so that it is no longer prejudicial to the public interest.

However no order shall be made in respect of

(a) any agreement between buyers relating to goods which are bought by the buyers for consumption and not for ultimate resale;

(b) a trade practice which is expressly authorised by any law in force.

2.3.2 Unfair Trade Practice :

An unfair trade practice means a trade practice, which, for the purpose of promoting any sale, use or supply of any goods or services, adopts unfair method, or unfair or deceptive practice.

Unfair practices may be categorised as under:

False Representation

The practice of making any oral or written statement or representation which:

- Falsely suggests that the goods are of a particular standard quality, quantity, grade, composition, style or model;
- Falsely suggests that the services are of a particular standard, quantity or grade;
- Falsely suggests any re-built, second-hand renovated, reconditioned or old goods as new goods;
- Represents that the goods or services have sponsorship, approval, performance, characteristics, accessories, uses or benefits which they do not have;
- Represents that the seller or the supplier has a sponsorship or approval or affiliation which he does not have;

- Makes a false or misleading representation concerning the need for, or the usefulness of, any goods or services;
- Gives any warranty or guarantee of the performance, efficacy or length of life of the goods, that is not based on an adequate or proper test;
- Makes to the public a representation in the form that purports to be-

  (a) a warranty or guarantee of the goods or services,

  (b) a promise to replace, maintain or repair the goods until it has achieved a specified result, if such representation is materially misleading or there is no reasonable prospect that such warranty, guarantee or promise will be fulfilled
- Materially misleads about the prices at which such goods or services are available in the market; or
- Gives false or misleading facts disparaging the goods, services or trade of another person.

False Offer Of Bargain Price

Where an advertisement is published in a newspaper or otherwise, whereby goods or services are offered at a bargain price when in fact there is no intention that the same may be offered at that price, for a reasonable period or reasonable quantity, it shall amount to an unfair trade practice.

The 'bargain price', for this purpose means-

(a) the price stated in the advertisement in such manner as suggests that it is lesser than the ordinary price, or

(b) the price which any person coming across the advertisement would believe to be better than the price at which such goods are ordinarily sold.

Free Gifts Offer And Prize Schemes

The unfair trade practices under this category are:

- Offering any gifts, prizes or other items along with the goods when the real intention is different, or
- Creating impression that something is being offered free alongwith the goods, when in fact the price is wholly or partly covered by the price of the article sold, or

- Offering some prizes to the buyers by the conduct of any contest, lottery or game of chance or skill, with real intention to promote sales or business.

Non-Compliance Of Prescribed Standards

Any sale or supply of goods, for use by consumers, knowing or having reason to believe that the goods do not comply with the standards prescribed by some competent authority, in relation to their performance, composition, contents, design, construction, finishing or packing, as are necessary to prevent or reduce the risk of injury to the person using such goods, shall amount to an unfair trade practice.

Hoarding, Destruction, Etc.

Any practice that permits the hoarding or destruction of goods, or refusal to sell the goods or provide any services, with an intention to raise the cost of those or other similar goods or services, shall be an unfair trade practice.

Inquiry Into Unfair Trade Practices

The Commission may inquire into

Any unfair trade practice

- Upon receiving a complaint from any trade association, consumer or a registered consumer association, or
- Upon reference made to it by the Central Government or State Government
- Upon an application to it by the Director General or
- Upon its own knowledge or information.

Relief Available

After making an inquiry into the unfair trade practice if the Commission is of the opinion that the practice is prejudicial to the pubic interest, or to the interest of any consumer it may direct that -

- The practice shall be discontinued or shall not be repeated;
- The agreement relating thereto shall be void in respect of such unfair trade practice or shall stand modified.

- Any information, statement or advertisement relating to such unfair trade practice shall be disclosed, issued or published as may be specified
- The Commission may permit the party to carry on any trade practice to take steps to ensure that it is no longer prejudicial to the public interest or to the interest of the consumer.

However no order shall be made in respect a trade practice which is expressly authorised by any law in force.

The Commission is empowered to direct publication of corrective advertisement and disclosure of additional information while passing orders relating to unfair trade practices.

Now Let us do a simple exercise:

SELF ASSESSMENT QUESTION I

Fill up the blanks:

(1) This fact goes against the argument that the -------- bring in large amounts of foreign capital with them

(2) A common form of MNC participation in Indian Industry is through ------------- agreements

(3) MRTP ensure that the operation of the economic system does not result in the -----------of economic power in hands of few.

(4) Where an advertisement is published in a newspaper or otherwise, whereby goods or services are offered at a bargain price when in fact there is no intention that the same may be offered at that price, for a reasonable period or reasonable quantity, it shall amount to an unfair ------ practice.

Check your answer with the one provided at the end of the unit

2.3.3 Powers Of The Commission

The MRTP Commission has the following powers:

(1) Power of Civil Court under the Code of Civil Procedure, with respect to:

(a) Summoning and enforcing the attendance of any witness and examining him on oath;

(b) Discovery and production of any document or other material object producible as evidence;

(c) Reception of evidence on affidavits;

(d) Requisition of any public record from any court or office.

(e) Issuing any commission for examination of witness; and

(f) Appearance of parties and consequence of non-appearance.

(2) Proceedings before the commission are deemed as judicial proceedings with in the meaning of sections 193 and 228 of the Indian Penal Code.

(3) To require any person to produce before it and to examine and keep any books of accounts or other documents relating to the trade practice, in its custody.

(4) To require any person to furnish such information as respects the trade practice as may be required or such other information as may be in his possession in relation to the trade carried on by any other person.

(5) To authorise any of its officers to enter and search any undertaking or seize any books or papers, relating to an undertaking, in relation to which the inquiry is being made, if the commission suspects tat such books or papers are being or may be destroyed, mutilated, altered, falsified or secreted.

Preliminary Investigation

Before making an inquiry, the Commission may order the Director General to make a preliminary investigation into the complaint, so as to satisfy itself that the complaint is genuine and deserves to be inquired into.

2.3.3 Remedies Under The Act :

The remedies available under this act are -

Temporary Injunction

Where, during any inquiry, the commission is satisfied that any undertaking or any person is carrying on, or is about to carry on, any monopolistic, restrictive or unfair trade practice, which is a pre-

judicial to the public interest or the interest of any trader or class of traders generally, or of any consumer or class of consumers, or consumers generally, the commission may grant a temporary injunction restraining such undertaking or person form carrying on such practice until the conclusion of inquiry or until further orders.

Compensation

Where any monopolistic, restrictive or unfair trade practice has caused damage to any Government, or trader or consumer, an application may be made to the Commission asking for compensation, and the Commission may award appropriate compensation.

Where any such loss or damage is caused to a number of persons having the same interest, compensation can be claimed with the permission of the commission, by any of them on behalf of all of them.

2.4 Let Us Sum Up :

Once again, I would like you to sum up the entire unit within 150 words. You can use the available space provided below to write the same.

2.5 Key Words :

'Monopoly' means sole player (Seller) in the market.

'Unfair Trade Practice' is a practice which can not be treated as just and fair for a common man.

2.6 Probable Answers:

1. SAQI : (i) MNC (ii) collaborative (iii) concentration (iv) trade

2.7 Reflective Questions :

- Define MRTP. Why is it so important for a country like India?
- List the important provision of MRTP. Do you think these are adequate enough?
- Discuss the role of MNC's in India with some practical examples.
- Critically evaluate the restrictive and unfair trade practices under the MRTP act.
- Argue on the powers given to the commission by the MRTP act.

2.8 Suggested Readings for Unit 2:

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.) (Chapter 1,2 & 3)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004) (Chapter 1 & 6)
- Dewett K.K., Verma J.D. & Sharma M.L., Indian Economics, S.Chand & Company Ltd., New Delhi (Chapter 31)

BLOCK - 3
POLICIES AND MOBILIZATION OF RESOURCES

INTRODUCTION

In the last block (block 2) you have learned about various Government controls and also the various legal issues as well as the role of MNCs in Indian context. However, at this juncture you might be wondering about the various policies of the government that has been adopted to regulate the business environment. This block has been divided into two units so as to enable you to grasp the idea of monetary & pricing policy in developing economy and also the mobilization of resources through fiscal policy for economic progress. These units have been designed to enable the students to understand in details about:

- Monetary policy of India
- Price policy adopted by India
- Mobilization of resources through Fiscal policy.

In sum this block will equip you with the broad understanding of issues and dimensions of Monetary and Price policies in India along with mobilization of resources through Fiscal policies.

While going through these units you are suppose to answer the Self Assessment Questions provided within each of the units to assess yourself about your understanding of the subject matter. In order to update yourself, it is always better if you read business magazines, news paper etc. regularly and also visit websites.

UNIT 1
MONETARY & PRICE POLICY IN DEVELOPING ECONOMY

Structure

1.0 Objective
1.1 Introduction
1.2 Monetary Policy- meaning
1.3 Indian Monetary Policy
1.3.1 Features
1.3.2 Monetary Growth
1.3.3 Credit Policy
1.4 Price policy in developing economy
1.5 Let Us Sum Up

1.0 Objectives

After going through this unit you will be able to:

- Define Monetary policy
- Discuss the Indian Monetary policy
- Analyze the importance of pricing policy in developing economy
- Establish relationship between credit policy and monetary growth.
- Develop a paper on Indian Monetary policy - issues and prospects.

1.1 Introduction

The monetary and pricing policies have an important influence on the gross national product. This unit has been design to focus some issues in Indian monetary policy. The credit policy has an impact on the overall monetary policy and hence some of the issues have also been highlighted in this unit. The pricing policy requires prudent consideration as it plays a big role in the developing economy.

1.2 Monetary Policy-Meaning

Monetary Policy involves changes in the base rate of interest to influence the rate of growth of aggregate demand, the money supply and ultimately price inflation.

Monetarist economists believe that monetary policy is a more powerful weapon than fiscal policy in controlling inflation. Monetary policy also involves changes in the value of the exchange rate since fluctuations in the currency also impact on macroeconomic activity (incomes, output and prices)

Changes in short term interest rates affect the spending and savings behaviour of households and businesses over time and therefore feed through the circular flow of income and spending. The transmission mechanism of monetary policy works with variable time lags depending on the interest elasticity of demand for different goods and services - e.g. the demand for interest-sensitive consumer goods and services bought on credit or the demand for capital investment from private sector businesses. Because of the time lags involved in setting an appropriate level of short-term interest rates, the Bank of England sets nominal interest rates on the basis of hitting the inflation target over a two year forecasting horizon.

1.3 Indian Monetary Policy

The fundamental objective of monetary policy in a developing economy is the promotion of economic growth with economic stability. The monetary authority can promote economic growth by directing the flow of funds in the desirable channel of investment. The Indian first Five Year Plan underlies the role of monetary policy in economic development thus; "Central banking in planned economy can hardly be confined to the regulation of the overall supply of credit or to a somewhat negative regulation of the flow of bank credit. It would have to take a direct and active role, firstly in increasing or helping to create the machinery needed for financing development activities all over the country and, secondly, in ensuring that finance available flows in the direction intended.

1.3.1 Features

In mid 90s in India the thrust of monetary policy was to reduce the annual inflation rate and provide credit support for production.

Money supply (M3) was reduced considerably, mainly because of a slow growth in bank deposits and a decline in the growth of reserve money.

● ***Slow growth***

Another major factor in controlling this growth was the lower level of foreign exchange inflows. Slower monetary growth was accompanied by lower bank credit to the commercial sector. These trends were compounded by a decline in other sources of finance to industry, such as primary issues in the domestic stock market and GDR issues in Euro markets.

● ***Other reasons***

Funds raised from capital markets declined and the amount raised through Euro issue loans also fell down nearly 70 percent over the same period. Continued high levels of government borrowing associated with a large and over-budget fiscal deficit kept money markets tight throughout the period. This in turn put increasing pressure on interest rates.

1.3.2 Monetary Growth

Despite falling inflation, real rates faced by industry remained high, and the prime lending rate of most of the banks was 16.5 percent. Based on an inflation rate of 6 percent and projected GDP growth of 6.6 percent for 1996-97, monetary growth had been targeted at 15.5-16 percent for 1996-97.

● ***RBI measures***

The RBI reduced banks' cash reserve requirements by one percentage point, freed bank deposit interest rates of over one year term and shortened the minimum term for deposits from 46 days to 30 days. It also withdrew a refinancing facility for banks' investments in government securities. These steps were to add the equivalent of USD 1.2 billion to the banking sector. Short-term call money market rates of interest and forward premiums on the dollar have dropped sharply.

- ***Response***

While financial and industry sources have welcomed the liquidity-easing measures, they remain worried at the rigidity of high lending rates of interest and suspect that the Government will soon absorb this new bank liquidity by increasing Government borrowing from the market.

- ***Growth of M3***

Growth in broad money (M3) in 1997-98 registered an increase, higher than the RBI's growth target. The increase was due to a substantial expansion of domestic credit to the government and the business sector, and an increase in net foreign exchange assets. Bank credit to business increased, net RBI credit to the government increased and strong foreign exchange inflows during the first half of 1997-98 coupled with sluggish credit creation ensured that the money market was awash with liquidity. Banks investment in government securities increased by 17.7 percent in 1997-98, and non-food credit to business increased by 14.2 percent.

1.3.3 Credit policy

The credit policy for April-October 1998, aimed to accelerate industrial investment and output, keep inflation under control, continue financial sector reforms, reduce interest rates and improve credit availability to meet business requirements. Key reference rates were reduced by one percentage point each, sending a strong signal that commercial banks should lower interest rates for commercial borrowers. Banks responded by reducing prime lending rates to 13 percent. The Cash Reserve Ratio requirement was left unchanged at 10 percent.

Under the new credit policy, FIIs were allowed to invest up to 30 percent of their assets in treasury bills, and banks were given freedom to fix penalties on premature withdrawal of deposits. In January 1998, the rupee hit a low of Rs 40.45/ dollar, due in large part to concerns about the Asian currency crisis.

- ***RBI measures***

The RBI adopted a number of measures that stopped the rupee's slide and actually led to some appreciation. These measures included an increase in banks' cash reserve ratio and an increase in the RBI's bank rate. Once the rupee had stabilized, the RBI announced a two-phase rollback of the bank rate to 10 percent, and of the CRR to 10 percent. In both cases, the first phase was to be effective from late March and the second in early April. The interest rate on short-term domestic deposits was also deregulated and banks were allowed to set different prime lending rates.

The Monetary Policy of India for the year 2006-07 (as amnd. upto date) has been provided in the Annexure I.

Let us do a simple exercise:

SELF ASSESSMENT QUESTION I

State whether the following are true or false:

(i) Monetarist economists believe that fiscal policy is a more powerful weapon than monetary policy in controlling inflation.

(ii) The Indian first Five Year Plan underlies the role of monetary policy in economic development.

(iii) India often witness slower monetary growth which accompanied by lower bank credit to the commercial sector.

(iv) In 1998, short-term call money market rates of interest and forward premiums on the dollar have dropped sharply.

(v) Once the rupee had stabilized, the RBI announced a two-phase rollback of the bank rate to 10 percent, and of the CRR to 20 percent.

Check your answer with the one provided at the end of the unit.

1.4 Price Policy in a Developing Economy

It is generally recognized that price movements have vital influence on the pace of economic growth and on inter-sectoral relations in a developing economy. The fundamental objective of

the price policy for a developing economy is to accelerate economic growth and at the same time to maintain stability of the economy. With the above objective in view, the price policy should aim at :

- Checking violent price movements to ensure reasonably stable price level.
- Mobilizing resources for economic growth.
- Optimum utilization of resources by bringing about their rational allocation.
- Rapid economic growth by providing incentives for increasing production.
- Giving relief to the poorer sections.

A careful watch on the price changes means appropriate action to be taken to curve the hike/fall in price rise so that the economic imbalances may not occur. Even when the production potential of the country has been strengthened considerably, both in agricultural and in industry, and deficit financing has been strictly limited in the scheme of mobilising the financial resources, the possibilities of a significant and even disturbing price raise can not been entirely ruled out.

The main reasons for disturbing price changes are:

- The usual uncertainty in regards to monsoons
- The various restraints on consumption implicit in the plans may not operate to the full extent; and
- While the plan envisage a certain balance between the rates of growth in various sectors, some imbalances is almost certain to appear from time to time.

The major constituents of the price policy are:

- Integrated price wage and Income policy which always spokes about an integrated linkage to stable the economy as a whole.
- Policy to restrain price raise which often focus on appropriate fiscal policy, Suitable income policy and suitable monetary policy.

The essence of the price policy for a developing economy is to promote economic growth and make room for ascertain measures of equality, thereby preventing social stresses and conflicts. In short, the price policy should be geared to economic growth, equality and social justice. It should provide with adequate incentives to production and investment. It must either stabilize prices at levels fair to all sections of the community or secure to them full compensation for the erosion of their purchasing power through soaring prices. Hence the policy must take into account the effect of rising prices on the country's wage system, it exports and other aspects of the economy.

In the light of the above the price policy should consist of two parts: one relating to the prices in the agricultural sector and the other to prices, profits and other non-wage incomes in the industrial sector. The price policy for agricultural commodities should be in accord with the needs of a rapid growth of productivity in the agricultural sector. Agricultural prices should be remunerative to the growers, but not too high for the consumers.

As regards the price policy for the non agricultural sector, it must take into account the impact of changes in prices of raw materials, capital goods and intermediate products. The prices must be such that it ensures a reasonable return on the investment and a renewed flow of fresh savings into industry.

Let us do another simple exercise:

SAQ II

Fill up the blanks:

(i) Price policy aims at checking -------- price movements to ensure reasonably stable price level.

(ii) Price changes in India mainly due to the usual uncertainty in regards to -----------.

(iii) Integrated price wage and Income policy which always spokes about an ----------- linkage to stable the economy as a whole.

(iv) Policy to ----------- price raise which often focus on appropriate fiscal policy, Suitable income policy and suitable monetary policy.

Check your answer with the one provided at the end of the unit.

1.5 Let Us Sum Up

The monetary and pricing policies have an important influence on the gross national product. Monetary Policy involves changes in the base rate of interest to influence the rate of growth of aggregate demand, the money supply and ultimately price inflation. The fundamental objective of monetary policy in a developing economy like India is the promotion of economic growth with economic stability. The monetary authority can promote economic growth by directing the flow of funds in the desirable channel of investment. The credit policy for April-October 1998, aimed to accelerate industrial investment and output, keep inflation under control, continue financial sector reforms, reduce interest rates and improve credit availability to meet business requirements.

A careful watch on the price changes means appropriate action to be taken to curve the hike/fall in price rise so that the economic imbalances may not occur. Even when the production potential of the country has been strengthened considerably, both in agricultural and in industry, and deficit financing has been strictly limited in the scheme of mobilising the financial resources, the possibilities of a significant and even disturbing price raise can not been entirely ruled out. That is why the government of India focuses on the Pricing pattern and adopts clear cut policies regarding this.

1.6 Annexure

Annexure I

The Monetary Policy of India 2006-07

Amidst much hype (as usual), the Annual Monetary Policy 2006-07 was announced on April 18,2006. While interest rates and cash reserve ratio (CRR) were maintained at the same level, the Reserve Bank of India (RBI) has advised caution on some aspects like commodity prices and credit quality. Here is our view on the Annual Policy.

Current Annual Monetary Policy stance - April 2006

- To ensure a monetary and interest rate environment that enables continuation of the growth momentum consistent

with price stability while being in readiness to act in a timely and prompt manner on any signs of evolving circumstances impinging on inflation expectations.

- To focus on credit quality and financial market conditions to support export and investment demand in the economy for maintaining macroeconomic, in particular, financial stability.
- To respond swiftly to evolving global developments. Stance in the Third-quarter review of the Annual Monetary Policy - January 2006
- To maintain the emphasis on price stability with a view to anchoring inflationary expectations.
- To continue to support export and investment demand in the economy for maintaining the growth momentum by ensuring a conducive interest rate environment for macroeconomic, price and financial stability.
- To provide appropriate liquidity to meet genuine credit needs of the economy with due emphasis on quality.
- To consider responses as appropriate to evolving circumstances.

What is different?

- To focus on credit quality and financial market conditions to support export and investment demand in the economy for maintaining macroeconomic, in particular, financial stability.
- To respond swiftly to evolving global developments.

Unlike January 2006, there is a greater emphasis on the need to focus on credit quality in general for the banking sector in the recent Annual Monetary Policy statement.

Some of the measures like the hike in general provisioning requirement on personal loans, loans and advances qualifying as capital market exposures and residential housing loans beyond Rs 2 m are aimed at slowing credit disbursals. The provisioning requirement as far as commercial real estate loans from the present level of 0.4% to 1.0% signals the fact that the RBI is worried about

the increase in real estate prices in India (risk weight on exposures to commercial real estate raised from 125% to 150%). Higher provisioning impacts banks and consumers alike. For instance, banks have to set aside Rs 150 as provision for every Rs 100 advanced towards commercial real estate developers. Either the bank absorbs the same in its books or adjusts the lending rate to reflect this higher provisioning requirement. If the bank absorbs the same, the return on equity will be affected.

Another interesting aspect, which we subscribe to whole-heartedly, is the emphasis on global developments. Globally, interest rates have been on the rise in the since the last two years. Commodity prices (including crude oil) are governed by global demand and supply. Indian corporate sector is also expanding rapidly in the global markets (both organically and through acquisitions). Given this, it is riskier to assume that India is 'insulated' by global factors. In the analyst meet of UTI Bank yesterday, Mr. P. J. Nayak emphasized the need for caution as far as global expansion by Indian corporates is concerned. He also highlighted the fact that in the case of any adverse movement in exchange rate, the impact on Indian companies will be immediate (at the consolidated level).

Observation

In short, the Annual Monetary Policy is on expected lines i.e. without any interest rate hikes. The GDP growth prospects of 7.5% to 8% in FY07 with inflation at 5% to 5.5% are positives for the economy as a whole. But for some caution on the quality of credit disbursals, investors have nothing significant to worry about at the macro level.

1.7 Key words

Monetary Policy -the RBI adopted a credit squeeze policy with a view to contain the excessive credit creation and the storm of money supply at large.

Growth of M3- Growth in broad money

Credit Policy- RBI regulated to restrain bank credit

1.8 Probable Answers:

SAQI :	(i) False	(ii) True	(iii) true
	(iv) true	(v) false	
SAQII:	(i) violent	(ii) monsoon	(iii) integrated
	(iv) restrain		

1.9 Reflective Questions:

- Define monetary policy. Discuss in details the Indian Monetary policy
- Analyze the importance of pricing policy in developing economy. Do you think that the Indian pricing policy has been successful after the independence?
- Establish relationship between credit policy and monetary growth. How you would like to differentiae the two in terms of practical applications.
- Write a note on Indian Monetary policy - issues and prospects.
- Develop a paper on the Indian monetary policy based on its changing scenario.

Suggested Readings for Unit 1:

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.) (Chapter 5&6)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004) (Chapter 1 to 6)
- Dewett K.K., Verma J.D. & Sharma M.L., Indian Economics, S.Chand & Company Ltd., New Delhi (Chapter 30 to 35)

UNIT 2
MOBILIZATION OF RESOURCES

Structure

2.0 Objective
2.1 Introduction
2.2 Mobilization of Resources through Fiscal Policy
2.2.1 Fiscal policy -meaning
2.2.2 Types of fiscal policy
2.2.3 Expenditure and Taxation
2.2.4 Borrowing
2.2.5 Economic & monetary effects
2.3 Indian Scenario
2.3.1 Mobilization of resources through taxation
2.3.2 Containment of current expenditure
2.3.3 Consequences of public borrowing
2.4 Public Enterprise savings
2.4.1 Central Government Public Enterprise
2.4.2 State Government Public Enterprises.
2.5 Household saving behaviours
2.5.1 Changing Structure of Private Savings
2.5.2 Policy incentives for private savings
2.6 Let Us Sum Up

2.0 Objectives

After going through the unit you will be able to:

- Define Fiscal Policy
- List different types of fiscal policy
- Discuss the mobilization of resources through taxation
- Analyze the consequences of public borrowings
- Focus on public enterprise savings.
- Critically evaluate the household saving behaviours of Indian people.

2.1 Introduction

In the last unit you have learned about the Monetary and Price policy in developing economy with special reference to India. However one must not forget that the successes of these policies are mainly lies on the mobilization of its resources to the maximum optimum level. While analyzing the utilization of resources, perhaps one has to give due importance to Savings and Expenditure pattern. This unit will focus on these issues in details.

2.2 Mobilization of Resources through Fiscal Policy

In the earlier part, monetary policy was identified as one of the tools that a national government uses to influence its domestic economy. The second tool available to government (and one that is used by all levels of government) is fiscal policy. The term fiscal policy refers to the expenditure a government undertakes to provide goods and services and to the way in which the government finances these expenditures.

There are two methods of financing: taxation and borrowing. Taxation takes many forms in the developed countries including taxation of personal and corporate income, value added taxation and the collection of royalties or taxes on specific sets of goods. The debt burden assumed by the government is itself an important policy variable and one that has implications for the conduct of monetary policy. Governments in democratic societies act on many different, occasionally conflicting objectives. They may want to smooth out the nation's income in order to minimize the pejorative effects of the business cycle or they may want to take steps designed to increase the national income. They may also want to take steps intended to achieve specific social objectives deemed to be appropriate by the political or legal process.

2.2.1 Fiscal policy : Meaning

'Fiscal policy' is the economic term which describes the actions of a government in setting the level of public expenditure and how that expenditure is funded.

It contrasts with monetary policy, which describes the policies about the supply of money to the economy.

- ***Objectives***

The principal objectives of fiscal policy in a developing economy are:

- To mobilize resources for financing the development programmes in the public sector;
- To promote development in the private sector;
- To bring an optimum utilization of resources;
- To restrain inflationary pressures in the economy with a view to ensuring economic stability; and
- To improve the distribution of income and wealth in the community by lessening economic inequalities.

2.2.2 Types of Fiscal Policy

Expansionary fiscal policy - an increase in government purchases of goods and services, a decrease in net taxes, or some combination of the two for the purpose of increasing aggregate demand and expanding real output.

Contractionary fiscal policy - a decrease in government purchases of goods and services, an increase in net taxes, or some combination of the two for the purpose of decreasing aggregate demand and thus controlling inflation.

Neutral fiscal policy - Modest fiscal policy. Generally not a common stance to take as there is no intention of effecting economic activity - this is rare, especially in contemporary times.

- ***Methods of raising funds***

Governments spend money on a wide variety of things, from the military and police to services like education and healthcare, as well as transfer payments such as welfare benefits.

This expenditure can be funded in a number of different ways:

- Taxation of the population
- Seignorage, the benefit from printing money

Borrowing money from the population, resulting in a fiscal deficit

● ***Funding of deficits***

A fiscal deficit is often funded by issuing bonds, like Treasury bills or consols. These pay interest, either for a fixed period or indefinitely. If the interest and capital repayments are too great, a nation may default on its debts, most usually to foreign debtors.

● ***Levels of government***

In a democratic system, there are two ways to organize a government: a unitary system and a federal system.

Canada is an excellent example of a federal system of government in which there is one central or federal government and there are ten provincial governments. Underneath the provincial governments, there is a patchwork of local government.

The United Kingdom is an example of a unitary system in which there is effectively one central government with no provincial governments. There are, of course, local governments.

2.2.3 Expenditures and taxation

There are two types of expenditures: money spent on the delivery of goods and services and the transfer of funds to other levels of government.

All of the money that the government spends has a stimulative effect on the economy. The government is large enough that it can spend during periods of economic contraction thereby helping to prop up the economy and consumer confidence. This school of thought in which the government plays an activist role in stimulating the economy in times of recession and in easing their spending in times of success is called the Keynesian School, after the economist John Keynes. Keynes, a legendary speculator, formulated his theories during the Great Depression as governments in Europe and North America struggled to revive economies troubled by a pullback in the provision of private credit and the negative effects of beggar-thy-neighbour competitive currency devaluations.

The problem with this school of thought is that when it is applied, it is politically very appealing to be spending money during

a downturn and helping people when they need help. It is also politically very attractive to be spending money and helping people during a boom time.

It is also very appealing to try and redistribute goods to one group from other groups in the society. This is a very common objective of fiscal policy. Politicians in Western democracies often try to redistribute resources to people living in poverty from people living in comparative wealth. In Canada, one of the most controversial fiscal policy decisions of the post-war era was the Trudeau government's move during the oil crisis of 1978 to force Alberta to sell its oil and gas to Central Canadians at prices that were far below the price that Alberta could have received by selling those resources on the open international market. This constituted a real transfer of money from the people of Alberta to the people of Ontario and Quebec. People in the West are still bitter about that policy twenty years after the fact.

The types of goods that governments typically provide are called public goods. A good or a service is said to be a public good if it is characterized by an externality. This is best demonstrated by an example.

If I buy a chocolate bar, my consumption of that chocolate bar is excludable. If I choose to do so, I can eat the whole thing myself. If I eat the chocolate bar without sharing it, nobody else gets any benefit from it.

Consider now the case where I hire a security service to patrol my street. Not only is my house safer but so are the other houses on that street. However, in this case, I am the only one paying for the service from which everyone else derives a benefit. The other people living on my street are said to be "free-riding" on my provision of the security service. There is nothing that I can do to inhibit them from obtaining this benefit, short of cutting out the service altogether. If everyone on my street were to chip in for what would be the "optimal" level of security service, there would be inevitably some people who would not contribute anything and there would be others

who would not contribute their fair share. Relying on the group to privately provide this public good would mean that too little of it would be supplied.

Traditionally, governments have stepped in to the role of providing these public goods in order to get around the "free-riding" problem. They are deemed to be able to ascertain the optimal amount of the public good to be supplied and to be able to collect the funds to fund it.

Naturally, this is a value-driven exercise. One has to determine how the government should judge what is "optimal" and what is the individual's "fair share." In a democracy, these kinds of normative questions are answered by the people's vote.

In practice, expenditures are driven by all kinds of considerations.

Some people talk about "pork barrel" politics, a situation in which politicians reward their friends and constituents at the expense of people outside of their group. It is not difficult to imagine the local Member of Parliament arguing in favour of the maintenance of his local Armed Forces base and the removal of another base in someone else's riding.

There are other politicians and bureaucrats who have a set of ideological objectives to fulfill. They may want to make the taxation system more progressive, for example. This means taxing people with higher incomes at higher rates and, possibly, not taxing people in the lower income brackets at all.

The construction of the taxation system is very difficult. Another set of objectives may be to distort production as little as possible. That is, in designing the tax code, we may want to develop a set of rules that do not change the relative prices of goods and services (and therefore the decisions investors must make about where to invest and in what industry, etc.).

2.2.4 Borrowing

A government that wants to provide a great deal of goods and services to its people while not having the immediate tax revenue to

fund that expenditure can turn to the capital markets to borrow the necessary money. They do this primarily by issuing securities, either Treasury Bills or Treasury Bonds. All levels of government will borrow money at some point. These securities are obligations compelling the government to repay the borrowed amount at maturity and also to pay interest in the form of coupons at specific points in time.

● ***Borrowing has a number of effects.***

If a country borrows too much money, it has to pay a great deal of interest every year in order to service that debt. This represents money that could have been used to pay for program spending instead. By borrowing money, the government has placed a greater emphasis on spending in the present than in the future. It has discounted the value of future expenditure.

Depending on how much money the citizens of that country or that province save out of their own incomes, the borrowing government must sell its obligations to foreigners. By doing so, the government makes itself vulnerable to the shifting and often volatile sentiment of the international capital markets. If they have a sufficiently large external debt in relation to their GDP (as an indicator of their current and future capacity to repay), speculators might attack their currency or their country's bond markets forcing interest rates higher and causing the value of their economy to degrade in international terms.

Indeed, an excessive debt policy can lead to a vicious cycle of speculative attacks, followed by higher interest rates and higher interest payments that can cause an economic slowdown. Just when a simulative policy is required to help the economy struggle back to its normal growth trajectory, the government finds itself crippled by high interest rates and poor liquidity. Nobody else will lend the government money with which it can stimulate the economy under anything but the most onerous terms.

This vicious cycle is one that has plagued economies of the Third World, and particularly Brazil, for years.

On the other hand, it may be prudent to borrow during economic downturns in order to stimulate the economy with the intention of

repaying those funds (and thereby dampening the economy) in times of economic growth.

The conduct of fiscal policy is very complicated in its effects on the economy, its reliance on external factors and the value-driven objectives that characterize much of the redistribution of resources and other fiscal policy choices.

2.2.5 Economic and Monetary Effect:

- ***Economic effects of fiscal policy***

Fiscal Policy is used by governments to influence the level of aggregate demand in the economy, in an effort to achieve economic objectives of price stability, full employment and economic growth. Keynesian economics suggests that a government running a Budget Deficit or a lower surplus compaired to the previous finacial year, will stimuate aggregate demand. This can be used in times of ressision or low economic activity as an essentual tool in providing the framework for strong economic growth and working toward full employment.

During periods of high economic growth, a budget surplus can be used to decrease activity in the economy. A Budget surplus will be implemented in the economy if inflation is high, in order to achive the objective of price stability. The removal of funds from the economy will, by Keynesian Theory, reduce levels of aggregate demand in the econonmy and contract it, bringing about price stability.

Despite the importance of fiscal policy, a paradox exists. In the case of a government running a budget deficit, funds will need to come from public borrowing (the issue of government bonds), overseas borrowing or the printing of new money. When governments fund a deficit with the release of government bonds, an increase in intest rates aross the market can occur. This is because government borrowing creates higher demand for credit in finacial markets, causing lower AD due to lack of disposible income, contary to the objective of Budget Deficit. This concept is called crowding out.

● ***Monetary effects of fiscal policy***

The fiscal policy of a government can affect the monetary policy. Government borrowing competes for the same loanable funds as other investment, so an increased deficit may result in a rise in interest rates. Government debt also represents a form of money on the broad definition, increasing the money supply.

Let us do a simple excersise:

SELF ASSESSMENT QUESTION I

State whether the following are true or false:

(i) The term fiscal policy refers to the expenditure a government undertakes to provide goods and services and to the way in which the government finances these expenditures.

(ii) The objective of fiscal policy is to promote development in the public sector.

(iii) Government expenditure can be funded only through taxation on the population.

(iv) There are two types of expenditures: money spent on the delivery of goods and services and the transfer of funds to other levels of government.

Check your answer with the one provided at the end of the unit.

2.3 Indian Scenario

Let us now discuss the various modes of mobilization of resources in India.

2.3.1 Mobilization of resources through taxation

Broad trends in tax revenues in relation to GDP has seen that there has been a steady increase in the ratio of indirect taxation to GDP over the period from 9.6 per cent of GDP in 1970-71 to 14.3 per cent in l983-1984. The trend in direct taxes is somewhat different. Direct taxes as a percentage of GDP rose upto the mid-seventies reaching a peek of-3.6 per cent of GDF in 1975-1976 but thereafter the percentage actually declined and was estimated to be only about 2.8 per cent of GDP in 1983-1984 almost the same percentage as in

1970-1971. The share of direct taxes in total tax revenues steadily declined from 22 per cent in 1970-1971 to less than 18 per cent in 1982-83. This development is contrary to the normal expectation that the share of direct taxes would increase with development. The imbalance between direct and indirect taxation is one point of criticism frequently levelled against the Indian tax structure.

The relatively low share of direct taxes in total tax revenue suggested that there was scope for mobilizing additional revenues through direct taxes. But there were quite severe institutional and organizational difficulties achieving this objective. The organisational difficulties in increasing revenues from direct taxation arise from the fact that a very large part of economic activity in India takes place in the unorganised sector where the limited spread of modern accounting practices makes enforcement of direct taxation extremely difficult. Furthermore, the constitution provides that taxation of agricultural income is a state-subject outside the purview of the Central Government. In practice this has meant that direct taxation of agriculture (mainly through land revenue) has been extremely light and diminishing in importance.

There was certainly scope for raising a larger volume of direct tax revenues by spreading the tax net to cover individuals and business units' whish presently escape direct taxation to a very large extent. This was largely a matter of improving revenue administration and streamlining procedures. A number of steps have been taken towards this end in recent years. As far as personal income taxation was concerned the existing was to reduce the burden on the tax machinery arising from very large number of relatively low paid employees being within the tax net. Accordingly, the exemption limit which was Rs 10,000 prior to 1980-81, was raised to Rs 15,000 and it is estimated that this may have taken 1.5 million taxpayers, of a total of about 4.5 million, out of the tax net. Steps were also taken to tighten up lawn relating to charitable trusts which in the past served as vehicles for tax evasion. Furthermore all establishments with a gross turnover of over Rs. 4 million per year are now required to have their accounts audited, again with a view to minimising the scope for tax evasion.

All these measures aimed at increasing the effectiveness of direct tax laws have been combined with a reduction in marginal rates of taxation in order to promote greater voluntary compliance with direct taxation. The maximum marginal rate of income tax was as high as 97.7 per cent in the mid seventies. Such high rates encouraged evasion and for this reason the marginal rates were progressively reduced over time. Most recently in 1984-85 there has been a significant reduction of 5 percentage points in rates of tax applicable on all income slabs. The maximum marginal rate of taxation currently was 62 per cent.

The performance on revenue mobilisation through indirect taxes over the years was commendable and there was a steady increase in the indirect tax revenues as a percentage of GDP. This increase came mainly from excise and customs duties levied by the Centre with sales tax (levied by States) also showing healthy growth. A major problem with such heavy reliance upon indirect taxation was that the overall burden of indirect taxes could not be as progressive as if the same revenues were raised through direct income taxation.

Efforts have been made to differentiate to rate structure of indirect taxation by commodities so as to achieve a measure of progressivity but there are limits to what can be done in this respect. Studies of the incidence of indirect taxation based on the direct effect of taxes on final consumption goods have shown a reasonable degree of progressivity but more recent studies taking account of both the direct effect and the indirect effect of taxation on intermediate inputs traced through the input-output matrix have yielded different results7. These show that while a measure of progressivity in the total (direct and indirect) impact of indirect taxation was achieved at the very top income levels, the overall incidence on the general population was not progressive. This was probably because progressivity at the top was easily achieved by very high rates of tax on consumer durables and other luxuries but the direct, indirect burden of indirect taxation on other income groups showed much less differentiation because a substantial proportion of indirect tax revenue came from intermediate inputs which feed into a wide variety of outputs. The incidence of this taxation was therefore spread on all consumption

groups. These calculations could not be treated as definitive because of data problems and problems of aggregation, but they certainly pointed to a potential problem with continuing reliance on indirect taxation to increase the tax ratio.

Apart from the problem of lack of progressivity heavy reliance upon indirect taxation also has the effect that the cumulative burden of duties can sometimes be unduly high on particular commodities leading to unexpected distortions in the cost-price structure. There was increasing recognition of this problem and led to a strong demand for rationalisation either a by shifting to some sort of a value added taxation system, or if this was not administratively feasible, by shifting to a system of "set offs" for duties paid on inputs for selected products facing high rates-of duty. Similarly, there were pressures to reduce customs duties in some areas with a view to reducing domestic costs of production. All these rationalisations of the tax system were likely to involve some revenue loss. While this could be made up through other measures the basic conclusion remained that there was very limited scope for raising the ratio of indirect taxation to GDP without introducing distortions in the tax system.

2.3.2 Containment of current expenditure

In view of the limited scope for raising the tax ratio to GDP for the reasons discussed above, much of the scope for increasing Government savings in future must lie in the containment of growth in current expenditure. It is useful in this context to examine the components of current expenditure in order to determine areas where reductions can be contemplated.

One point needs to be clarified in this connection. While reductions in current expenditure will add to public savings and to that extent help to finance investment it should not be assumed that all current expenditure is wasteful. On the contrary, much of current expenditure is actually developmental expenditure. The breakdown of current expenditure reveals that education, health and economic services accounted for 52 per cent of total current expenditure in 1981-1982. This proportion rose over time from 46 per cent in 1975-1976. The proportion accounted for by general public services and defence declined from 46 per cent in 1975-1976 to about 40 per cent

in 1981-1982. Nevertheless, there was room for economising by containing growth in expenditure while maintaining quality of services through improvements in efficiency.

An important aspect of growth in current expenditure was the growth in interest payments. It shows that whereas most other items increased at a rate close to the total of current expenditures, the item interest payments increased very rapidly indeed. This growth in interest payments was the cumulative result of the increased reliance of the Government upon borrowing to meet its rapidly growing investment financing needs. As pointed out earlier the public sector is a deficit sector and it investment greatly exceeds its own savings. This led to heavy resort to borrowing over the years. The relative importance or borrowed funds (domestic and external) in the consolidated budgetary transactions of the Centre, States and Union territories can be seen that borrowed resources (including the budget deficit) increased substantially relative to total expenditures and also GDP. In 1975-1976 borrowing resources were 24 per cent of total expenditure and 4.5 percent of GDP. By 1984-1985 they increased to per cent respectively. This increase rising interest rates, is reflected in the rapidly rising level of interest payments.

2.3.3 Consequences of public borrowing

A major question regarding the increased resort to borrowing by the public sector is whether it led to excessive monetary expansion in the economy. This depends upon the form of borrowing. If Government borrowing takes the form of large budget deficits financed by the expansion of high powered money there is clearly a danger of excessive monetary expansion, which would in turn fuel inflation.

The increasing resort of the Centre and States to net borrowing as a means of financing the gap between revenues and expenditures mainly reflected rapid growth in domestic borrowing. Much of this borrowing consisted of small savings and provident funds which constituted non-inflationary mobilization of the community's resources. A large part of this borrowing also consisted of "market borrowing", mainly investment by the commercial banks in Government securities.

Market borrowing from the commercial banks may also be treated as non-inflationary in Indian institutional conditions. These resources are mobilized under the provision that a fixed percentage of the demand and time liabilities of the commercial banks should be invested in Government securities or Government approved securities. This is essentially a device for allocating the savings of the community mobilized by the banking system between the private sector and the public sector. In view of the fact that the banks remain the most important financial intermediaries in India, and also in view of the fact that deposit mobilisation by the banks is actively encouraged by fiscal concessions, it is reasonable that a share of these resources be diverted to the public sector. This is especially so when the public sector bears an extremely heavy burden of providing resources for investment in infrastructure sectors such as power, coal and railways. The percentage of demand and time liabilities to be invested in Government and Government approved securities has been steadily increased. It was 33 per cent in 1975-1976, and was raised to 34 per cent in 1977-1978, 35 per cent in 1981-1982 and finally to 36 per cent in 1984-1985.

The main potentially inflationary component of Government borrowing is the budgetary deficit which leads to a direct expansion in high powered money or the monetary base. This component has varied over time. It was fairly high as a percentage of GDP in the early years of the seventies, then declined in 1975-1976 and 1976-1977 and rose sharply again in 1979-1980 and 1980-1981. Subsequently it declined again. It must be emphasised however that it is difficult to evaluate the appropriative ness of any given level of budgetary deficit isolated from other monetary and financial developments. For example, in the period after 1980-1981 part of the expansionary impulse of high powered money creation through deficit financing of the period 1980-1981 and 1981-1982 was offset by a reduction in net foreign assets of the banking system as foreign reserves declined. In this case credit creation was not inflationary since it was offset by leakage of demand abroad financed by reduced reserves.

It is perhaps more appropriate to judge the monetary consequences of Government borrowing directly in terms of the end result of monetary expansion. It will be seen that although the rate of growth of high powered money increased considerably, the rate of growth of broad money (m3) in recent years varied around an average of 16 per cent. This was probably consistent with a growth rate of 5 per cent in real GDP and inflation of around 8 per cent per year. Thus the increased overall recourse to borrowing by government in recent years took place in a framework in which monetary stability was maintained. This was reflected in the relatively moderate rates of inflation in India . Inflation had accelerated considerably in 1975-1976 and again in 1979-1980 and 1980-1981. In both cases the upsurge was due to a combination of poor agricultural performance and a sharp rise in import prices. Apart from these episodes the average rate of inflation has not been too high though inflationary pressure has been greater in the 1980s than in the mid-1970s.

Let us do another simple exercise:

SELF ASSESSMENT QUESTION II

State whether the following are true or false:

(i) The imbalance between direct and indirect taxation is one point of criticism frequently levelled against the Indian tax structure.

(ii) The maximum marginal rate of income tax was as high as 90.7 per cent in the mid seventies

(iii) An important aspect of growth in current expenditure was the growth in interest payments.

(iv) It is perhaps more appropriate to judge the monetary consequences of Government borrowing directly in terms of the end result of monetary expansion.

(v) Increase in government expenditure leads to relatively moderate rates of inflation in India.

Check your answer with the one provided at the end of the unit.

2.4 Public enterprise savings

Internal generation of resources within the public sector assumes special importance in an economy such as India's in which substantial proportion if investment takes place in the public sector and these high proportions are expected to continue. The savings performance of the public sector enterprises is not very impressive especially considering the very large volume of investment in the public sector.

There was little or no improvement in the volume of savings generated by the departmental enterprises (mainly railways and Post & Telegraphs in the Central Government and irrigations in the States), the figure having fluctuated around 0.7 per cent of GDP over the period 1970-1971 to 1982-1983. There was a modest upward trend in the volume of savings generated by the non-departmental financial institutions (which includes part of the profits of the Reserve Bank). The performance of the non-departmental non-financial institutions appeared quite poor upto 1980-1981 with gross savings as a percentage GDP fluctuating around 0.8 per cent. There was a significant improvement in1981-1982 and 1981-1983. This increase was partly a reflection of the impact of the increase in the prices of domestic crude oil affected in 1981 whereby the price of domestic crude was raised from Rs.324.41 per ton for onshore crude and Rs.452.65 per tonne for offshore crude to Rs 1,182 per ton. This was expected to raise additional resources of Rs 1,100 crores per year.

2.4.1 Central Government Public Enterprise

Trends in gross savings of the non-departmental non-financial enterprises of the Central Government can be assessed from the reports of the Bureau of Public Enterprises. The trends in the gross internal resources generated by these enterprises in recent years (commercial profits after taxes plus depreciation) are summarized with internal resources of the petroleum sector taken separately. There was a very marked improvement in recent years in the total internal resources generated, which corresponds roughly to gross savings. Taking all enterprises together the net profits after taxes were negative

(a net loss) in 1978-1979, 1979-1980 and 1980-1981. However when depreciation is included, as it should be for measuring gross savings, the total resources generated 1982 were positive. In 1981-1982 there was a very substantial increase in gross internal resource generation due to both larger depreciation provisions and a conversion of the aggregate losses of public sector enterprises into net profits after tax. A large part of the improvement was obviously due to the resource generation by the petroleum companies. Internal resources generated by other enterprise also increased substantially in 1981-1982 and 1982-1983 but this was mainly because of depreciation provisions.

Non-petroleum enterprises as a group continued to make losses in commercial terms. This is mainly because of large losses in some enterprises especially coal and steel. Figures for 1983-1984 were not available but a deterioration in were likely performance of the public sector enterprises because two important sectors coal and steel, faced severe problems. In the case of coal, an increase in coal prices which was overdue because of rising costs of operation and a costly wage settlement was delayed until January 1984. Steel also suffered because of low off take reflecting poor demand in 1983-1984 and rising costs.

The need to mobilise additional resources from the public sector enterprises has been repeatedly emphasized in Plan documents and was becoming increasingly urgent as the economy approached the limits of raising the tax ratio and also the rate of private savings. The total capital invested in the Central Public sector enterprises as of 1 April 1983 was about Rs 30,000 crores (at historical cost) of which about half was in the form of equity. If this was to yield profits after tax of even 10 per cent of the book value of capital invested, the total profits of public sector enterprises would be about Rs 1,500 crores per year. This compares with realization of Rs 618 crores in 1982-1983, which was again largely due to the increase in petroleum prices. It is obviously difficult to establish norms for public sector profitability taking account of the many special factors which characterize public sector profitability taking account of the many special factors which characterize public sector operations.

Nevertheless it appeared that there was a large between the actual-performance of the public sector and a normative level of performance. This gap could well be of the order pf 0.5 per cent of GDP in terms of its potential contribution to public savings.

2.4.2 State Government Public Enterprises

The major no-departmental public enterprises in the States Electricity Boards (the electricity utilities) and the State Road Transport Corporations. The financial performance of both, aggregated for all States, during the Sixth Plan period indicated commercial losses .

Over the Sixth Plan period as a whole the total commercial losses of the State Electricity Boards and the State Road Transport Corporations amounted to Rs 4,140 crores.

At the time of formulation regarding resources generation from the State Electricity Boards and the State Electricity Boards and the State Road Transport Corporations was as follows.8 The State Electricity Boards were expected to make commercial losses (after providing for depreciation of Rs 4,400 crores at the prevailing levels of tariffs (assuming constant prices for inputs also). However with depreciation provisions at Rs 3,872 crores, the resources contribution at 1979-1980 rates of tariff was Rs- crores. The Sixth Plan envisaged that additional efforts would be made to reduce the projected losses to no more than Rs 900 crores in 1979-1980 prices in the Sixth Plan period. The actual performance presented above) should cumulative losses of Rs 3,294 crores in current prices! The total investment in the State Electricity Boards was almost Rs 40,000 crores all of which took the form of loans. The average interest at which these loans are to be serviced is quite low (about 7 per cent) and therefore the prevalence of losses reflects an inability to earn even a modest return on total capital invested. If the norm for financial performance were fixed at a profit of 2 per cent on capital invested after servicing the relatively low interest loans, the annual profit should be Rs 800 crores instead of annual losses of about Rs 650 crores. In other words the shortfall in resource mobilization compared to a modest norm in this sector was Rs 1,450 crores corresponding to about 0.75 per cent of GDP.

The performance of the Road Transport Corporations is also is appointing. The Sixth Plan had projected total losses in 1980-1981 to 1984-1985 of Rs 1,340 crores which, with depreciation included, yielded gross resources of Rs.506 crores. The objective was to take additional measures to wipe out the commercial losses entirely. Actual performance however showed annual losses of about Rs150 crores.

The problems of resource mobilisation in these two sectors are partly problems of pricing and partly problem of management. Both have to be tackled simultaneously. Because both types of activity are in the nature of public utilities, there is strong resistance to raising prices. However, there is no alternative to making the necessary adjustment especially in the interest of rational energy use in the economy. Existing electricity prices were below marginal cost of generation and though prices have been continuously raised to cover rising prices of inputs, electricity remained somewhat under priced. Much of the problem however arises from operational inefficiency in these sectors which also needs to be attacked directly.

To summarise, the savings performance of the Central and State owned public enterprises needed to be greatly improved in order to increase surplus generation in this sector. There was also a role for graduated price adjustments where prices may have got out of line. Rough calculations suggested that an increase of about 1.3 percentage point in public savings as a per cent of GDP could be achieved over time with appropriate action on this front.

2.5 Household Savings Behaviour

As noted earlier, growth of private household savings has been the major factor behind the growth of gross domestic savings in India. This expansion in private savings cannot be explained solely by the growth in income per head. Between 1970-1971 and 1978-1979 per capita income increased by only 13 per cent but the rate of private savings as a percentage of GDP increased from 12 per cent in 1970-1971 to 18 per cent in 1978-1979. Clearly there were other factors at work. There is considerable measure of agreement among analysis that the remarkable growth in private savings was the result of a

conscious policy of encouraging the development of financial institutions capable of mobilizing private savings combined with appropriate interest rate policy and fiscal incentives. This policy paid handsome dividends in that it succeeded not only in raising the level of private savings but also channelling an increasing proportion of savings through financial intermediaries, which was an added advantage since it helped to direct additional savings towards preferred areas of investments in line with development objectives.

2.5.1 Changing Structure of Private Savings

The structure of private household savings in terms of dis-aggregation into different categories of savings instruments reveals a major structural change in the composition of household savings with a steadily rising share of financial savings in total savings. In 1970-1971, when private household saving was only 12 per cent of GDP, the share of financial saving in this total was only 25 per cent. By 1982-1983 when private savings 16 per cent of GDP the share of financial savings had increased to 40 per cent.

There was a steady decline in the proportion of private savings taking the form of direct investment in physical assets with a rising share for financial instruments. There was a sharp increase in the share of bank deposits from 10.1 per cent in the period 1971-1972 to 1972-1973 to 16.5 per cent in the period 1976-1977 to 1978-1979. Thereafter there was a decline in this item in favour of net claims on Government (mainly small savings certificates issued by the Government). The share of bank deposits and Government securities together increased dramatically from 7.3 per cent in the period 1970-1971 to 1972-1973 to 17.1 per cent in 1979-1980 to 1981-1982. The share of private savings invested of shares and debentures, though small, has also increased in recent years.

2.5.2 Policy incentives for private savings

The success in mobilizing increasing volumes of private household savings through the financial system is the result of a

conscious policy of developing and expanding the institutional base for financial intermediation by encouraging the development of a variety of financial instruments, offering attractive interest rates for private savers through the nationalised banks and Government securities, and providing fiscal incentives In support of financial savings. These are discussed in detail below:

● ***Expansion of banking infrastructure and small savings scheme***

Expansion of banking services and facilities was given high priority especially after the nationalisation of commercial banks in 1969. The number of bank branches on 30 June, 1969 was only 8262. It had increased to 18,730 on 30 June 1975 and reached 44,000 on 30 June, 1983. A major effort has been made to extend banking into the rural areas to channel credit to those areas and also to mobilize financial surpluses emerging in rural areas in the wake of rising agricultural incomes. The number of rural branches increased from 1832 on 20 June 1969 to 6,806 on 30 June 1975 and 22,618 on 30 June1983. Parallel with the expansion of bank branches a major effort has been made to promote small savings schemes whereby individual savers could purchase interest purchase interest paying small savings certificates from post offices.

● ***Interest rate policy***

The rate of interest available to savers is a major instrument for promoting private savings and government policy thought to ensure that interest rates variety of financial instruments art attractive. A commonly held view regarding the use of interest rate policy for this purpose is that it should provide a positive real return to the saver. Interest rates offered on a variety of financial instruments ensured this.

Bank deposits remained the principal savings instrument used by rates savers and interest rates on term deposits were fixed at levels which provided a positive real return. For three-year deposits,

inflation rate was higher than the interest rate in 1975-1976 but thereafter, upto 1980-1981 interest rates were higher. The three year interest rate fell below the three-year inflation was lower thereafter. As far as five-year deposits were concerned, the interest rates were consistently above the average annual rate of inflation over the five years after 1975-1976.

Although interest rates on bank deposits of three years and above generally provided a positive return to savers, this was not the case with small savings certificates until recently. Until 1980-1981 National Savings Certificates provided a return of 6.5 percent for seven-year maturity and though seven-year inflation rate was around for in 1981-1982 a new Notional Savings Certificate (NSC VI & VII) was issued with maturity of 6 years and interest rate of 12 per cent (compound).These certificates are eligible for early encashment, with a 9 per cent interest rate payable after 3 years. This provided a strong positive expected return to savers. The results were evident from the mobilization of saving under the small savings scheme which increased very sharply from a level of Rs 1,105 crores in 1979/80 to Rs 2,200 crores in 1983/84 (revised estimates) and to Rs 2,400 crores in 1984/85 (budget estimates).

Until 1979-1980 the rate of interest payable on debentures issued by the corporate sector (seven year maturities) was limited to a maximum of 10.5 per cent. In 1980-1981 this was raised to 13.5 per cent. In 1982-1983 the ceiling of 13.5 per cent was applied only to convertible debentures (a new instrument which includes the option of converting a part of the value of the debenture within a specified period into equity at a fixed, usually discounted price). The ceiling on non-convertible debentures was raised to 15 per cent. These developments substantially raised the rate of interest available to private to private savers in the past ten years with a base level positive return ensured for highly secure and safe three year investment, with higher returns available as the term of maturity or degree of risk increases.

Now let us do another simple exercise:

SELF ASSESSMENT QUESTION III

State whether the following are true or false:

(i) Internal generation of resources within the private sector assumes special importance in an economy like India.

(ii) There was a very marked improvement in recent years in the total internal resources generated, which corresponds roughly to gross savings.

(iii) The savings performance of the Central and State owned public enterprises needed to be greatly improved in order to increase surplus generation in this sector.

(iv) Expansion of banking services and facilities was given high priority especially after the nationalisation of commercial banks in 1979.

(v) In 1982-83 the ceiling on non convertible debentures was raised to 10%

Check your answer with the one provided at the end of the unit.

2.6 Let Us Sum Up

Once again I would like you to sum up this unit within 150 words. You can use the available space provided below to write the same.

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2.7 Key Words

Fiscal Policy is used to accelerate the growth of the economy.

Funding of deficit in order to control rapid rise in price.

Borrowings is an action of borrowing money usually referred in bank loans.

Public Ownership means a situation where an industry is nationalized.

2.8 Probable Answers

SAQI :	(i) True	(ii) False	(iii) False	(iv) True
SAQII:	(i)True	(ii) False	(iii) True	iv) True
	(v) False			
SAQ III:	(i) False	(ii) True	(iii) True	(iv) False
	(v) False			

2.9 Reflective Questions

- Define Fiscal policy. List the different types of Fiscal Policies.
- Discuss how effectively the resources can be mobilized through taxation.
- Analyze the consequences of public borrowings with special reference to Indian scenario.
- Evaluate the performance of public enterprises in India regarding their savings.
- Critically evaluate the household saving behaviours of Indian people. Do you think that there is a lack of rationality behind their decision making?

2.10 Suggested Readings for Unit 2

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.) (Chapter 5&6)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004) (Chapter 1 to 6)
- Dewett K.K., Verma J.D. & Sharma M.L., Indian Economics, S.Chand & Company Ltd., New Delhi (Chapter 30 to 35)

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PART II

BLOCK 4
CONSUMER PROTECTION, CAPITAL MARKET & FOREIGN TRADE

INTRODUCTION

As you have already gone through the first three blocks where you have learned about the basic concepts of business environment in general; in the first block and subsequently in the following two blocks regarding controls, industrial policies, monetary policies, fiscal policies etc. By now I am sure that you have generated keen interest in this subject. But I am afraid, the study will be not meaningful to you unless if you do not see from the consumers' perspective. This block has been divided into three units so as to enable you to grasp the idea of consumers' protection in India and their responsibilities; the functioning of capital market in India and the direction of foreign trade in India. These units have been designed to enable you to understand in details about:

- Consumer protection through acts and the responsibilities of the consumers.
- Evolution, growth and functioning of Indian Capital Market
- Application of Foreign Exchange Management Act.

In sum this block will equip you with the broad understanding of issues and dimensions of consumer protection, brief idea about Indian capital Market and of course a critical review of FEMA.

While going through these units you are suppose to answer the Self Assessment Questions provided within each of the units to assess yourself about your understanding of the subject matter. In order to update yourself, it is always better if you read business magazines, news paper etc. regularly and also visit websites.

UNIT 1
CONSUMER PROTECTION

Structure

1.0 Objectives
1.1 Introduction
1.2 Consumer protection: Introduction and Definition
1.3 Objects of Consumer protection Act
1.4 Definition of Different terms under the act.
1.5 Redressal Machinery under the Act
1.6 Important Cases
1.7 Consumer rights and responsibilities
1.8 Let us sum up

1.0 Objectives

After going through this unit you will be able to:

- Define Consumer Protection.
- Discuss the objects of consumer protection
- Analyze the importance of redressal machinery under the Act
- Establish the problems of the Act with the help of case laws.
- Develop a paper on consumer rights and responsibilities.

1.1. Introduction

The importance of consumers in business environment can not simply be ignored. After the globalization, the paradigm has shifted from the sellers market to consumers' market. Hence it is always important to know the protections of consumers through various acts and their responsibilities and rights. This unit will highlight these issues in detail.

1.2 Consumer Protection: Introduction & Definitions

A consumer is a user of goods and services. Any person paying for goods and services which he uses is entitled to expect that the goods and services are of a nature and quality promised to him by the seller.

The earlier principle of "Caveat Emptor" or "let the buyer beware" which was prevalent has given way to the principle of "Consumer is King". The origins of this principle lie in the fact that in today's mass production economy where there is little contact between the producer and consumer, often sellers make exaggerated claims and advertisements which they do not intend to fulfill. This leaves the consumer in a difficult position with very few avenues for redressal. The onset on intense competition also made producers aware of the benefits of customer satisfaction and hence by and large, the principle of "consumer is king" is now accepted.

The need to recognise and enforce the rights of consumers is being understood and several laws have been made for this purpose. In India, we have the Indian Contract Act, the Sale of Goods Act, the Dangerous Drugs Act, the Agricultural Produce (Grading and Marketing) Act, the Indian Standards Institution (Certification Marks) Act, the Prevention of Food Adulteration Act, the Standards of Weights and Measures Act, the Trade and Merchandise Marks Act, etc which to some extent protect consumer interests. However, these laws required the consumer to initiate action by way of a civil suit which involved lengthy legal process proving to be too expensive and time consuming for lay consumers. Therefore, the need for a more simpler and quicker access to redressal to consumer grievances was felt and accordingly, it lead to the legislation of the Consumer Protection Act, 1986.

1.3 Objects of the Consumer Protection Act, 1986

The preamble to the Act states that the Act is legislated to provide for better protection of the interests of consumers and for that purpose to make provision for the establishment of consumer councils and other authorities for the settlement of consumer's disputes and for matters connected therewith.

The basic rights of consumers as per the Consumer Protection Act (CPA) are

- the right to be protected against marketing of goods and services which are hazardous to life and property
- the right to be informed about the quality, quantity, potency, purity, standard and price of goods, or services so as to protect the consumer against unfair trade practices
- the right to be assured, wherever possible, access to variety of goods and services at competitive prices
- the right to be heard and be assured that consumers' interests will receive due consideration at appropriate forums
- the right to seek redressal against unfair trade practices or restrictive trade practices or unscrupulous exploitation of consumers
- the right to consumer education

The CPA extends to the whole of India except the State of Jammu and Kashmir and applies to all goods and services unless otherwise notified by the Central Government.

1.4 Definitions of Important Terms

Before studying the provisions of the CPA, it is necessary to understand the terms used in the Act. Let us understand some of the more important definitions.

Complainant means :-

1. A consumer; or
2. Any voluntary consumer association registered under the Companies Act,1956 or under any other law for the time being in force; or
3. The Central Government or any State Government, who or which makes a complaint; or
4. One or more consumers where there are numerous consumers having the same interest

Complaint means any allegation in writing made by a complainant that :-

1. an unfair trade practice or a restricted trade practice has been adopted by any trader
2. the goods bought by him or agreed to be bought by him suffer from one more defects
3. the services hired or availed of or agreed to be hired or availed of by him suffer from deficiency in any respect
4. the trader has charged for the goods mentioned in the complaint a price excess of the price fixed by or under any law for the time being in force or displayed on the goods or any package containing such goods.
5. goods which will be hazardous to life and safety when used, are being offered for sale to the public in contravention of the provisions of any law for the time being in force, requiring traders to display information in regard to the contents, manner and effect of use of such goods ;with a view to obtaining any relief provided by law under the CPA.

Consumer means any person who :-

1. buys any goods for a consideration which has been paid or promised or partly paid and partly promised, or under any system of deferred payment (eg hire purchase or installment sales) and includes any other user of such goods when such use is made with the approval of the buyer, but does not include a person who obtains such goods for resale or for any commercial purpose ; or
2. hires or avails of any services for a consideration which has been paid or promised, or partly paid and partly promised, or under any system of deferred payment and includes any beneficiary of such services when such services are availed of with the approval of the first mentioned person

For the purposes of this defination "commercial purpose" does not include use by a consumer of goods bought and used bv him exclusively for the purpose of earning his livelihood by means of self-employment.

Goods means goods as defined in the Sale of Goods Act, 1930. Under that act, goods means every kind of movable property other than actionable claims and money and includes stocks and shares, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale.

Service is defined to mean service of any description which is made available to potential users and includes the provision of facilities in connection with banking, financing, insurance, transport, processing, supply of electrical or other energy, board or lodging or both, housing construction, entertainment, amusement or the purveying of news or other information but does not include the rendering of any service free of charge or under a contract of personal service.

Consumer dispute means dispute where the person against whom a complaint has been made, denies or disputes the allegation contained in the complaint.

Restrictive Trade Practice means any trade practice which requires a consumer to buy, hire, or avail of any good or as the case may be, services as a condition precedent for buying, hiring or availing of any other goods or services.

Unfair Trade Practice means unfair trade practice as defined under the Monopolies and Restrictive Trade Practices Act. The MRPT act has defined certain practices to be unfair trade practices. Defect means any fault, imperfection or shortcoming in the quality, quantity, potency, purity or standard which is required to be maintained by or under any law for the time being in force or under any contract, express or implied, or as is claimed by the trade in any manner whatsoever in relation to any goods.

Deficiency means any fault, imperfection or shortcoming or inadequacy in the quality, nature and manner of performance which is required to be maintained by or under any law for the time being in force or has been undertaken to be performed by a person in pursuance of a contract or otherwise in relation to any service.

Now let us do a simple exercise:

SAQ I

Fill up the blanks :

(1) The earlier principle of ------- ------ which was prevalent has given way to the principle of "Consumer is King".

(2) The need for a more simpler and quicker access to redressal to consumer grievances was felt and accordingly, it lead to the legislation of the Consumer Protection Act, -------.

(3) The right to be assured, wherever --------, access to variety of goods and services at competitive prices

(4) an unfair trade practice or a restricted trade practice has been adopted by any trader is considered as ---------- under the act.

Check your answer with the one provided at the end of the unit.

1.5 Redressal Machinery under the Act

- ***Consumer Protection Councils***

The interests of consumers are enforced through various authorities set up under the CPA. The CPA provides for the setting up of the Central Consumer Protection Council, the State Consumer Protection Council and the District Forum

- ***Central Consumer Protection Council***

The Central Government has set up the Central Consumer Protection Council which consists of the following members :-

(a) The Minister in charge of Consumer Affairs in the Central Government who is its Chairman, and

(b) Other official and non-official members representing varied interests

The Central council consists of 150 members and its term is 3 years. The Council meets as and when necessary but at least one meeting is held in a year.

● ***State Consumer Protection Council***

The State Council consists of :-

(a) The Minister in charge of Consumer Affairs in the State Government who is its Chairman, and

(b) Other official and non-official members representing varied interests

The State Council meets as and when necessary but not less than two meetings must be held every year.

Redressal Machinery under the Act

The CPA provides for a 3 tier approach in resolving consumer disputes. The District Forum has jurisdiction to entertain complaints where the value of goods / services complained against and the compensation claimed is less than Rs. 5 lakhs, the State Commission for claims exceeding Rs. 5 lakhs but not exceeding Rs. 20 lakhs and the National Commission for claims exceeding Rs. 20 lakhs.

● ***District Forum***

Under the CPA, the State Government has to set up a district Forum in each district of the State. The government may establish more than one District Forum in a district if it deems fit. Each District Forum consists of :-

(a) a person who is, or who has been, or is qualified to be, a District Judge who shall be its President

(b) two other members who shall be persons of ability, integrity and standing and have adequate knowledge or experience of or have shown capacity in dealing with problems relating to economics, law, commerce, accountancy, industry, public affairs or administration, one of whom shall be a woman.

Appointments to the State Commission shall be made by the State Government on the recommendation of a Selection Committee consisting of the President of the State Committee, the Secretary - Law Department of the State and the secretary in charge of Consumer Affairs

Every member of the District Forum holds office for 5 years or upto the age of 65 years, whichever is earlier and is not eligible

for re-appointment. A member may resign by giving notice in writing to the State Government whereupon the vacancy will be filled up by the State Government.

The District Forum can entertain complaints where the value of goods or services and the compensation, if any, claimed is less than rupees five lakhs. However, in addition to jurisdiction over consumer goods services valued upto Rs. 5 lakhs, the District Forum also may pass orders against traders indulging in unfair trade practices, sale of defective goods or render deficient services provided the turnover of goods or value of services does not exceed rupees five lakhs.

A complaint shall be instituted in the District Forum within the local limits of whose jurisdiction -

(a) the opposite party or the defendant actually and voluntarily resides or carries on business or has a branch office or personally works for gain at the time of institution of the complaint; or

(b) any one of the opposite parties (where there are more than one) actually and voluntarily resides or carries on business or has a branch office or personally works for gain, at the time of institution of the complaint provided that the other opposite party/parties acquiescence in such institution or the permission of the Forum is obtained in respect of such opposite parties; or

(c) the cause of action arises, wholly or in part.

● ***State Commission***

The Act provides for the establishment of the State Consumer Disputes Redressal Commission by the State Government in the State by notification. Each State Commission shall consist of -

(a) a person who is or has been a judge of a High Court appointed by State Government (in consultation with the Chief Justice of the High Court) who shall be its President;

(b) two other members who shall be persons of ability, integrity, and standing and have adequate knowledge or experience of, or have shown capacity in dealing with,

problems relating to economics, law, commerce, accountancy, industry, public affairs or administration, one of whom must be a woman.

Every appointment made under this hall be made by the State Government on the recommendation of a Selection Committee consisting of the President of the State Commission, Secretary -Law Department of the State and Secretary in charge of Consumer Affairs in the State.

Every member of the District Forum holds office for 5 years or upto the age of 65 years, whichever is earlier and is not eligible for re-appointment. A member may resign by giving notice in writing to the State Government whereupon the vacancy will be filled up by the State Government.

The State Commission can entertain complaints where the value of goods or services and the compensation, if any claimed exceed Rs. 5 lakhs but does not exceed Rs. 20 lakhs;

The State Commission also has the jurisdiction to entertain appeal against the orders of any District Forum within the State

The State Commission also has the power to call for the records and appropriate orders in any consumer dispute which is pending before or has been decided by any District Forum within the State if it appears that such District Forum has exercised any power not vested in it by law or has failed to exercise a power rightfully vested in it by law or has acted illegally or with material irregularity.

- ***National Commission***

The Central Government provides for the establishment of the National Consumer Disputes Redressal Commission The National Commission shall consist of -

(a) a person who is or has been a judge of the Supreme Court, to be appoint by the Central Government (in consultation with the Chief Justice of India) who be its President;

(b) four other members who shall be persons of ability, integrity and standing and have adequate knowledge or experience of, or have shown capacity in dealing with, problems relating to economics, law, commerce,

accountancy, industry, public affairs or administration, one of whom shall be a woman

Appointments shall be by the Central Government on the recommendation of a Selection Committee consisting of a Judge of the Supreme Court to be nominated by the Chief Justice of India, the Secretary in the Department of Legal Affairs and the Secretary in charge of Consumer Affairs in the Government of India.

Every member of the National Commission shall hold office for a term of five years or upto seventy years of age, whichever is earlier and shall not be eligible for reappointment.

The National Commission shall have jurisdiction :-

(a) to entertain complaints where the value of the goods or services and the compensation, if any, claimed exceeds rupees twenty lakhs.

(b) to entertain appeals against the orders of any State Commission; and

(c) to call for the records and pass appropriate orders in any consumer dispute which is pending before, or has been decided by any State Commission where it appears to the National Commission that such Commission has exercised a jurisdiction not vested in it by law, or has failed to exercise a jurisdiction so vested, or has acted in the exercise of its jurisdiction illegally or with material irregularity.

Complaints may be filed with the District Forum by :-

1. the consumer to whom such goods are sold or delivered or agreed to be sold or delivered or such service provided or agreed to be provided
2. any recognized consumer association, whether the consumer to whom goods sold or delivered or agreed to be sold or delivered or service provided or agreed to be provided, is a member of such association or not
3. one or more consumers, where there are numerous consumers having the same interest with the permission of the District Forum, on behalf of or for the benefit of, all consumers so interested

4. The Central or the State Government.

On receipt of a complaint, a copy of the complaint is to be referred to the opposite party, directing him to give his version of the case within 30 days. This period may be extended by another 15 days. If the opposite party admits the allegations contained in the complaint, the complaint will be decided on the basis of materials on the record. Where the opposite party denies or disputes the allegations or omits or fails to take any action to represent his case within the time provided, the dispute will be settled in the following manner:-

I. In case of dispute relating to any goods: Where the complaint alleges a defect in the goods which cannot be determined without proper analysis or test of the goods, a sample of the goods shall be obtained from the complainant, sealed and authenticated in the manner prescribed for referring to the appropriate laboratory for the purpose of any analysis or test whichever may be necessary, so as to find out whether such goods suffer from any other defect. The appropriate laboratory' would be required to report its finding to the referring authority, i.e. the District Forum or the State Commission within a period of forty- five days from the receipt of the reference or within such extended period as may be granted by these agencies.

- ***Appropriate laboratory means a laboratory or organization:-***

(i) recognized by the Central Government;

(ii) recognized by a State Government, subject to such guidelines as may be prescribed by the Central Government

(iii) any such laboratory or organization established by or under any law for the time being in force, which is maintained, financed or aided by the Central Government or a State Government for carrying out analysis or test of any goods with a view to determining whether such goods suffer from any defect.

The District Forum / State Commission may require the complainant to deposit with it such amount as may be specified towards payment of fees to the appropriate laboratory for carrying out the tests. On receipt of the report, a copy thereof is to be sent by

District Forum/State Commission to the opposite party along with its own remarks.

In case any of the parties disputes the correctness of the methods of analysis/test adopted by the appropriate laboratory, the concerned party will be required to submit his objections in writing in regard to the report. After giving both the parties a reasonable opportunity of being heard and to present their objections, if any, the District Forum/Slate Commission shall pass appropriate orders.

II. In case of dispute relating to goods not requiring testing or analysis or relating to services: Where the opposite party denies or disputes the allegations contained in the complaint within the time given by the District Forum / State Commission, it shall dispose of the complaint on the basis of evidence tendered by the parties. In case of failure by the opposite party to represent his case within the prescribed time, the complaint shall be disposed of on the basis of evidence tendered by the complainant.

- ***Limitation period for filing of complaint***

The District Forum, the State Commission, or the National Commission shall not admit a complaint unless it is filed within two years from the date on which the cause of action has arisen. However, where the complainant satisfies the District Forum / State Commission, that he had sufficient cause for not filing the complaint within two years, such complaint may be entertained by it after recording the reasons for condoning the delay.

- ***Powers of the Redressal Agencies***

The District Forum, State Commission and the National Commission are vested with the powers of a civil court under the Code of Civil Procedure while trying a suit in respect of the following matters:-

1. the summoning and enforcing attendance of any defendant or or witness examining the witness on oath;
2. the discovery and production of any document or other material producible as evidence;
3. the reception of evidence on affidavits;

4. the requisitioning of the report of the concerned analysis or test from the appropriate laboratory or from any other relevant source;
5. issuing of any commission for the examination of any witness; and
6. any other matter which may be prescribed.

Under the Consumer Protection Rules, 1987, the District Forum, Commission and the National Commission have the power to require any person :-

(i) To produce before, and allow to be examined by an officer of any authorities, such books of accounts, documents or commodities as may be required and to keep such book, documents etc. under its custody for the purposes of the Act;

(ii) To furnish such information which may be required for the purposes to any officer so specified.

They have the power to :-

(i) To pass written orders authorizing any officer to exercise power of entry and search of any premises where these books, papers, commodities, or documents are kept if there is any ground to believe that these may be destroyed, mutilated, altered, falsified or secreted. Such authorized officer may also seize books, papers, documents or commodities if they are required for the purposes of the Act, provided the seizure is communicated to the District Forum / State Commission / National commission within 72 hours. On examination of such documents or commodities, the agency concerned may order the retention thereof or may return it to the party concerned.

(ii) to issue remedial orders to the opposite party.

(iii) to dismiss frivolous and vexatious complaints and to order the complainant to make payment of costs, not exceeding Rs. 10,000 to the opposite party.

- ***Remedies Granted under the Act***

The District Forum / State Commission / National Commission may pass one or more of the following orders to grant relief to the aggrieved consumer :-

1. to remove the defects pointed out by the appropriate laboratory from goods in question;
2. to replace the goods with new goods of similar description which shall be free from any defect;
3. to return to the complainant the price, or, as the case may be, the charges paid by the complainant;
4. to pay such amount as may be awarded by it as compensation to the consumer for any loss or injury suffered by the consumer due to negligence of the opposite party;
5. to remove the defects or deficiencies in the services in question;
6. to discontinue the unfair trade practice or the restrictive trade practice or not to repeat them;
7. not to offer the hazardous goods for sale ;
8. to withdraw the hazardous goods from being offered for sale ;
9. to provide for adequate costs to parties.

- ***Appeals***

Any person aggrieved by an order made by the Forum may prefer an appeal to the State Commission in the prescribed form and manner. Similarly, any person aggrieved by any original order of the State Commission may prefer an appeal to the National Commission in the prescribed form and manner. Any person aggrieved by any original order of the National Commission may prefer an appeal to the Supreme Court.

All such appeals are to be made within thirty days from the date of the order provided that the concerned Appellate authority may entertain an appeal after the said period of thirty days if it is satisfied that there was sufficient cause for not filling it within that period. The period of 30 days is to be computed from the date of receipt of the order by the appellant.

Where no appeal has been preferred against any of the orders of the authorities, such orders would be final. The District Forum, State Commission or National Commission may enforce respective orders as if it were a decree or order made by a Court and in the event of their inability to execute the same, they may send the order to the Court for execution by it as if it were a Court decree or order.

● ***Penalties***

Failure or omission by a trader or other person against whom a complaint is made or the complainant to comply with any order of the State Commission or the National Commission shall be punishable with imprisonment for a term which shall not be less than one month but which may extend to 3 years, or with fine of not less than Rs. 2,000 but which may to Rs. 10000 or with both.

However, if it is satisfied that the circumstances of any case so requires, then the District Forum or the State Commission or the National Commission may impose a lower fine or a shorter term of imprisonment .

Now let us again do a small exercise :

SAQ II

State whether the following are true or false:

(1) The state Government has set up the Central Consumer Protection Council.

(2) The CPA provides for a 3 tier approach in resolving consumer disputes.

(3) Appointments to the State Commission shall be made by the State Government on the recommendation of a Selection Committee consisting of the President of the State Committee, the Secretary - Law Department of the State and the secretary in charge of Foreign Affairs

(4) The Act provides for the establishment of the State Consumer Disputes Redressal Commission by the State Government in the State by notification.

Check your answer with the one provided at the end of the unit.

1.6 Important Case Laws

● ***Gist of important Consumer Law Cases***

1. No compensation for defective machines purchased for manufacturing activities In the case of Abbay Chemicals Pvt. Ltd. v. Kanti Bhai D. Patel , the National Commission held that no compensation could be awarded in respect of defects of a machine worth more than Rs. 10 lakhs, purchased for use in large scale manufacturing activity, since the purchase would be for a commercial purpose and the buyer in such case would not be a consumer under the Consumer Protection Act. Similar decision was given in the case of Synco Textiles Pvt Ltd. v. Greaves Cotton & Co. Ltd.

2. Highly inflated electricity bills and defective electricity meter In the case of Y N Gupta vs DESU , the National Commission considered a complaint regarding the inflated electricity bills served by DESU on the complainant. In this case, DESU did not raise bills in keeping with the cycle normally adopted. It also did not replace the defective meter. However, it slapped the bill for over Rs. 1.06 lacs for a period from 21st December, 1988 to 25th March, 1990. The power connection was also disconnected but restored after making a complaint to the General Manager. The National Commission ruled that it was difficult to envisage a situation where the consumer could have utilised over 1 lakh units of electricity and the expect a poor consumer to pay bills of over a lakh. The National Commission ruled that the bills were casualty prepared. DESU did not have the authority to raise bills upon a defective meter beyond six months under the Electricity Act, 1910. In these circumstances, the National Commission concluded that there was deficiency in services on the part of DESU and awarded a compensation of Rs.30000 and costs of Rs. 5,000.

3. Government servants not doing any service for consideration but a statutory function In the case of S.P. Goel v. Collector of Stamps, it was held that a government official does not render any service in the course of doing his statutory duties. Hence, no remedy can be granted under the CPA. In this case, the complainant presented before the Sub-Registrar a document claiming it to be a will for registration. The Sub-registrar did not register the document claiming it to be a

deed of conveyance and hence not adequately stamped. He impounded the document and sent it to the Collector of Stamps for action. Despite several notices issued to him by the Collector, the appellant did not appear before him. When the appellant appeared before the Collector he was asked to furnish certain other documents. In the meantime, however, the appellant filed a complaint before the District Forum under the Consumer Protection Act alleging harassment by the Sub-Registrar and Collector and had prayed for compensation being awarded to him.

The District Forum held the view that the appellant having paid registration fees, he shall be treated to have hired the services of the Sub-Registrar and the Collector and since the Collector had not taken any decision as to the nature of the document for about six years, allowed compensation to be paid to the complainant.

On appeal by the Collector, the State Commission, upheld the order of the District Forum and enhanced the compensation to Rs. 5,000.

On the revision petition filed by the Collector, the National Commission held the view that the appellant was not a "consumer" under the CPA. because there was no hiring of services by the complainant for consideration and because a government official doing his duty as functionary of the State under law could not be said to be rendering a survive to the complainant. It stated that assuming the Collector was discharging a service, he was doing the same as a functionary of the government under the authority of the statute and for the benefit of the revenue for which he was being paid by the Government and not by the complainant.

The Supreme Court upheld the order of the National Commission on appeal.

4. Maintenance of Guest house - Not for commercial purpose In the case of J.K. Puri Engineers v. Mohan Breweries & Distilleries Ltd, it was held that a guest house maintained for company officials is not for commercial purposes and hence benefit under the CPA can be availed of.: The company maintained a guest house for use of its managing director and other executives. It entered into a contract with the appellants for the installation of a central air-conditioning system. The company alleged that the system installed did not

properly, developed snags, and that there was leakage of water from the dusting system. The appellant having failed to make good the defects, the complainant appointed a consultant and obtained from him a report on the working of the system which pointed out a number of defects. The State Commission held that the complainant was a consumer under the CPA and that the air-conditioning system had not been installed for a commercial purpose because the guest house was not maintained for a commercial purpose. The National Commission upheld the decision of the State Commission.

5. Failure to deliver houses by the housing board is deficiency in service. In the case of S.P. Dhavaskar v/s Housing Commissioner, Kamataka Housing Board & Vice Versa, the complainant had made a deposit of Rs. 1.66 lakhs with the Housing Board for a house proposed to be built by the Board. He was told that the construction be completed within two years from March, 1987. In March, 1992 he was informed that the construction was not upto the expected level because of the use of low cost technology and that the houses constructed developed distress and might not long and suggested that the complainant might take back the amount of deposit without interest or opt for a new house in lieu of the house already allotted. The complainant made a claim of Rs. 4.65 lakhs which was rejected. The State Commission held that the act of the Housing Board amounted to a deficiency in service and returning deposit amount without interest was unreasonable and ordered payment of interest at 18% p.a. In appeal, the National Commission upheld the order of the State Commission.

6. Failure to provide basic safeguards in the swimming pool amounted to deficiency in service. In the case of Sashikant Krishnaii Dole v. Shitshan Prasarak Mandali, the National commission held that failure to amount basic safeguards in the swimming pool amounts to deficiency in service. A school owned a swimming pool and offered swimming facilities to the public on payment of a fee. The school conducted winter and summer training camps to train boys in swimming and for this purpose engaged a trainer/coach. The complainants had enrolled their only son for learning swimming under the guidance of the coach. It was alleged that due to the negligence of the coach, the boy drowned and died. The school denied

any responsibility on its part. The coach claimed that he had considerable experience in coaching young boys is swimming. When the deceased was found to have been drowned, the coach immediately took him out of the water and removed the water from his stomach and gave him artificial respiration and thereafter took him to a doctor. The doctor advised that the boy be taken to the nearest hospital where the boy died. The State Commission held the school and the coach deficient in rendering service to the deceased. On appeal, the order was upheld by the National Commission.

7. Failure to settle provident fund claim in time amounts to deficiency in service. In the case of Regional Provident Fund Commissioner, Faridabad v. Shiv Kumar Joshi, it was held that failure to settle providend fund dues on time amounts to deficiency in service.

8. Removal of ladder of an aircraft while disembarking by the passenger amounts to deficiency in service. In the case of Station Manager, Indian Airlines v. Dr. Jiteswar Ahir, the National Commission held that removal of ladder while a passenger was disembarking, leading to injury to the passenger amounted to deficiency in service. The complainant after he was seated on the plane, was intimated by announcement that part of his luggage was lying on the ground unidentified. He moved towards the door and finding that the ladder was in place, tried to get down. But before he could get his entire body on the ladder, the ladder was moved as a result of which of which he fell to the ground and sustained injuries. The passenger demanded compensation of Rs. 10 lakhs from the Airline. The Airline was willing to pay Rs. 40000/- which was the maximum amount payable under the Carriage by Air Act, 1972. The State Commission ordered a compensation of Rs. 4 lakhs and Rs. 1 lakh for mental agony and distress plus costs. The order of the State Commission was upheld by the National Commission.

9. Imparting education is not a service. In the case of Chairman, Board of Examinations v. Mohideen Abdul Kader, the complainant, a student who wished to appear in the subject of production technology was denied permission to write that paper by the hall supervisor on the ground that his name appeared against Code No. 2 while the paper fell under Code No.1. He alleged that he was wrongly

restrained and prevented from writing the examination on that day because of the attitude and negligence of the staff and therefore he claimed compensation for the inconvenience caused to him. The National commission in its order stated that a candidate who appeared for an examination could not be regarded as a person who had hired or availed of the services of the university or board for consideration. Therefore he was not a consumer under the Consumer Protection Act and no compensation was awarded.

10. In the case of Poonam Verma v/s Ashwin Patel, it was held that a doctor qualified under the homeopathic system of medicines treats a patient with allopathic medicines, he is guilt of negligence and compensation is due if the patient dies on such account.

11. In the case of Bharathi Knitting Co. v. DHL Worldwide Express Courier Division of Airfreight Limited, it was held that the liability of the courier company in case of delayed delivery of articles was limited to the amount of damages agreed to under the contract. In the case of Devi Engineering Co v/s Union of India, it was held that the Post Office was not liable for wrong delivery of registered postal articles.

12. In the case of Department of Posts & Telegraphs v. Dr. R.C. Saxena, it was held that there is deficiency in service where the Post Office refuses to pay interest on deposits simply by invoking technical rules. In February, 1988 the consumer opened a national savings scheme account in the General Post Office in Lucknow. In March, 1989 he opened a similar account at Chamba (H.P.) depositing Rs. 90,000. On his retirement from service he got both accounts transferred to Kangra. When he wanted to close the account by withdrawing the balance, the post office refused to grant him interest on the Rs.90000 deposited by him in his second account on the ground that under the NSS rules, one person can have only one NSS account. The National Commission held that the opening of the second account was merely an irregularity not amounting to contravention of the rules and that the investor was entitled to interest on the second deposit.

13. In the case of Union of India v/s Nathmal Hansaria, it was held that the railways are liable for deficiency in service when a person passing through the inter connecting passage way between two compartments of a train fell down resulting in death.

14. In the case of Harshad J Shah v/s Life Insurance Corporation of India, it was held that the Life Insurance Corporation could not be held liable for lapse in policy due to non-payment of premium even if the premium was paid on time to the agent of LIC but was not paid by him to the LIC within the prescribed time.

1.7 Consumer Rights and Responsibilities

India has been observing 15 March since 1989 as the National Consumers' Day. This day has a historic importance as it was on this day in 1962, when the Bill for Consumer Rights was moved in the US Congress. During his speech President John F. Kennedy had remarked:

"If a consumer is offered inferior products, if prices are exorbitant, if drugs are unsafe or worthless, if the consumer is unable to choose on an informed basis, then his dollar is wasted, his health and safety may be threatened, and national interest suffers."

John F. Kennedy had equated the rights of the ordinary American consumer with national interest. He gave the American consumer four basic rights:

1. The Right to Safety - to be protected against the marketing of goods which are hazardous to health or life.
2. The Right to Choose - to be assured, wherever possible, access to a variety of products and services at competitive prices: and in those industries where competition is not workable and Government regulation is substituted, an assurance of satisfactory quality and service at fair prices.
3. The Right to Information - to be protected against fraudulent, deceitful or grossly misleading information, advertising, labeling, or other practices, and to be given the facts s/he needs to make an informed choice.
4. The Right to be Heard - to be assured that consumer interests will receive full and sympathetic consideration

in the formulation of Government policy, and fair and expeditious treatment in its administrative tribunals.

Kennedy recognized that consumers are the largest economic group in the country's economy, affecting and affected by almost every public and private economic decision. But they were also the only important group who were not effectively organized, whose views were not heard.

Therefore, the Federal Government, by nature the highest spokesman for all people, had a special obligation to the consumer's needs. Thirteen years later President Gerald Ford felt that the four rights constituted in Kennedy's Bill of Rights were inadequate for a situation where most consumers are not educated enough to make the right choices. So he added the Right to Consumer Education, as an informed consumer cannot be exploited easily.

While these rights served the interest of the American consumer well enough, they did not cover the whole gamut, because a global consumer did need, apart from them, other well-defined rights like basic needs, a healthy environment and redress.

The Consumers International (CI), former International Organization of Consumer Unions (IOCU), the umbrella body, for 240 organisations in over 100 countries, expanded the charter of consumers rights contained in the US Bill to eight, which in a logical order reads:

1. Basic Needs
2. Safety
3. Information
4. Choice
5. Representation
6. Redress
7. Consumer Education and
8. Healthy Environment.

This charter had a universal significance as they symbolized the aspirations of the poor and disadvantaged. On this basis, the United Nations, in April 1985, adopted its Guidelines for Consumer Protection.

● ***Birth Of Consumers' Day***

Considering the importance of Kennedy's speech to the US Congress on this day, and the resultant law, the CI took a decision in 1982 to observe 15 March as the World Consumer Rights Day from 1983. Peculiar though it may sound, 15 March is not observed as a special day in the world's largest and most pulsating consumer society - the US. But at home in India the Government, adopted 15 March as the National Consumer's Day.

India is a country, which never fell behind in introducing progressive legislation - we were among the first in the world to introduce universal adult franchise for women.

Gandhi had rightly said:

"A customer is the most important visitor on our premises. He is not dependent on us. We are dependent on him. He is not an interruption in our work - he is the purpose of it. We are not doing him a favour by serving him. He is doing us a favour by giving us the opportunity to serve him."

● ***Birth Of 'Copra'***

The right to redress lead to the passing of the Consumer Protection Act (COPRA) in 1986 in India which has been defined as the Magna Carta of consumers but, it recognises only six of these eight rights:

1. Safety;
2. Information;
3. Choice;
4. Representation;
5. Redress and
6. Consumer Education.

Besides this statutory recognition, COPRA has succeeded in bringing about revolutionary judicial reforms by providing juristic quasi-judicial courts solely for redressal of consumer grievances (where a price has been paid), for adjudication within a limited time frame of 90 to 150 days.

The rights of basic needs and healthy environment could not be provided in COPRA as these symbolized the aspiration of the

poor and the disadvantaged, and were not the subject matter of priced commodities and services available in the market place. However, these are the backbone of peoples' movements in both the developing and the developed worlds.

Yet, in spite of pulsating movements, the rights of consumers could and were trampled on and often. There existed a vacuum in the definition of rights. It was often seen that boycotts would be spontaneous or organized in an adversarial situation, examples of, which are numerous. On an occasion in Calcutta a boycott of fish was successfully organized and the marketing cartel had to bow down, by cutting the inflated prices, rather than store rotting fish.

- ***Right To Boycott***

Taking a leaf out of India's freedom movement, when Mahatma Gandhi had successfully organised various boycotts of foreign cloth, salt etc. we at CUTS, declared and adopted the 9th Consumer Right on India's Independence Day -15 August 1990: "The right to resist and boycott any person, goods or services in the event of conflict with consumer's interest".

This right was the ultimate one, to be used when all methods fail. And many a times they do: the seller does not heed, the administration does not listen, and the judiciary fails. This right inherently signifies consumer unity as an individual consumer can be helpless or even apathetic, and it is a collective action that succeeds.

While the right to boycott epitomizes the enability of consumer rights, the right to basic needs remained abstract. It only defined a consumer's necessities required to survive and live a dignified life but it did not demand the means to obtain them - the right to work.

However, the right to work is also vague, as this colloquially meant easy jobs, and did not feature in the existing charter of Consumer's Rights. In the interlude, a new Union Government in India raised a debate to recognize the right to work, as a fundamental right on the one hand, and advocating self employment schemes for everyone, including the poor, on the other.

Observing the societal disarray created by government job and dole schemes, whether permanent or temporary, and how they maim

the spirit of enterprise which prevails in the mass humanity of India, 'CUTS' was inspired to declare and adopt the 10th (enabling) Consumer Right on 26 January 1991: "The right to opportunities to acquire basic needs which will enable one to work and to earn a living, without exploitation."

This inherently demands execution of the state's singular responsibility to provide productive infrastructure, work ethos, job opportunities, social justice and economic equity. Both these rights were adopted at the Third National Convention of Consumer Activists at Calcutta during 1-3 November 1991, calling and urging the now (CI) IOCU to recognize and take suitable steps in expansion of the Consumer Rights internationally.

● ***India's Global Reputation***

Laws, rules, regulations and orders (for which India has unparalleled distinction in the Guinness book of records) alone do not protect consumers, but it is the rights' movement of people which produce results in a democracy.

One of the greatest achievements of the Indian consumer movement is the enactment of the dynamic consumer law: COPRA. Coming 39 years after Independence, it has acknowledged the rampant consumer abuses, including those of the government owned public utilities like telephones, transport, power etc. These utilities, in the first place, were created as state monopolies ostensibly to protect consumers!

Critics of COPRA rightly conclude that it can't do anything about rising prices, but it has succeeded in bringing about fair play in the supply of goods and services available in the market place, giving substance to the adage: Customer is King. Also, COPRA has encouraged active consumer bodies to demand, and perhaps see in the near future, independent Public Utility Regulatory Commissions to debate costing, pricing and promote competition.

This confidence emanates from the empowerment of voluntary organisations in COPRA and other consumer laws. While right to information is enshrined in COPRA, addition of the enlarged Right to Know in the fundamental rights chapter of the Indian Constitution would only result in meaningful empowerment - no more tight rope walking, but total glasnost.

In fact the Central Consumer Protection Council has recommended to the Government to enact a Freedom of Information Act on the pattern of a similar law in the US. Another major achievement of the Indian consumer movement in the context of the world scenario, was to get the government in 1989, to adopt 15 March, the World Consumer Rights Day, as the National Consumers' Day. Unlike the Labour Day on 1 May, which has roots in the US, the Consumer Rights Day, which also has roots in the US, is not even observed there.

Today India is the only country in the world, which has exclusive courts for consumer redressal. At the IOCU's 13th World Congress held in Hong Kong during 7-13 July 1991 it came in for praise and developed countries were called upon to emulate. In the same year, these developments inspired Jim Sugarman, a noted US consumer activist and a close associate of Ralph Nader, to candidly observe: "India is getting a global reputation for the rapid development of its consumer movement."

● ***Bureaucrat's Revenge***

COPRA, which was amended by an ordinance in June 1993, is a mixture of sad and happy tidings. And tragic because of one surprise which our bureaucrats sprung onto the bill, a matter which was not even discussed in the high power working group of the Central Consumer Protection Council.

The law then proposed a limitation of one year to file complaints, where none existed. An utter nonsense, which goes beyond the principles of our well established Limitations Act of 1963, wherein courts cannot be approached after the expiry of three years of the last cause of action.

Since there was no limitation period prescribed under COPRA, in one matter, the apex consumer court, the National Commission had pronounced that the principles of the Limitations Act do not apply but can be relied upon, though not religiously.

This proposal would not only have put consumers at a terrible disadvantage but also annoy them badly. Most warranties and guarantees on goods expire in one year, and manufacturers often

drag on many consumers during this period by attending to complaints, instead of setting it right or replacing or refunding the price of the defective goods. They will thus be deprived of the easy redressal avenue by this one-year 'deadline'.

Consumers will be angry because the rule on the time limit of 90/150 days provided in COPRA for disposal of cases are practiced more in the breach, and cases drag on for years. Under this situation, expecting consumers to meet a deadline will be very irritating. Granted that delayed complaints can be entertained, but that would mean a set of lengthy arguments on just the admissibility of the case.

Fourthly, the law also enables consumers to file class action complaints, which incidentally always existed, but there can be no basis to determine the deadline in such matters. For instance, if the Motor Vehicles Act, 1988 provides for certain mandatory safety features which have been ignored by manufacturers; after research, we decide to file a complaint what would be the limitation period?

Due to these arguments and lobbing the time limit was revised to two years, when the ordinance was put on the table of the parliament.

- ***Belying Expectations***

The law belied the consumer affairs Minister, A K Antony's note in the statement of objects and reasons, wherein he says the working of the redressal agencies has helped to arouse the expectations of the people on several other grounds as well.

Housing by way of plots or flats or houses has been covered under the definition of 'services' under COPRA. Rather than adopt the words: 'real estate', as defined under the MRTP Act, 1969 from which the whole definition clause of services was borrowed in the first instance, a new jargon: 'housing construction' is added. This would mean that the consumer courts will only entertain complaints relating to: flats, land, houses purchased or to be purchased.

In a beacon case involving a plot: Garima Shukla vs. UP Avas evam Vikas Nigam, the National Commission had held that the dispute is covered as a deficiency in the service of housing. The Supreme Court upheld the orders of the National Commission.

Among several other recommendations of the Central Council, another major one has also been diluted. In view of several protests

by consumers, the council had agreed to recommend incorporation of an open, democratic and a transparent process of selection of the non-official members of consumer courts.

The recommendation was that a selection committee headed by the minister and consisting of the secretary in charge of the department, a nominee of the chief justice of the state high court and two consumer activists (one a woman) would be the right form. The bill now proposes a committee headed by the President of the state commission and the consumer affairs secretary and the state law secretary.

It is thus heavily loaded against transparency. I have seen many a president of the State Commission sitting in the chamber of the secretary, especially when s/he is a retired high court judge. By and large the secretary has to follow the minister's orders, therefore the transparency sought in the selection process will be doubtful. Presence of two activists would have perhaps changed the odds.

However the president of the State Commission can only be appointed after consultation with the Chief Justice of the concerned high court, but those who know, consultation does not mean consent or concurrence. On several occasions, in spite of opposition, people have been appointed, after the so-called consultation.

● ***The Broom Stick***

The Council had made several other vital recommendations after long deliberations and critical debates, but they have been given the broomstick. These were:

1. Consumer rights were to be put in a separate chapter so that violations of the same could be an additional ground, if not the basis of a complaint. These will now continue as decorations in COPRA, for the central council to 'talk, about - only once in a year, as against twice as recommended'.
2. Services rendered by public health care system and civic bodies were to be covered, as they are not charities but are run from the taxpayer money. So that consumer could get value for money and these white elephants are brought to heel. The union health ministry prevailed.

3. Lawyers were to be debarred except when the complainant had engaged one, or with his consent or if the consumer court directed the parties to engage lawyers, when questions of law were involved. This was recommended because lawyers often delay the settlement of cases by court craft etc. Apparently the belligerent lawyers lobby proved stronger.
4. Writ jurisdiction of high courts has to be excluded by bringing COPRA under Article 323B of the constitution as their interference, particularly the Calcutta High Court, delays the proceedings especially when an hierarchy of appeals is provided under COPRA where the Supreme Court is the ultimate arbiter.
5. Empowering Consumer Courts by giving them the authority to order cease and desist, or interim injunction or take suo motu action (of its own accord and on its own information) like the MRTP Commission, so as to meet the ends of justice have not been incorporated. For, bureaucrats felt that it would give unbridled power to over 450 district fora and 30 state commissions and that would have created havoc.

Some readers might remember the case of ITC LTD's Wills brand being injuncted by a Gangtok district judge, which cost ITC a large sum of money to get it vacated from the Supreme Court under its extraordinary jurisdiction. This type of case is a freak but without such power our consumer courts will be hamstrung in protecting the consumers interest, as it were.

Section 1(4) of COPRA says this Act will apply to all goods and services, therefore under the definition of services, where illustrations are given, it was understood that it was an all inclusive definition and exclusions had to be specified.

To correct the anomaly, especially in view of the hectic lobbying by the medical fraternity and other professional groups, it was proposed to put a semi-colon, and add, "not limited to" before the illustrations. But this has also not been inserted in the amendment bill.

● ***Recalling Unsafe Goods***

So much so for the bureaucratic revenge and/or sabotage. However there are many welcome steps, though confused as well, which will take the consumer movement considerably forward. These are:

● Enhancement in the scope of relief under COPRA to stop the sale of and/or order withdrawing the marketing of hazardous goods. This will entitle consumers and consumer groups to challenge harmful goods, provided a law says so, like the BVO case when this toxic chemical was banned but continued to be used in soft drinks like Pepsi, Coca-Cola, Limca, Gold Spot etc.

But the clause does not empower consumers to challenge hazards in services. For instance the Electricity Act provides for certain safety measures to be adopted by the suppliers, but consumers may not be able to challenge it.

This is more so surprising when in all the consumer rights in COPRA 'services' have been added along with 'goods', and under the relief section power has also been given to consumer courts to remove defects and deficiencies in services.

● A major beneficial change has been added to cover agreements for purchase, as against the earlier provision for only goods or services actually purchased. This would cover disputes relating to booking of flats, cars, scooters and similar contracts, where delivery has not been made.

● Restrictive trade practices have been added, also enabling the courts to stop these, as well as unfair trade practices. This means that there would be a mini-MRTP Commission in every district.

● Monetary jurisdiction of a district forum has been raised to Rs 5 lakh, while that of a state commission to Rs 20 lakh. Beyond this, the National Commission. Age limit of the members of the state commissions has been fixed at 67, while that of the national commission at 70. No mention of the age limits of members of the district forums.

● Complaints against goods purchased for commercial purpose will ordinarily not be adjudicable under COPRA save and except where such goods in dispute have been purchased by a self-employed businessperson like a taxi owner-driver.

● Costs would be awardable to consumers or their organisations that win cases. Simultaneously consumers who file frivolous or vexatious complaints could be penalized with a fine of upto Rs 10,000. And if they don't pay up, they could face a worse fate of paying a further fine of upto Rs 10,000 and/or undergo imprisonment of upto three years like other offenders.

● Following the Supreme Court order, in the Common Cause Vs Union of India case, administrative control of district fora will now be under the state commissions, who will in turn report to the National Commission. A proper reporting system and procedures will also be incorporated.

Lastly, a quiet change has been incorporated to redefine the department of civil supplies as consumer affairs, which is what we in the consumer movement have been shouting for a long time.

Now let us do a small exercise :

SAQ III

State whether the following are true or false:

(1) India has been observing 15 March since 1990 as the National Consumers' Day

(2) Kennedy recognized that consumers are the largest economic group in the country's economy, affecting and affected by almost every public and private economic decision.

(3) The right to redress lead to the passing of the Consumer Protection Act (COPRA) in 1987 in India.

(4) The right to work is also vague, as this colloquially meant easy jobs, and did not feature in the existing charter of Consumer's Rights

Check your answer with the one provided at the end of the unit.

1.8 Let us sum up

A consumer is a user of goods and services. Any person paying for goods and services which he uses is entitled to expect that the goods and services are of a nature and quality promised to him by the seller.

The need to recognise and enforce the rights of consumers is being understood and several laws have been made for this purpose. In India, we have the Indian Contract Act, the Sale of Goods Act, the Dangerous Drugs Act, the Agricultural Produce (Grading and Marketing) Act, the Indian Standards Institution (Certification Marks) Act, the Prevention of Food Adulteration Act, the Standards of Weights and Measures Act, the Trade and Merchandise Marks Act, etc which to some extent protect consumer interests. However, these laws required the consumer to initiate action by way of a civil suit which involved lengthy legal process proving to be too expensive and time consuming for lay consumers. Therefore, the need for a simpler and quicker access to redressal to consumer grievances was felt and accordingly, it lead to the legislation of the Consumer Protection Act, 1986. The preamble to the Act states that the Act is legislated to provide for better protection of the interests of consumers and for that purpose to make provision for the establishment of consumer councils and other authorities for the settlement of consumer's disputes and for matters connected therewith.

One of the greatest achievements of the Indian consumer movement is the enactment of the dynamic consumer law: COPRA. Coming 39 years after Independence, it has acknowledged the rampant consumer abuses, including those of the government owned public utilities like telephones, transport, power etc. Quiet a number of change has been incorporated to redefine the department of civil supplies as consumer affairs, which is what we in the consumer movement have been shouting for a long time.

1.9 Key Words:

Consumer is a person or a body who buys and uses good or services

Consumer Protection means protecting consumers against unfair or illegal traders.

1.10 Probable Answers:

SAQI :	(i) Caveat emptor	(ii) 1986	(iii) possible
	(iv) complain		
SAQII:	(i) False	(ii)True	(iii)False
	(iv) True		
SAQIII:	(i) False	(ii)True	(iii)False
	(iv) True		

1.11 Reflective Questions:

- Define Consumer Protection. Discuss the objects of consumer protection
- Analyze the importance of redressal machinery under the consumer protection act.
- Establish the problems of the consumer protection act with the help of case laws.
- Develop a paper on consumer rights and responsibilities.

1.12 Suggested Readings for Unit 1:

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.) (Chapter 9, 10 &11)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004) (Chapter 8)
- Dewett K.K., Verma J.D. & Sharma M.L., Indian Economics, S.Chand & Company Ltd., New Delhi (Chapter 27,28 & 49)
- Chidambaram K; Alagappan ; Business Environment, Vikas Publishing house pvt. Ltd. (Chapter 5,7&12)

UNIT 2
INDIAN CAPITAL MARKET

Structure

2.0 Objectives
2.1 Introduction
2.2 Indian Capital Market- evaluation
2.3 Indian Stock Exchange
2.4 Institutional Investors
2.5 Other issues
2.6 Let us sum up

2.0 Objectives:

After going through this unit you will be able to:

- Discuss the evolution of Indian capital market
- Analyze the importance of Indian stock exchange in capital market growth.
- Establish the problems of institutional investors.
- Write a seminar paper on the Indian Capital Market.

2.1 Introduction

The importance of capital market in an economy can not be simply ignored. After the globalization, the importance of capital market even receives more importance because of the volatile movements in countries like India. In this unit the role of stock markets in India, role of institutional investors etc. has been detailed elaborately.

2.2 Indian Capital Market: Evolution

Indian Stock Markets are one of the oldest in Asia. Its history dates back to nearly 200 years ago. The earliest records of security dealings in India are meager and obscure. The East India Company was the dominant institution in those days and business in its loan securities used to be transacted towards the close of the eighteenth century.

By 1830's business on corporate stocks and shares in Bank and Cotton presses took place in Bombay. Though the trading list was broader in 1839, there were only half a dozen brokers recognized by banks and merchants during 1840 and 1850.

The 1850's witnessed a rapid development of commercial enterprise and brokerage business attracted many men into the field and by 1860 the number of brokers increased into 60.

In 1860-61 the American Civil War broke out and cotton supply from United States of Europe was stopped; thus, the 'Share Mania' in India begun. The number of brokers increased to about 200 to 250. However, at the end of the American Civil War, in 1865, a disastrous slump began (for example, Bank of Bombay Share which had touched Rs 2850 could only be sold at Rs. 87).

At the end of the American Civil War, the brokers who thrived out of Civil War in 1874, found a place in a street (now appropriately called as Dalal Street) where they would conveniently assemble and transact business. In 1887, they formally established in Bombay, the "Native Share and Stock Brokers' Association" (which is alternatively known as " The Stock Exchange "). In 1895, the Stock Exchange acquired a premise in the same street and it was inaugurated in 1899. Thus, the Stock Exchange at Bombay was consolidated.

- ***Other leading cities in stock market operations***

Ahmedabad gained importance next to Bombay with respect to cotton textile industry. After 1880, many mills originated from Ahmedabad and rapidly forged ahead. As new mills were floated, the need for a Stock Exchange at Ahmedabad was realised and in 1894 the brokers formed "The Ahmedabad Share and Stock Brokers' Association".

What the cotton textile industry was to Bombay and Ahmedabad, the jute industry was to Calcutta. Also tea and coal industries were the other major industrial groups in Calcutta. After the Share Mania in 1861-65, in the 1870's there was a sharp boom in jute shares, which was followed by a boom in tea shares in the 1880's and 1890's; and a coal boom between 1904 and 1908. On June 1908, some leading brokers formed "The Calcutta Stock Exchange Association".

In the beginning of the twentieth century, the industrial revolution was on the way in India with the Swadeshi Movement; and with the inauguration of the Tata Iron and Steel Company Limited in 1907, an important stage in industrial advancement under Indian enterprise was reached.

Indian cotton and jute textiles, steel, sugar, paper and flour mills and all companies generally enjoyed phenomenal prosperity, due to the First World War.

In 1920, the then demure city of Madras had the maiden thrill of a stock exchange functioning in its midst, under the name and style of "The Madras Stock Exchange" with 100 members. However, when boom faded, the number of members stood reduced from 100 to 3, by 1923, and so it went out of existence.

In 1935, the stock market activity improved, especially in South India where there was a rapid increase in the number of textile mills and many plantation companies were floated. In 1937, a stock exchange was once again organized in Madras - Madras Stock Exchange Association (Pvt) Limited. (In 1957 the name was changed to Madras Stock Exchange Limited).

Lahore Stock Exchange was formed in 1934 and it had a brief life. It was merged with the Punjab Stock Exchange Limited, which was incorporated in 1936.

Now let us do a simple exercise:

SAQ I

Fill up the blanks:

(1) Indian Stock Markets are one of the oldest in Asia & Its history dates back to nearly ------- years ago.

(2) However, at the end of the American Civil War, in ----, a disastrous slump began

(3) On June 1908, some leading brokers formed "The ------- Stock Exchange Association".

(4) Indian cotton and jute textiles, steel, sugar, paper and flour mills and all companies generally enjoyed phenomenal prosperity, due to the ----------World War

Check your answer with the one provided at the end of the unit.

2.3 Indian Stock Exchanges - An Umbrella Growth

The Second World War broke out in 1939. It gave a sharp boom which was followed by a slump. But, in 1943, the situation changed radically, when India was fully mobilized as a supply base.

On account of the restrictive controls on cotton, bullion, seeds and other commodities, those dealing in them found in the stock market as the only outlet for their activities. They were anxious to join the trade and their number was swelled by numerous others. Many new associations were constituted for the purpose and Stock Exchanges in all parts of the country were floated.

The Uttar Pradesh Stock Exchange Limited (1940), Nagpur Stock Exchange Limited (1940) and Hyderabad Stock Exchange Limited (1944) were incorporated.

In Delhi two stock exchanges - Delhi Stock and Share Brokers' Association Limited and the Delhi Stocks and Shares Exchange Limited - were floated and later in June 1947, amalgamated into the Delhi Stock Exchange Association Limited.

● *Post-independence Scenario*

Most of the exchanges suffered almost a total eclipse during depression. Lahore Exchange was closed during partition of the country and later migrated to Delhi and merged with Delhi Stock Exchange.

Bangalore Stock Exchange Limited was registered in 1957 and recognized in 1963.

Most of the other exchanges languished till 1957 when they applied to the Central Government for recognition under the Securities Contracts (Regulation) Act, 1956. Only Bombay, Calcutta, Madras, Ahmedabad, Delhi, Hyderabad and Indore, the well established exchanges, were recognized under the Act. Some of the members of the other Associations were required to be admitted by the recognized stock exchanges on a concessional basis, but acting on the principle of unitary control, all these pseudo stock exchanges were refused recognition by the Government of India and they thereupon ceased to function.

Thus, during early sixties there were eight recognized stock exchanges in India (mentioned above). The number virtually remained unchanged, for nearly two decades. During eighties, however, many stock exchanges were established: Cochin Stock Exchange (1980), Uttar Pradesh Stock Exchange Association Limited (at Kanpur, 1982), and Pune Stock Exchange Limited (1982), Ludhiana Stock Exchange Association Limited (1983), Gauhati Stock Exchange Limited (1984), Kanara Stock Exchange Limited (at Mangalore, 1985), Magadh Stock Exchange Association (at Patna, 1986), Jaipur Stock Exchange Limited (1989), Bhubaneswar Stock Exchange Association Limited (1989), Saurashtra Kutch Stock Exchange Limited (at Rajkot, 1989), Vadodara Stock Exchange Limited (at Baroda, 1990) and recently established exchanges - Coimbatore and Meerut. Thus, at present, there are totally twenty one recognized stock exchanges in India excluding the Over The Counter Exchange of India Limited (OTCEI) and the National Stock Exchange of India Limited (NSEIL).

The Table given below portrays the overall growth pattern of Indian stock markets since independence. It is quite evident from the Table that Indian stock markets have not only grown just in number of exchanges, but also in number of listed companies and in capital of listed companies. The remarkable growth after 1985 can be clearly seen from the Table, and this was due to the favouring government policies towards security market industry.

Table 2.1: Growth Pattern of the Indian Stock Market

Sl.No.	As on 31st December	1946	1961	1971	1975	1980	1985	1991	1995
1	No. of Stock Exchanges	7	7	8	8	9	14	20	22
2	No. of Listed Cos.	1125	1203	1599	1552	2265	4344	6229	8593
3	No. of Stock Issues of Listed Cos.	1506	2111	2838	3230	3697	6174	8967	11784
4	Capital of Listed Cos. (Cr. Rs.)	270	753	1812	2614	3973	9723	32041	59583
5	Market value of Capital of Listed Cos. (Cr. Rs.)	971	1292	2675	3273	6750	25302	110279	478121
6	Capital per Listed Cos. (4/2) (Lakh Rs.)	24	63	113	168	175	224	514	693
7	Market Value of Capital per Listed Cos. (Lakh Rs.) (5/2)	86	107	167	211	298	582	1770	5564
8	Appreciated value of Capital per Listed Cos. (Lak Rs.)	358	170	148	126	170	260	344	803

Source : Various issues of the Stock Exchange Official Directory, Vol.2 (9) (iii), Bombay Stock Exchange, Bombay.

- ***Trading Pattern of the Indian Stock Market***

Trading in Indian stock exchanges is limited to listed securities of public limited companies. They are broadly divided into two categories, namely, specified securities (forward list) and non-specified securities (cash list). Equity shares of dividend paying, growth-oriented companies with a paid-up capital of at least Rs.50 million and a market capitalization of at least Rs.100 million and having more than 20,000 shareholders are, normally, put in the specified group and the balance in non-specified group.

Two types of transactions can be carried out on the Indian stock exchanges: (a) spot delivery transactions "for delivery and payment within the time or on the date stipulated when entering into the contract which shall not be more than 14 days following the date of

the contract" : and (b) forward transactions "delivery and payment can be extended by further period of 14 days each so that the overall period does not exceed 90 days from the date of the contract". The latter is permitted only in the case of specified shares. The brokers who carry over the outstanding pay carry over charges (cantango or backwardation) which are usually determined by the rates of interest prevailing.

A member broker in an Indian stock exchange can act as an agent, buy and sell securities for his clients on a commission basis and also can act as a trader or dealer as a principal, buy and sell securities on his own account and risk, in contrast with the practice prevailing on New York and London Stock Exchanges, where a member can act as a jobber or a broker only.

The nature of trading on Indian Stock Exchanges are that of age old conventional style of face-to-face trading with bids and offers being made by open outcry. However, there is a great amount of effort to modernize the Indian stock exchanges in the very recent times.

● ***Over The Counter Exchange of India (OTCEI)***

The traditional trading mechanism prevailed in the Indian stock markets gave way to many functional inefficiencies, such as, absence of liquidity, lack of transparency, unduly long settlement periods and benami transactions, which affected the small investors to a great extent. To provide improved services to investors, the country's first ringless, scripless, electronic stock exchange - OTCEI - was created in 1992 by country's premier financial institutions - Unit Trust of India, Industrial Credit and Investment Corporation of India, Industrial Development Bank of India, SBI Capital Markets, Industrial Finance Corporation of India, General Insurance Corporation and its subsidiaries and CanBank Financial Services.
Trading at OTCEI is done over the centers spread across the country.
Securities traded on the OTCEI are classified into:

● ***Listed Securities -*** The shares and debentures of the companies listed on the OTC can be bought or sold at any OTC counter all over the country and they should not be listed anywhere else

- ***Permitted Securities -*** Certain shares and debentures listed on other exchanges and units of mutual funds are allowed to be traded
- ***Initiated debentures*** - Any equity holding at least one lakh debentures of a particular scrip can offer them for trading on the OTC.

OTC has a unique feature of trading compared to other traditional exchanges. That is, certificates of listed securities and initiated debentures are not traded at OTC. The original certificate will be safely with the custodian. But, a counter receipt is generated out at the counter which substitutes the share certificate and is used for all transactions.

In the case of permitted securities, the system is similar to a traditional stock exchange. The difference is that the delivery and payment procedure will be completed within 14 days.

Compared to the traditional Exchanges, OTC Exchange network has the following advantages:

- OTCEI has widely dispersed trading mechanism across the country which provides greater liquidity and lesser risk of intermediary charges.
- Greater transparency and accuracy of prices is obtained due to the screen-based scrip less trading.
- Since the exact price of the transaction is shown on the computer screen, the investor gets to know the exact price at which she is trading.
- Faster settlement and transfer process compared to other exchanges.
- In the case of an OTC issue (new issue), the allotment procedure is completed in a month and trading commences after a month of the issue closure, whereas it takes a longer period for the same with respect to other exchanges.

Thus, with the superior trading mechanism coupled with information transparency investors are gradually becoming aware of the manifold advantages of the OTCEI.

• ***National Stock Exchange (NSE)***

With the liberalization of the Indian economy, it was found inevitable to lift the Indian stock market trading system on par with the international standards. On the basis of the recommendations of high powered Pherwani Committee, the National Stock Exchange was incorporated in 1992 by Industrial Development Bank of India, Industrial Credit and Investment Corporation of India, Industrial Finance Corporation of India, all Insurance Corporations, selected commercial banks and others.

Trading at NSE can be classified under two broad categories:

(a) Wholesale debt market and

(b) Capital market.

Wholesale debt market operations are similar to money market operations - institutions and corporate bodies enter into high value transactions in financial instruments such as government securities, treasury bills, public sector unit bonds, commercial paper, certificate of deposit, etc.

There are two kinds of players in NSE :

(a) trading members and

(b) participants.

Recognized members of NSE are called trading members who trade on behalf of themselves and their clients. Participants include trading members and large players like banks who take direct settlement responsibility.

Trading at NSE takes place through a fully automated screen-based trading mechanism which adopts the principle of an order-driven market. Trading members can stay at their offices and execute the trading, since they are linked through a communication network. The prices at which the buyer and seller are willing to transact will appear on the screen. When the prices match the transaction will be completed and a confirmation slip will be printed at the office of the trading member.

NSE has several advantages over the traditional trading exchanges. They are as follows:

- NSE brings an integrated stock market trading network across the nation.
- Investors can trade at the same price from anywhere in the country since inter-market operations are streamlined coupled with the countrywide access to the securities.
- Delays in communication, late payments and the malpractice's prevailing in the traditional trading mechanism can be done away with greater operational efficiency and informational transparency in the stock market operations, with the support of total computerized network.

Unless stock markets provide professionalized service, small investors and foreign investors will not be interested in capital market operations. And capital market being one of the major source of long-term finance for industrial projects, India cannot afford to damage the capital market path. In this regard NSE gains vital importance in the Indian capital market system.

Now let us do another simple exercise:

SAQ II

State whether the following are true or false:

(1) The Second World War broke out in 1939.

(2) In Delhi two stock exchanges - Delhi Stock and Share Brokers' Association Limited and the Delhi capital and Shares Exchange Limited - were floated in 1946.

(3) Trading in Indian stock exchanges is limited to listed securities of public limited companies.

(4) The brokers who carry over the outstanding pay carry over charges which are usually determined by the rates of interest prevailing.

(5) OTC has a unique feature of trading compared to other traditional exchanges.

Check your answer with the one provided at the end of the unit.

2.4 Institutional Investors

- ***Role of FIIs in Indian capital market***

FIIs are contributing to the foreign exchange inflow as the funds from multilateral finance institutions and FDI are insufficient, says Abhijit Roy.

THE RECENT spat over the tax authorities issuing notices to foreign institutional investors (FIIs) which take advantage under the Indo-Mauritius Double Taxation Avoidance Agreement, has once again drawn attention to the role that FII investment is playing in the capital markets in India. This article endeavours to place the overall picture in perspective.

The Union Government allowed the entry of FIIs in order to encourage the capital market and attract foreign funds to India. Today, FIIs are permitted to invest in all securities traded on the primary and secondary markets, including equity shares and other securities listed or to be listed on the stock exchanges. The original guidelines were issued in September 1992. Subsequently, the Securities and Exchange Board of India (SEBI) notified the SEBI (Foreign Institutional Investors) Regulations, 1995 in November 1995.

Over the years, different types of FIIs have been allowed to operate in Indian stock markets. They now include institutions such as pension funds, mutual funds, investment trusts, asset management companies, nominee companies, incorporated/institutional portfolio managers, university funds, endowments, foundations and charitable trusts/societies with a track record. Proprietary funds have also been permitted to make investments through the FII route subject to certain conditions.

The SEBI is the nodal agency for dealing with FIIs, and they have to obtain initial registration with SEBI. The registration fee is $10,000. For granting registration to an FII, the SEBI takes into account the track record of the FII, its professional competence, financial soundness, experience and such other criteria as may be considered relevant by SEBI. Besides, FIIs seeking initial registration with SEBI will be required to hold a registration from an appropriate foreign regulatory authority in the country of domicile/incorporation

of the FII. The broad based criteria for FII registration has recently been relaxed. An FII is now considered as broad based if it has at least 20 investors with no investor holding more than 10 per cent of shares/units of the company/fund.

The SEBI's initial registration is valid for five years. The Reserve Bank of India's general permission to FIIs will also hold good for five years. Both will be renewable. There are approximately 500 FIIs registered with SEBI, but not all of them are active.

The RBI, by its general permission, allows a registered FII to buy, sell and realize capital gains on investments made through initial corpus remitted to India, subscribe/renounce rights offerings of shares, invest in all recognized stock exchanges through a designated bank branch and appoint domestic custodians for custody of investments held.

FIIs can invest in all securities traded on the primary and secondary markets. Such investments include equity/debentures/ warrants/other securities/instruments of companies unlisted, listed or to be listed on a stock exchange in India including the Over-the-Counter Exchange of India, derivatives traded on a recognized stock exchange and schemes floated by domestic mutual funds. A major feature of the guidelines is that there are no restrictions on the volume of investment - minimum or maximum - for the purpose of entry of FIIs. There is also no lock-in period prescribed for the purpose of such investments.

Further, FIIs can repatriate capital gains, dividends, incomes received by way of interest and any compensation received towards sale/renouncement of rights offering of shares subject to payment of withholding tax at source. The net proceeds can be remitted at market rates of exchange.

All secondary market operations would be only through the recognized intermediaries on the Indian stock exchanges, including OTCEI. Forward exchange cover can be provided to FIIs by authorized dealers both in respect of equity and debt instruments, subject to prescribed guidelines. Further, FIIs can lend securities through an approved intermediary in accordance with stock lending schemes of SEBI.

● ***Investment restrictions***

Portfolio investments in primary or secondary markets were initially subject to a ceiling of 24 per cent of issued and paid up share capital for the total holdings of all registered FIIs in any one company, taking into account the conversions arising out of the fully and partly convertible debentures issued by the company. Further, the maximum holding of 24 per cent, for all FII investments did not include portfolio investments by non-resident Indians (NRIs), NRI-OCBs (overseas corporate bodies), direct foreign investments, offshore single/regional funds, global depository receipts and euro convertibles. In the case of public sector banks, the overall limit is 20 per cent of the paid-up capital.

In 1997, it was decided to increase the limit of aggregate investment in a company by FIIs to 30 per cent of issued and paid-up share capital, subject to the condition that the board of directors of the company approved the limit and the general body of the company passed a special resolution in this behalf. Further, the Finance Minister in his budget speech in February this year announced that, subject to approval by the board of directors and a special resolution of the general body of the company, this limit of foreign portfolio investment was being increased to 40 per cent of issued and paid-up capital of a company.

The holdings of a single FII in any company are also subject to a ceiling of 10 per cent of total issued capital. For this purpose, the holdings of an FII group will be counted as holdings of a single FII. In addition to FIIs, NRIs, OCBs and Persons of Indian Origin (PIOs) are allowed to invest in the primary and secondary capital markets in India through the portfolio investment scheme (PIS). Under this scheme, NRIs/OCBs/PIOs can acquire shares/debentures of Indian companies through stock exchanges in India.

The ceiling on overall investment is 10 per cent for NRIs/OCBs/PIOs. This ceiling can be raised to 24 per cent, subject to the approval of the general body of the company passing a resolution to that effect. Further, the ceiling for FIIs is independent of the ceiling of 10/24 per cent for NRIs/OCBs/PIOs. If one adds the amount that can be raised by Indian companies in the form of FDI and euro issues, one

realizes that the foreign investment norms applicable to Indian companies have become liberal.

The RBI monitors the ceilings on FII/NRI/OCB/PIO investments in Indian companies on a daily basis. In order to prevent crossing of the ceilings, the RBI has fixed cut-off points that are two percentage points lower than the actual ceilings. The cut-off point, for instance, is fixed at 8 per cent for companies in which NRIs/ OCBs/ PIOs can invest up to 10 per cent of the company's paid up capital. The cut-off limit for companies with 24 per cent ceiling is 22 per cent and for companies with 30 per cent ceiling, is 28 per cent. Similarly, the cut-off limit for public sector banks (including State Bank of India) is 18 per cent.

Once the aggregate net purchases of equity shares of the company by FIIs/NRIs/OCBs/PIOs reach the cut-off point, the RBI cautions all designated bank branches so as not to purchase any more equity shares of the respective company on behalf of FIIs/NRIs/ OCBs/PIOs without prior approval of the RBI. On reaching the aggregate ceiling limit, the RBI advises all designated bank branches to stop purchases on behalf of their FIIs/NRIs/OCBs/PIOs clients. The RBI also informs the general public about the `caution' and the `stop purchase' in these companies through press releases.

Under the FII route for investment under the portfolio management scheme, there are two basic routes for investment by FIIs. The first is for mainly equity related instruments wherein the quantum of debt instruments can be up to a maximum of 30 per cent of the total investment. The other scheme is for 100 per cent debt related instruments. Transactions in debt securities include transactions in government securities and treasury bills which will be carried out in a manner specified by the RBI. Investments under the 100 per cent debt route will be permitted in debentures which are listed or to be listed, dated government securities and treasury bills. FII investment in debt through the 100 per cent debt route is subject to an overall debt cap for investment by all FIIs. These dedicated debt funds for the purpose of balance of payment management will come under the overall level of external commercial borrowings. Individual ceilings will depend on the track record of the FII and its experience in managing debt funds in emerging

markets. The Government is a little wary of allowing substantial investments in the debt market, including investment in treasury bills, on account of the experience of some nations where once the exchange rate came under pressure, there was sudden outflow of funds, thus worsening the exchange rate and balance of payment positions further.

For carrying out transactions, the FIIs should designate a bank branch and open accounts in that branch. The investment operations of FIIs will be conducted through the bank branch designated by them. The RBI will permit the designated bank branch to open a foreign currency denominated account and a special non-resident rupee account in the name of the FII. The FII will also be permitted to (a) transfer funds from foreign currency account to rupee account and vice versa, (b) make investments out of the balance in the rupee account, (c) credit the sale proceeds of shares and other investments as also dividend/interest earned on the investments in the rupee account, and (d) transfer the repatriable proceeds (net of taxes) from the rupee account to the foreign currency account.

The RBI will make available to the designated bank branches a list of companies where no further investment will be allowed.

FIIs can also appoint as custodian, an agency approved by SEBI. The custodian will be in charge of all securities of the FII and will report to SEBI/RBI in order to comply with the disclosure and reporting guidelines. At present there are 14 registered custodians. There are however some restrictions. An FII will not engage in any short selling in securities. Also, it has to take delivery of securities purchased and effect delivery of securities sold.

Firm allotment to FIIs in public issues can be done subject to the maximum ceiling applicable for all FIIs and 10 per cent for a single FII. Preferential allotment also can be made to FIIs subject to ceilings and fulfilment of certain conditions including price norms.

The price at which the shares are offered should be the higher of the following:

The highest price during the last 26 weeks prior to the relevant date, that is, 30 days prior to the date of the resolution passed by the general body of shareholders under Sec. 81(1A) of the Companies Act.

The average price of the weekly high and low of the closing prices during the two weeks preceding the relevant date.

- ***Tax provisions***

The tax on interest payment on bonds held by FIIs is 20 per cent.

Dividend on shares held by them is exempt after June 1, 1997.

Short-term capital gains are taxed at 30 per cent while long-term capital gains are taxed at 10 per cent.

The provisions of Avoidance of Double Taxation Agreement will however be applicable. However, on account of the concessional rate of income tax on capital gains, the provisions now available to non-residents for protection from fluctuation of the rupee value against foreign currency for computing capital gains arising from the transfer of securities of an Indian company will not apply to the FIIs which are covered under Sec. 115AD of the Income-tax Act. Further, the benefit of cost inflation indexation will also not be available to FIIs while computing long-term capital gains arising to them on transfer of securities. Shares in a company will have to be held for more than 12 months in order to qualify as a long-term capital asset. Other securities will have to be held for more than 36 months in order to qualify as a long-term capital asset.

The tax benefits accorded to FIIs have become a controversial issue. The route taken by FIIs for investment in India has been usually the Mauritius route as Mauritius based residents, including FIIs, will not be taxed in respect of capital gains on sale of business. It was known from the beginning that FIIs were taking this route in order to take advantage of the treaty, and once a certificate of residency is issued by the Mauritius authorities, Indian tax authorities do not have any option but to accept this method of investing in India.

The question then arises as to the wisdom of allowing this route. One argument of levying a tax is that domestic investors have to pay tax in the case of capital gains, which is now 10 per cent in the case of shares and units. On the other hand, the FIIs say that India is competing with other capital markets, and in most cases no capital gains are payable. The debate continues.

● ***Foreign brokers in India***

With a view to facilitating the operational procedures for foreign institutional investment in India and encouraging the present investment trends, it was decided to increase the role of foreign brokers in transactions of FIIs by allowing them to provide assistance to the FIIs registered with SEBI in their dealings in India.

A few foreign broking firms have set up fully owned subsidiaries in India. These broking outfits can deal directly in the Indian stock markets. Further, custodial services could be rendered by custodians approved by SEBI.

The FIIs have been playing a major role in the Indian capital market with cumulative investments having reached $11.24 billion by March-end 2000. As compared to this, the cumulative amount of foreign direct investment (FDI) since 1991 up to December end 1999 has been estimated at $19.2 billion. The market capitalization varies depending on share market prices.

● ***Impact on prices***

Along with the domestic mutual funds, the FIIs have started playing a critical role in the movement of stock prices. The assets under management of domestic mutual funds have crossed Rs. 100,000 crores. About half of these funds are income funds, and the remaining balanced funds and equity funds. Hence, the FIIs and the domestic mutual funds play an important part in the movement of stock prices. A few other developments have strengthened the role of the FIIs. The Unit Trust of India's share in mutual fund collection has been going down. In fact, the UTI today is more successful with its income funds rather than with equity funds. In recent months, privately managed domestic mutual funds have been the most successful in garnering fresh funds from the public. Not surprisingly a few of these foreign owned fund managers are also well known names among FIIs.

Another development during recent years has been the declining role of development financial institutions (DFIs) such as IDBI, ICICI and IFCI in the capital markets. This is partly on account of their

limited access to cheap funds and partly because of the withdrawals of the convertibility clause under which these DFIs managed to acquire equity shares of companies which were financed by them.

A positive contribution of the FIIs has been their role in improving the stock market infrastructure. The SEBI has no doubt contributed much in improving the stock exchange infrastructure. However, it is doubtful whether one would have witnessed such rapid developments in computerizing the operations of the stock markets and introduction of paperless trading in the demat form if the FIIs had not built up pressure on the authorities to move in this direction. The FIIs are playing an important role in bringing in funds needed by the equity market. Additionally, they are contributing to the foreign exchange inflow as the funds from multilateral finance institutions and FDI are insufficient. However, the fact remains that FII investments are volatile and market driven, but this risk has to be taken if the country has to ensure steady inflow of foreign funds.

The Securities and Exchange Board of India is the nodal agency for dealing with FIIs.

An FII is considered broad based if it has at least 20 investors with no investor holding more than 10 per cent of shares/units of the company/fund.

The Reserve Bank of India, by its general permission, allows a registered FII to buy, sell and realize capital gains on investments made through initial corpus remitted to India.

FIIs can invest in all securities traded on the primary and secondary markets.

FIIs can repatriate capital gains, dividends, incomes received by way of interest and any compensation received towards sale/ renouncement of rights offering of shares subject to payment of withholding tax at source.

The RBI monitors the ceilings on FII/NRI/OCB/PIO investments in Indian companies on a daily basis.

Portfolio investments in primary or secondary markets were initially subject to a ceiling of 24 per cent of issued and paid up share capital. In 1997, it was decided to increase the limit of aggregate investment in a company by FIIs to 30 per cent. The Finance Minister

in his budget speech in February this year announced that, subject to approval by the board of directors and a special resolution of the general body of the company, this limit of foreign portfolio investment was being increased to 40 per cent of issued and paid-up capital of a company.

The provisions of Avoidance of Double Taxation Agreement will be applicable.

The route taken by FIIs for investment in India has been usually the Mauritius route.

Mauritius based residents, including FIIs, will not be taxed in respect of capital gains on sale of business provided they have a certificate of residency from that government.

Along with mutual funds, FIIs have a crucial role in stock price movements.

● ***Mutual Funds***

Indian investors have been able to invest through mutual funds since 1964, when UTI was established. Indian mutual funds have been organized through the Indian Trust Acts, under which they have enjoyed certain tax benefits. Between 1987 and 1992, public sector banks and insurance companies set up mutual funds. Since 1993, private sector mutual funds have been allowed, which brought competition to the mutual fund industry. This has resulted in the introduction of new products and improvement of services. The notification of the SEBI (Mutual Fund) Regulations of 1993, brought about a restructuring of the mutual fund industry. An arm's length relationship is required between the fund sponsor, trustees, custodian,and asset management company. This is in contrast to the previous practice where all three functions, namely trusteeship, custodianship, and asset management, were often performed by one body, usually the fund sponsor or its subsidiary. The regulations prescribed disclosure and advertisement norms for mutual funds, and, for the first time, permitted the entry of private sector mutual funds. FIIs registered with SEBI may invest in domestic mutual funds, whether listed or unlisted. The 1993 Regulations have been revised on the basis of the recommendations of the Mutual Funds 2000

Report prepared by SEBI. The revised regulations strongly emphasize the governance of mutual funds and increase the responsibility of the trustees in overseeing the functions of the asset management company. Mutual funds are now required to obtain the consent of investors for any change in the "fundamental attributes" of a scheme, on the basis of which unit holders have invested. The revised regulations require disclosures in terms of portfolio composition, transactions by schemes of mutual funds with sponsors or affiliates of sponsors, with the asset management company and trustees, and also with respect to personal transactions of key personnel of asset management companies and of trustees.

Now let us do a simple exercise:

SAQ III

State whether the following are true or false:

(1) FIIs are contributing to the foreign exchange inflow as the funds from multilateral finance institutions and FDI are sufficient.

(2) The Union Government allowed the entry of local people in order to encourage the capital market and attract foreign funds to India.

(3) For carrying out transactions, the FIIs should designate an insurance branch and open accounts in that branch.

(4) Shares in a company will have to be held for more than 06 months in order to qualify as a long-term capital asset.

Check your answer with the one provided at the end of the unit.

2.5 Other Issues

- ***Primary Market***

Since 1991/92, the primary market has grown fast as a result of the removal of investment restrictions in the overall economy

and a repeal of the restrictions imposed by the Capital Issues Control Act. In 1991/92, Rs62.15 billion was raised in the primary market. This figure rose to Rs276.21 billion in 1994/95. Since 1995/1996, however, smaller amounts have been raised due to the overall downtrend in the market and tighter entry barriers introduced by SEBI for investor protection (Table 2.2-1).

Table 2.2 -1

Table 1 : Issues in the Primary Market

	Public		Rights		Total	
Year	Number	Amount (Rs.Billion)	Number	Amount (Rs.Billion)	Number	Amount (Rs.Billion)
1994-95	1,342	210.44	350	65.88	1,692	276.32
1995-96	1,426	142.39	299	65.64	1,725	208.03
1996-97	753	115.65	131	27.19	884	142.84
Dec. 1997					59	21.99

Source : Reserve Bank of India.

Total market capitalization as of 1997/98 was Rs5,898 billion (Table 2), equivalent to about half of India's annual gross domestic product (GDP) for the same fiscal year. India compares favorably with other emerging markets in this respect. The market capitalization- GDP ratio at end-1995 was 22.4 percent for Brazil; 12.6 percent for Hong Kong, China;40 percent for Indonesia; 41 percent for Korea;and 37.1 percent for Mexico.1 It was higher however,in Malaysia (281.9 percent), Philippines (81.3), Singapore (233 percent), and Thailand (152.9 percent).

Table 2.2 -2

Table 2 : Number of Listed Companies and Market Capitalization

Year	Number of Listed Companies	Amount of Capitalization (Rs. billion)
1995/96	9,100	5,723
1996/97	9,890	4,883
1997/98	9,833	5,898
1999[a]	9,877	5,741

[a] As of March

Source : Reserve Bank of India, Report on Curency and Finance, 1998-1999.

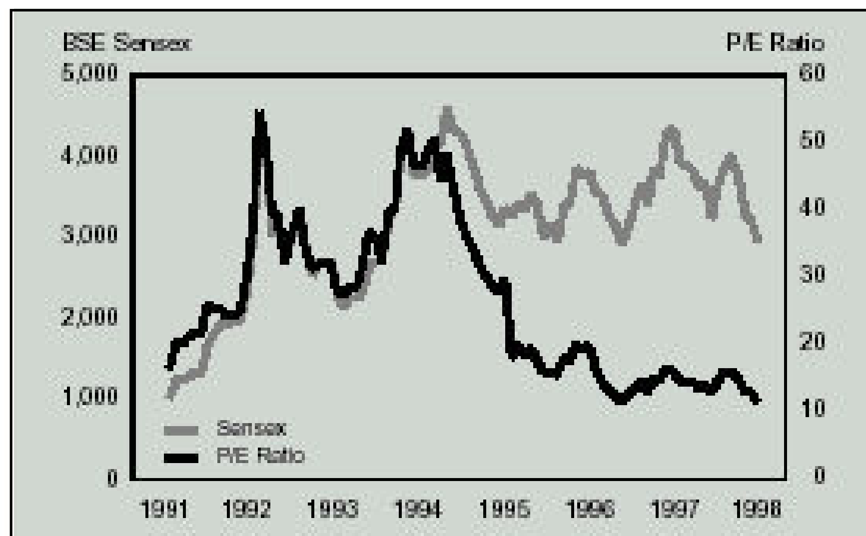
● ***Equity Price***

For the past 22 years, equity prices have seen two extended periods of declining prices and two periods of rising prices. Between April 1986 and March 1988, Sensex decreased from 589 to 398, or by 32 percent. Prices also fell between March 1992, when the monthly closing level of Sensex was 4,258, and April 1993, when the level was 2,122, a decline of 50.5 percent. Prices generally rose for extended periods from March 1988 to March 1992 and from May 1993 to August 1994. The monthly closing level of Sensex climbed from 398 in March 1988 to 4,285 in March 1992, an increase of more than 10 times. In the second period of extended rising equity prices, Sensex increased 1.16 times. Since 1995, it has fluctuated around the 3,000-4,000 mark (see Figure2.A- 1).

In April 1998, it hovered around 3,000. In the period of declining prices, from August 1994 to March 1998, the price-earnings (P/E) ratio fell more sharply than prices (Figure 1). In March 1998,the monthly average Sensex P/E ratio was 15.65 while the figure for October 1993 was 38.76.

Figure 2.A-1

Figure 1 : Price and P/E Ratio for the Sensitive Index of the Stock Exchange



Data from January 1991 to January 1995
Source : Bombay Stock Exchange.

- ***Risk Management System***

SEBI has taken several measures to improve the integrity of the secondary market. Legislative and regulatory changes have facilitated the corporatization of stockbrokers. Capital adequacy norms have been prescribed and are being enforced. A mark-to-market margin and intraday trading limit have also been imposed. Further, the stock exchanges have put in place circuit breakers, which are applied in times of excessive volatility. The disclosure of short sales and long purchases is now required at the end of the day to reduce price volatility and further enhance the integrity of the secondary market.

- ***Mark-To-Market Margin And Intraday Limit***

Under the current clearing and settlement system, if an Indian investor buys and subsequently sells the same number of shares of stock during a settlement period, or sells and subsequently buys, it is not necessary to take or deliver the shares. The difference between the selling and buying prices can be paid or received. In other words, the squaring-off of the trading position during the same settlement period results in non delivery of the shares that the investor traded. A short-term and speculative investment is thus possible at a relatively low cost. FIIs and domestic institutional investors are, however, not permitted to trade without delivery, since non delivery transactions are limited only to individual investors. One of SEBI's primary concerns is the risk of settlement chaos that may be caused by an increasing number of non delivery transactions as the stock market becomes excessively speculative. Accordingly, SEBI has introduced a daily mark-to-market margin and intraday trading limit. The daily mark-to market margin is a margin on a broker's daily position.

The intraday trading limit is the limit to a broker's intraday trading volume. Every broker is subject to these requirements. Each stock exchange may take any other measures to ensure the safety of the market. BSE and NSE impose on members a more stringent daily margin, including one based on concentration of business. A daily mark-to-market margin is 100 percent of the notional loss of the stockbroker for every stock, calculated as the difference between buying or selling price and the closing price of that stock at the end

of that day. However, there is a threshold limit of 25 percent of the base minimum capital plus additional capital kept with the stock exchange or Rs1 million, whichever is lower. Until the notional loss exceeds the threshold limit, the margin is not payable. This margin is payable by a stockbroker to the stock exchange in cash or as a bank guarantee from a scheduled commercial bank, on a net basis. It will be released on the pay-in day for the settlement period.

The margin money is held by the exchange for 6-12 days. This costs the broker about 0.4-1.2 percent of the notional loss, assuming that the broker's funding cost is about 24-36 percent (Endo 1998). Thus, speculative trading without the delivery of shares is no longer cost-free. Each broker's trading volume during a day is not allowed to exceed the intraday trading limit. This limit is 33.3 times the base minimum capital deposited with the exchange on a gross basis, i.e., purchase plus sale. In the event of brokers wishing to exceed this limit, they have to deposit additional capital with the exchange and this cannot be withdrawn for six months.

● ***Circuit Breaker***

SEBI has imposed price limits for stocks whose market prices are above Rs10 up to Rs20, a daily price change limit and weekly price change limit of 25 percent. BSE imposes price limits as a circuit breaker system to maintain the orderly trading of shares on the exchange (Table 2.2-3).

Table 2.2-3

Table 3 : Bombay Stock Exchange Price Limits

		Price Limit (Percent)	
Category	**Market Price of Share**	**Daily**	**Weekly**
A Group Shares	Over Rs 20	10	25
B1 & B2 Group Shares	Rs 10 up to Rs 20	25	25
	Rs 1 up to Rs 10	50	No Limit
	Up to Rs 1	75	No Limit

Source : Endo (1998)

BSE's computerized trading system rejects buy or sell orders of a stock at prices outside the price limits. The daily price limit of a stock is measured from the stock's closing price in the previous trading session. The weekly price limit is based on its closing price

of the last trading in the previous week, usually its closing price on the previous Friday.

- ***Short Sales And Long Purchases***

SEBI regulates short selling in the stock market by requiring all stock exchanges to enforce reporting by members of their net short sale and long purchase positions in each stock at the end of each trading day.

- ***Stock Lending***

A scheme for regulating stock lending was introduced in February 1997, following changes in tax regulations. Stock lending can take place through an intermediary registered for this purpose with SEBI, and which has a minimum capital of Rs500 million. Lenders and borrowers of securities have to enter into agreements with the intermediary. Stock lending facilitates the timely settlement of transactions on the stock exchanges, especially in an environment where physical delivery of certificates is required for settlement.

- ***Introduction of Derivatives Trading***

At present, there are two exchanges e.g. NSE & BSE where derivatives or over-the-counter derivative markets are there in the country. However, a new law has been passed permitting the trading of derivatives. This followed recommendations for the establishment of a regulatory framework for derivatives by a committee chaired by L.C. Gupta. It is expected that derivatives trading will soon form part of the entire Indian securities market.

Now let us do another simple exercise:

SAQ IV

State whether the following are true or false:

(1) Since 2001/02, the primary market has grown fast as a result of the removal of investment restrictions in the overall economy and a repeal of the restrictions imposed by the Capital Issues Control Act.

(2) SEBI has taken several measures to improve the integrity of the secondary market

(3) A mark-to-market margin and intraday trading limit have also been imposed by CCI

(4) The intra day trading limit is the limit to a broker's intraday buying volume.

(5) A scheme for regulating stock lending was introduced in February 1997.

Check your answer with the one provided at the end of the unit.

2.6 Let Us Sum Up

Indian Stock Markets are one of the oldest in Asia. Its history dates back to nearly 200 years ago. The earliest records of security dealings in India are meager and obscure. The East India Company was the dominant institution in those days and business in its loan securities used to be transacted towards the close of the eighteenth century.

Ahmedabad gained importance next to Bombay with respect to cotton textile industry. After 1880, many mills originated from Ahmedabad and rapidly forged ahead. As new mills were floated, the need for a Stock Exchange at Ahmedabad was realised and in 1894 the brokers formed "The Ahmedabad Share and Stock Brokers' Association".

During early sixties there were eight recognized stock exchanges in India. The number virtually remained unchanged, for nearly two decades. During eighties, however, many stock exchanges were established thus, at present, there are totally twenty one recognized stock exchanges in India excluding the Over the Counter Exchange of India Limited (OTCEI) and the National Stock Exchange of India Limited (NSEIL).

The SEBI is the nodal agency for dealing with FIIs, and they have to obtain initial registration with SEBI.

At present, there are two exchanges e.g. NSE & BSE where derivatives or over-the-counter derivative markets are there in the country. However, a new law has been passed permitting the trading of derivatives. This followed recommendations for the establishment of a regulatory framework for derivatives by a committee chaired by L.C. Gupta. It is expected that derivatives trading will soon form part of the entire Indian securities market.

2.7 Annexures & Appendix

Appendix 1

Reforms in Indian Securities Market Since 1992

The development in Indian securities market since 1992 can be summarized as follows:

● Capital Issues (Control) Act of 1947 repealed and the office of Controller of Capital Issues abolished control over price and premium of shares removed. Companies now free to raise funds from securities markets after filing prospectus with the Securities and Exchange Board of India (SEBI).

● The power to regulate stock exchanges delegated to SEBI by the Government.

● SEBI introduces regulations for primary and other secondary market intermediaries, bringing them within the regulatory framework.

● Reforms by SEBI in the primary market include improved disclosure standards, introduction of prudential norms, and simplification of issue procedures. Companies required to disclose all material facts and specific risk factors associated with their projects while making public issues.

● Listing agreements of stock exchanges amended to require listed companies to furnish annual statement to the exchanges showing variations between financial projections and projected utilization of funds in the offer document and actual figures. This is to enable shareholders to make comparisons between performance and promises.

● SEBI introduces a code of advertisement for public issues to ensure fair and truthful disclosures.

● Disclosure norms further strengthened by introducing cash flow statements.

● New issue procedures introduced-book building for institutional investors-aimed at reducing costs of issue.

● SEBI introduces regulations governing substantial acquisition of shares and takeovers and lays down conditions under which disclosures and mandatory public offers are to be made to the shareholders. Regulations further revised and strengthened in 1996.

● SEBI reconstitutes the governing boards of the stock exchanges and introduces capital adequacy norms for broker accounts.

● Private mutual funds permitted and several such funds already set up. All mutual funds allowed to apply for firm allotment in public issues-also aimed at reducing issue costs.

● Regulations for mutual funds revised in 1996, giving more flexibility to fund managers while increasing transparency, disclosure, and accountability.

● Over-the-Counter Exchange of India formed.

● National Stock Exchange (NSE) establishment as a stock exchange with nationwide electronic trading.

● Bombay Stock Exchange (BSE) introduces screen-based trading; 15 stock exchanges now have screened-based trading. BSE granted permission to expand its trading network to other centers.

● Capital adequacy requirement for brokers enforced.

● System of mark-to-market margins introduced in the stock exchanges.

● Stock lending scheme introduced.

● Transparency brought out in short selling.

● National Securities Clearing Corporation, Ltd. set up by NSE.

● BSE in the process of implementing a trade guarantee scheme.

● SEBI strengthens surveillance mechanisms and directs all stock exchanges to have separate surveillance departments.

● SEBI strengthens enforcement of its regulations. Begins the process of prosecuting companies for misstatements and ensures refunds of application money in several issues on account of misstatements in the prospectus.

● Indian companies permitted to access international capital markets through Euro issues.

● Foreign direct investment allowed in stockbroking, asset management companies, merchant banking, and other nonbank finance companies.

● Foreign institutional investors (FIIs) allowed access to Indian capital markets on registration with SEBI.

● FIIs also permitted to invest in unlisted securities and corporate and Government debt.

● The Depositories Act enacted to facilitate the electronic book entry transfer of securities through depositories.

● Guidelines for Offshore Venture Capital Funds announced. SEBI regulations for venture capital funds become effective.

Appendix 2
The Indian Securities Market Before 1992

The Indian securities market before 1992 had the following characteristics:

- Fragmented regulation; multiplicity of administration.
- Primary markets not in the mainstream of the financial system.
- Poor disclosure in prospectus. Prospectus and balance sheet not made available to investors.
- Investors faced problems of delays (refund, transfer, etc.)
- Stock exchanges regulated through the Securities Contracts (Regulations) Act. No inspection of stock exchanges undertaken.
- Stock Exchanges run as brokers clubs; management dominated by brokers.
- Merchant bankers and other intermediaries unregulated.
- No concept of capital adequacy.
- Mutual funds-virtually unregulated with potential for conflicts of interest in structure.
- Poor disclosures by mutual funds; net asset value (NAV) not published; no valuation norms.
- Private sector mutual funds not permitted.
- Takeovers regulated only through listing agreement between the stock exchange and the company.
- No prohibition of insider trading, or fraudulent and unfair trade practices.

Appendix 3
Regulatory Framework : Institutions

Securities and Exchange Board of India:

Securities and Exchange Board of India (SEBI) was set up as an administrative arrangement in 1988. In 1992, the SEBI Act was enacted, which gave statutory status to SEBI. It mandates SEBI to perform a dual function: investor protection through regulation of the securities market, and fostering the development of this market. SEBI has been delegated most of the functions and powers under the Securities Contract Regulation (SCR) Act, which brought stock

exchanges, their members, as well as contracts in securities which could be traded under the regulations of the Ministry of Finance (see Figure A3 for the present regulatory structure of the Indian securities market). It has also been delegated certain powers under the Companies Act. In addition to registering and regulating intermediaries, service providers, mutual funds, collective investment schemes, venture capital funds, and takeovers, SEBI is also vested with power to issue directives to any person(s) related to the securities market or to companies in areas of issue of capital, transfer of securities, and disclosures. It also has powers to inspect books and records, suspend registered entities, and cancel registration.

Reserve Bank of India

Reserve Bank of India (RBI) has regulatory involvement in the capital market, but this has been limited to debt management through primary dealers, foreign exchange control, and liquidity support to market participants. It is RBI and not SEBI that regulates primary dealers in the Government securities market. RBI instituted the primary dealership of Government securities in March 1998. Securities transactions that involve a foreign exchange transaction need the permission of RBI.

Department of Company Affairs

In 1947, the Capital Issues (Control) Act was enacted, which formalized and continued initial controls on the issue of securities that were introduced during World War II. This Act was administered by the office of the Controller of Capital Issues (CCI), which was a part of the Ministry of Finance. In line with economic reforms, it was repealed in 1992 to liberalize capital issuance and pricing. While capital issuance used to be regulated by the office of the CCI, both private and public companies were governed by the Companies Act of 1956, which was and continues to be administered by the Department of Company Affairs (DCA) under the Ministry of Law, Justice and Company Affairs. Besides governing the incorporation, management, mergers, and winding up of companies, this Act also specifies certain aspects concerning capital issuance and securities trading, particularly the issue of prospectus for public offers, contents of the prospectus, completion of allotment, issue, and trading of securities, and transfer and registration of securities.

Stock Exchanges

SEBI issued directives that require that half the members of the governing boards of the stock exchanges be non broker public representatives and include a SEBI nominee. To avoid conflicts of interest, stock brokers are a minority in the committees of stock exchanges set up to handle matters of discipline, default, and investor-broker disputes. The exchanges are required to appoint a professional, nonmember executive director who is accountable to SEBI for the implementation of its directives on the regulation of stock exchanges. SEBI has introduced a mechanism to remedy investor grievances against brokers.

Disclosure

Similar to companies in capital markets in other countries, a company offering securities in the Indian capital market is required to make a public disclosure of all relevant information through its offer documents.

These documents are as follows:

- prospectus,
- application form and the abridged prospectus (in case of an issue to the public), or
- letter of offer (in case of a rights issue to existing shareholders or debenture holders of a company with or without the right to renounce in favour of other persons). After a security is issued to the public and subsequently listed on a stock exchange, the issuing company is required under the listing agreement to continue to disclose in a timely manner to the exchange, to the holders of the listed securities (the shareholders or the bondholders), and to the public (through the exchange or the media), any information necessary to enable the holders of the listed securities to appraise its position and to avoid the establishment of a false market in such listed securities. Such information include:

- the date of the meeting of the board of directors for corporate actions;
- the audited financial results on an annual basis and the unaudited ones on a semiannual basis;
- any proposed change in the general character or nature of the company's business;
- any alterations of the company's capital; and
- any change of the company's directorate, including managing directors and auditors.

2.8 Key Words

Stock Exchange is a place where stocks and shares are purchased and sold.

Brokers are persons who buy or sell shares for clients on commission basis.

Foreign Direct Investments is concerned with the operation and ownership of host-country firms.

2.9 Probable Answers :

SAQI :	(i) 200	(ii) 1865	(iii) Calcutta
	(iv) First		
SAQII:	(i) True	(ii)False	(iii)False
	(iv) True	(v) True	
SAQIII:	(i) False	(ii)False	(iii)False
	(iv) False		
SAQIV:	(i) false	(ii) True	(iii) False
	(iv) True	(v) True	

2.10 Reflective Questions:

- Discuss the evolution of Indian capital market
- Analyze the importance of Indian stock exchange in capital market growth.
- Establish the problems of institutional investors.
- Write a seminar paper on the Indian Capital Market.
- Discuss the role of FDIs in Indian Capital Market.
- Do you think that SEBI is more effective then CCI in regulating the Indian Secondary Market? Give justifications.

1.11 Suggested Readings for Unit 2:

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.) (Chapter 9, 10 &11)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004) (Chapter 8)
- Dewett K.K., Verma J.D. & Sharma M.L., Indian Economics, S.Chand & Company Ltd., New Delhi (Chapter 27,28 & 49)
- Chidambaram K; Alagappan ; Business Environment, Vikas Publishing house pvt. Ltd. (chapter 5,7&12)

UNIT 3
DIRECTION OF INDIA'S FOREIGN TRADE

Structure

3.0 Objectives
3.1 Introduction
3.2 Trends in India's Foreign Trade
3.2.1 Trend in India's Export
3.2.2 Trend in India's Import
3.3 India's Foreign Trade: Recent trends
3.4 Foreign Exchange Management Act
3.4.1 Regulation and Management of Foreign Exchange
3.5 Let us sum up

3.0 Objectives

After going through this unit you will be able to:

- Define Foreign Exchange
- Discuss the trends of India's foreign trade
- Analyze the export -import matrix in India
- Establish the problems of Indian foreign trade.
- Argue on the relevance of FEMA.

3.1 Introduction

The importance of capital market in an economy has opened up many discussions on the importance of foreign trade and the balance of payment often depends upon the trends of foreign trade in a country. In this unit the export-import matrix in India has been discussed in length along with the conceptual analysis of foreign exchange management act.

3.2 Trends In India's Foreign Trade

After witnessing an impressive growth during the year 2002-03, export growth continued to maintain momentum during the year 2003 04. According to provisional data available for April-March 2003-04,

exports stood at Rs.283605 crores (US $ 61845 million) as against Rs. 255137 crores (US $ 52742 million) in the corresponding period of last year, recording a growth of 11.16% in Rupee terms and 17.26 % in Dollar terms . Imports also witnessed a robust growth of 19.01%, having increased to Rs. 346474 crores (US $ 75209 million) from Rs. 291133 crores (US $ 60189 million)during April to March, 2003-04. The trade deficit during April-March 2003-04 is estimated to have widened to Rs.62870 crores ($ 13364 million) from Rs. 35996 crores ($ 7447million)during the corresponding period of the previous year. The aggregate foreign trade data in Rupee terms and Dollar terms for the period April to March, 2002-03 as well as April to March 2003-04 are given in Table 3.1(a) and 3.1(b) respectively.

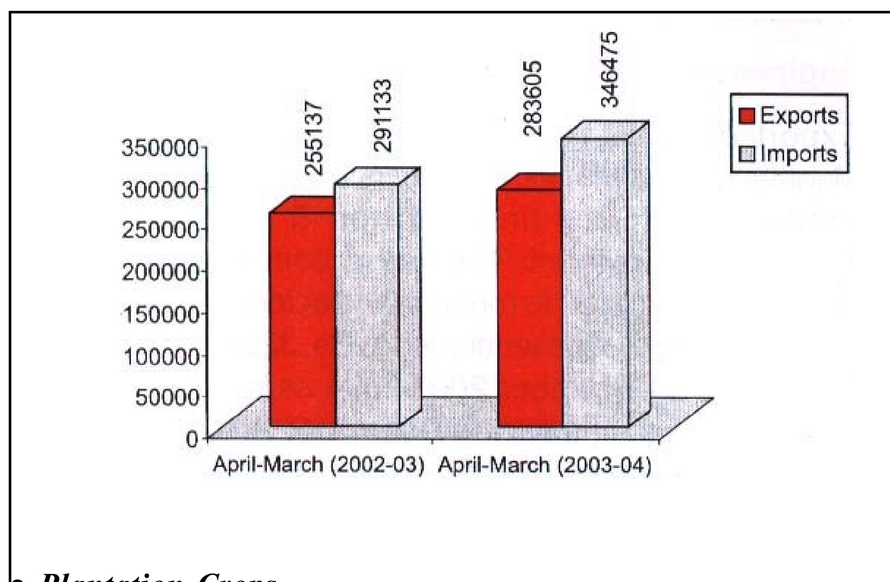
3.2.1 Trends In Exports

The details regarding India's export of principal products/groups during, 2001-02 ,2002-03 and April to December, 2002-2003 and April to December, 2003-2004 are given in Table 3.2 -II.

During April - December, 2003-2004, commodities/commodity groups registering significant increase in exports over the corresponding period of the previous year included Tea, Coffee, Wheat, Seasame & Niger Seeds Groundnuts, Oilmeals, Guargum Meals, Shellac, Floriculture Products, Processed Foods, Mica, Coal, Gems & Jewellery, Sports Goods, Chemicals & Allied Products (except Residual Chemicals), Engineering Goods, Electronic Goods, Manmade Textiles, Made Ups etc., Jute Manufactures, Hand Made Carpets (excluding Silk), Cotton Raw including waste and Petroleum Products. Major commodities registering a decline in exports were Rice, Tobacco, Spices, Nuts & Seeds, Marine Products, Iron Ore, processed Minerals, Residual Chemicals and Allied Products, Project Goods, Readymade Garments, Cotton Yarn Fabrics Made ups, etc., Wool & Woolen Manufactures, Coir, Handicrafts and Carpets.

The export performance of some principal commodity groups during the period April to December, 2003-2004 are given below :

Fig 3.A :Details of India's Foreign Trade



● ***Plantation Crops***

Export of Plantation Crops increased by 6.7% in Rupee terms during the first 9 months of 2003-2004 compared with the corresponding period of the previous year. The increase in the export of Plantation Crops was mainly due to reasonably good performance of Tea and Coffee. Export of Tea increased by 6.7% from Rs. 1137 crores during the first 9 months of last year to Rs. 1211 crores during the same period in the current year. Exports of Coffee also increased from Rs. 710 crores last year to Rs. 761 crores this year registering a growth of 7.2%.

● ***Agriculture and Allied Products***

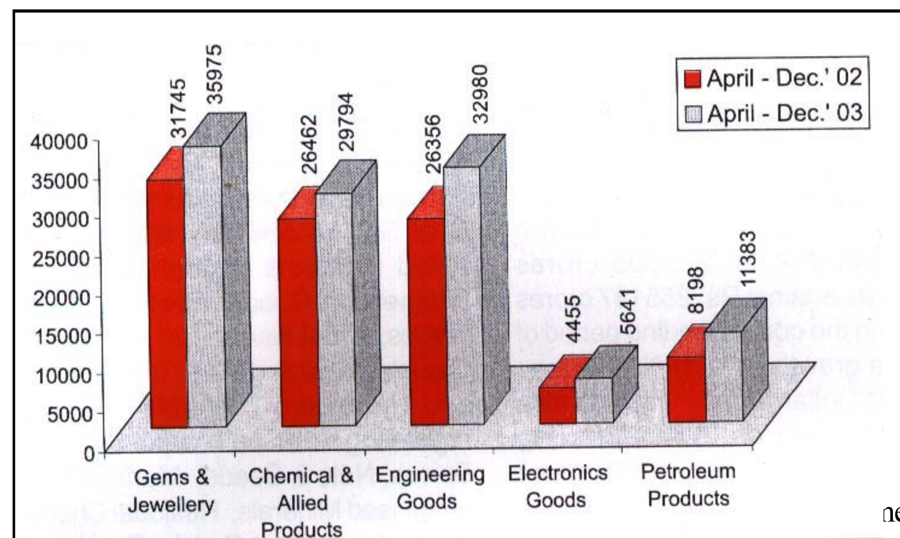
Agriculture and Allied Products comprises a wide variety of agricultural products covering Cereals, Pulses, Tobacco, Spices, Nuts and Seeds, Oil Meals, Guargum Meals, Castor Oil, Shellac, Sugar and Molasses, Processed Food, Meat and Meat Products, etc. During April to December 2003-2004, the exports of this group recorded a decline of 4.5% from Rs. 16435 crores in the previous year to Rs. 15691 crores during the current year. Cereals (except Rice) Groundnuts, Guargum Meals, Shellac, Processed Food & Spirit & Beverages registered growth

in exports.

● ***Marine products***

The exports of Marine Products stood at Rs. 4785 crores during April to December, 2003-2004 , recording a decline of 11.7% over Rs. 4785 crores during April- December, 2002-2003 . The USA, EU and Japan continued to be the major destination of marine exports from India.

Fig 3.B: India's Exports of Principal Commodities (Value in Rs. Crore)



ne

Ore, Aluminum, Mica and Coal are included in this product group. Exports of Ores and Minerals were estimated at Rs.6644 crores during this period recording a decline of 7.2% over the same period of last year. While exports of Mica, Other Ores & Minerals and Coal recorded a growth of 77.4%, 6.7% and 9.6% respectively, Iron Ore and Processed Minerals dipped by 16.8% and 7.5% respectively.

● ***Leather and Leather Manufactures***

Exports of Leather and Leather Manufactures registered a fall of 2.2% from Rs.6808 crores during April to December, 2002-2003 to Rs. 6661 crores during April to December, 2003-2004. Exports of Leather

Footwear increased by 0.7% during April to December, 2003-2004 as compared to the corresponding period of the previous year. Exports of Leather and Manufactures also declined by 3.4% during the same period.

- ***Gems and Jewellery***

The export of Gems and Jewellery during April to December, 2003-2004 stood at Rs. 35975 crores as compared to Rs.31745 crores during the corresponding period of last year, showing a modest growth of 13.3%.

- ***Chemicals and Allied Products***

Exports of Chemicals and Allied Products registered a growth of 12.6% during April to December, 2003-2004 over the same period of the previous year in Rupee terms. Three out of the four sub-groups under this head viz. Basic Chemicals, Pharmaceuticals & Cosmetics, Plastics & Linoleum, Rubber, Glass & Other Products have registered positive growth during April to December, 2003-2004 as compared to the corresponding period of previous year. However, Residual Chemicals and Allied Products showed a negative export growth of 8.0%.

- ***Engineering Goods***

Export of items under this group comprising Manufactures of Metals, Machinery and Instruments, Primary and Semi-finished Iron & Steel and Transport Equipment, showed a commendable growth as compared to most of the sectors. Exports of Engineering Goods amounted to Rs. 32980 crores during April to December, 2003-2004 as against Rs. 26356 crores during April to December, 2002-2003 showing an impressive growth of 25.1%.

- ***Electronic Goods***

Exports of Electronic Goods during the first 9 months of the current year were estimated at Rs. 5641 crores as compared to Rs.4455 crores during April to December, 2002-2003, thus recording a growth of 26.6%.

- ***Textiles and Handicrafts***

The total value of Indian textiles exports during April to December, 2003-2004 went down to Rs. 36752 crores from Rs.39097 crores during

the corresponding period of previous year showing a decline of 6%. Jute Manufactures (17.2%), Natural Silk Textiles (6.3%), Man-made Textiles, Made ups, etc., (16.5%) and Wool and Woollen Manufactures (6.0%) recorded a positive growth. Other sub-groups viz. Readymade Garments (7.3%), Cotton Yarn, Fabrics, Made ups, etc., (15.4%), and Coir & Coir Manufactures (8.9%) showed negative trends.

The main items of exports of Handicrafts are various types of works of art, such as Metal Artware, Textiles (hand printed), Woodwares and Zari goods. Exports of Handicrafts dipped to Rs. 1367 crores during April to December, 2003-2004 from Rs.2504 crores during the corresponding period of the last year registering a fall of 51.3%. Export of Carpets decreased during April to December, 2003-2004 to Rs. 1870 crores from Rs. 1933 crores during April to December, 2002-2003 registering a decline of 3.3%.

3.2.2 Trends In India's Imports

The trends in India's imports for the entire year 2002- 2003 and from April to December 2003-2004 as compared with the corresponding period of the previous year are reflected in Table-III.

Import of items under bulk category as a whole comprising inter-alia Fertilizers, Cereals, Sugar, Edible Oil, Iron and Steel and Petroleum Crude and Products recorded a substantial increase during April to December, 2003-2004 compared with the corresponding period of the previous year. It is notable that the commodity group recording the highest growth in imports was Machinery.

As far as import of individual items is concerned, significant growth was registered by Paper Board and Manufactures (47.59%) followed by Iron & Steel (43.76%), Crude Rubber including Synthetic (43.31%), Edible Oil (36.71%), Non-ferrous Metals (33.07%), News Print (29.72%), Fertilizer (15.60%) Pulp & Paper Waste (13.76%), Metalliferrous Ore & Scrap (11.66%) and Petroleum Crude and Products (4.44%).

Import of some items during this period registered a fall. These included Crude Fertilizer (25.55%). Import of Rice & Wheat came down to nil during the period under review.

- **Import by major product categories**

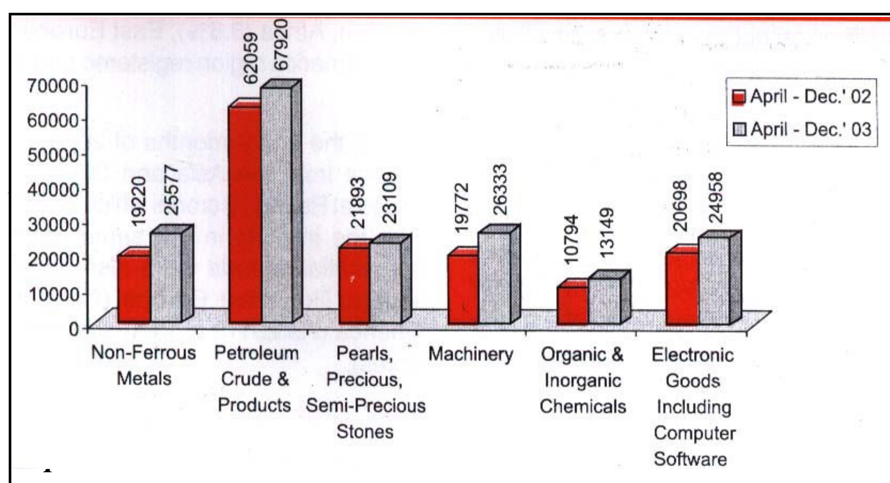
Fertilizers

During the first 9 months of 2003-2004 the total import of Fertilizers increased to Rs. 2742 crores from Rs. 2372 crores in the corresponding period of last year recording an increase of 15.60%. However import of Crude Fertilizer decreased by 25.55%.

Petroleum Crude & Products

The import of Petroleum Crude & Products was valued at Rs. 67920 crores during April-December 2003-2004 as against Rs. 62059 crores during April to December , 2002-2003 showing a growth of 9.44%.

Fig: 3.C: India's Impotrs Of Principal Commodities
(Value in Rs. Crore)



Import of Capital Goods, largely represented by machinery, including Transport Equipment as well as Project Goods recorded a notable increase during April to December, 2003-2004 over the same period of last year. Machine Tools segment saw a significant rise of 64.03%

in imports. Import of Project Goods, however, decreased from Rs. 1807 crores in April to December , 2002-2003 to Rs. 1221 crores in April to December, 2003-2004 registering a fall of 32.43%. Other items that showed positive import growth were Transport Equipments (62.06%) Non-Electrical Machinery (24.17%) , Electric Machinery (19.34%), and Professional Instruments (1.56%).

Chemicals and Chemical Materials

Organic and Inorganic Chemical Materials and Medicinal and Pharmaceuticals Products constituted the major components of imports under this category. The imports of organic and inorganic chemicals increased to Rs. 13149 crores during April to December , 2003-2004 from Rs. 10794 crores during April to December, 2002-2003, registering a growth of 21.82%. Import of medicinal and pharmaceutical products marginally declined to Rs. 2073 crores during April to December, 2003-2004 from Rs.2087 crores during the corresponding period of last year registering a fall of 0.67%.

Now let us do a simple exercise:

SAQ I

Fill up the blanks:

(1) Export of Plantation Crops increased by 6.7% in Rupee terms during the first 9 months of---------- compared with the corresponding period of the previous year.

(2) During April to December 2003-2004, the exports of ------- group recorded a decline of 4.5% from Rs. 16435 crores in the previous year to Rs. 15691 crores during the current year.

(3) The ------, EU and Japan continued to be the major destination of marine exports from India.

(4) It is notable that the commodity group recording the highest growth in imports was ----------.

(5) Organic and Inorganic Chemical Materials and Medicinal and Pharmaceuticals Products constituted the major components of imports under--------- industry.

Check your answer with the one provided at the end of the unit.

3.3 India's Foreign Trade: Recent Trends

The value of India's exports to and import from major regions/countries are given in Appendix V and Appendix VI respectively. During the first 9 months of the current fiscal, Asia and Oceania region comprising South Asian, East Asian, Mid-eastern and Gulf countries accounted for nearly 45.72% of India's total exports. Share of West Europe and America in our exports stood at 23.7% and 21.9% respectively. In fact the share of Asia and Oceania in India's exports during April-Dec 2003-04 has increased compared to the share last year, as also the shares of regions like Africa, EU and East Europe. On the contrary shares of North America, South America and Caribbean countries in India's total export showed a decline during this period.

As far as individual countries are concerned, USA, with a share of 18.75% of our exports, remained the most important export destination during April-Dec 2003-04, followed by United Arab Emirates (7.46%), Hong Kong (5.43%), UK (4.81%) and Germany (3.92%).

In the case of import also, share of Asia and Oceania in India's total import was highest at 33.65% during April-Dec 2003-04, followed by West Europe (23.82%) and America (9.03%). Coming to individual countries, the share of USA in our imports stood at 6.57% followed by Belgium (4.23%), UK (4.03%) and Germany (3.83%).

The trends in India's export to and import from different regions are given in Table IV and V respectively. During April to December, 2003-2004 Asia Oceania accounted for the highest growth in India's export at 16.4% over the corresponding period of the previous year followed by West Europe (10.7%), Africa (8.8%), East Europe (7.2%). The entire America region registered negative growth of 4.5%.

During the first 9 months of 2003-2004, India's imports from the Asia and Oceania region was valued at Rs.86158 crores which was 37.68% higher over the imports in the same period last year. Substantial imports were also accounted for by regions like West Europe (Rs. 60978 crores), America (Rs.23112 crores) and Africa (Rs.11627 crores).

- ***Import of sensitive items***

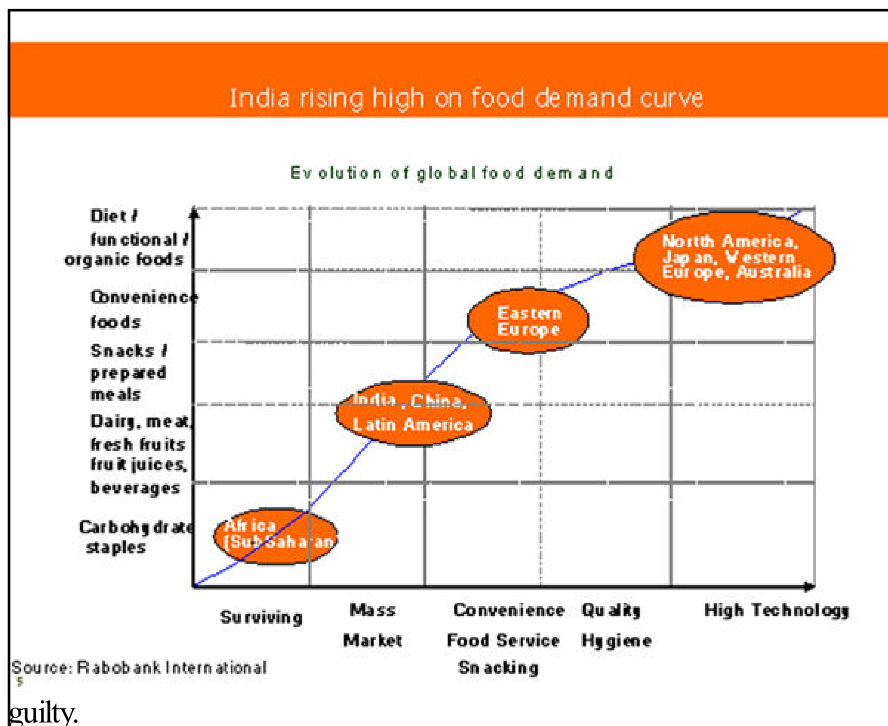
The total of 300 sensitive tariff lines for the period April-December 2003 has been Rs 13,541 crore as compared to Rs 10,329 crore during the corresponding period of last year thereby showing a growth of 31%. The gross import of all commodities during same period of current year was Rs 2,55,397 crore as compared to Rs 2,14,262 crore during the same period of last year. Thus import of 300 sensitive items constitute only 4.8% and 5.3% of the gross imports during last year and current year respectively. The major item that has contributed significantly to the growth is Crude Palm Oil and its fractions.

Import of Spices and Tea & Coffee have shown a decline at broad group level during the period. Import of Edible Oil, Cotton & Silk, Fruits & Vegetables, Automobiles, Rubber, Milk & Milk Products, Alcholic Beverages, SSI and other products have shown increase during the period under reference.

In the Edible Oil sector, the import has increased from Rs 6,459 crores last year to Rs 8,954 crores for the corresponding period of this year. However, significant feature of Edible Oil import is that although import of Crude Oil have gone up by 30%, that of Refined Palm Oil & Palmolein have increased by 89% but percentage share of crude to the total edible oil remains as high as 80% indicating a better utilization of the processing capacity in the country. Imports of Soya Bean Crude Oil, Kernail / Babasu Crude Oil and Sunflower Crude Oil have also gone up marginally.

Imports of sensitive items from Indonesia, Malaysia, Argentina, USA, Egypt, Thailand, Mali, Greece, Guinea Bisu, Cote D' Ivoire, Benin & Korea RP etc. have gone up while those from Czech Republic, Sri Lanka, Switzerland & Australia etc. have shown some decrease.

Fig. 3.D : Food Demand Curve (India)



guilty.

With liberalization, a need was felt to remove the drastic measures of FERA and replace them by a set of liberal foreign exchange management regulations. Therefore FEMA was enacted to replace FERA.

FEMA extends to the whole of India. It applies to all branches, offices and agencies outside India owned or controlled by a person resident in India and also to any contravention there under committed outside India by any person to whom this Act applies.

FEMA contains definitions of certain terms which have been used throughout the Act. The meaning of these terms may differ under other laws or under common language. But for the purposes of FEMA, the terms will signify the meaning as defined there under. Let us take up some of the more important ones.

"Authorized person" means an authorized dealer, money changer, off-

shore banking unit or any other person for the time being authorized to deal in foreign exchange or foreign securities;

"Capital Account Transaction" means a transaction which alters the assets or liabilities, including contingent liabilities, outside India of persons resident in India or assets or liabilities in India of persons resident outside India, and includes transactions by way of giving guarantees or surety for any debt, obligation or other liability of (1) a person resident outside India or (2) of a person resident in India and owed to a person resident outside India.

"Currency" includes all currency notes, postal notes, postal orders, money orders, cheques, drafts, travelers cheques, letters of credit, bills of exchange and promissory notes, credit cards or such other similar instruments, as may be notified by the Reserve Bank;

"Currency Notes" means and includes cash in the form of coins and bank notes;

"Current Account Transaction" means a transaction other than a capital account transaction and includes :-

(i) payments due in connection with foreign trade, other current business, services, and short-term banking and credit facilities in the ordinary course of business,

(ii) payments due as interest on loans and as net income from investments,

(iii) remittances for living expenses of parents, spouse and children residing abroad,

(iv) expenses in connection with foreign travel, education and medical care of parents, spouse and children;

"Export", with its grammatical variations and cognate expressions, means :-

(i) the taking out of India to a place outside India any goods,

(ii) provision of services from India to any person outside India;

"Foreign currency" means any currency other than Indian currency;

"Foreign Exchange" means foreign currency and includes :-

(i) deposits, credits and balances payable in any foreign currency,

(ii) drafts, travelers cheques, letters of credit or bills of

exchange, expressed or drawn in Indian currency but payable in any foreign currency,

(iii) drafts, travelers cheques, letters of credit or bills of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency;

"Foreign Security" means any security, in the form of shares, stocks, bonds, debentures or any other instrument denominated or expressed in foreign currency and includes securities expressed in foreign currency, but where redemption or any form of return such as interest or dividends is payable in Indian currency;

"Import", with its grammatical variations and cognate expressions, means bringing into India any goods or services;

"Indian currency" means currency which is expressed or drawn in Indian .rupees but does not include special bank notes and special one rupee notes issued under section 28A of the Reserve Bank of India Act, 1934 by the Ministry of Finance.

"Person" includes an individual, a Hindu undivided family, a company, a firm, an association of persons or a body of individuals, whether incorporated or not, every artificial juridical person and any agency, office or branch owned or controlled by such person;

"Person resident in India" means :-

(i) a person residing in India for more than one hundred and eighty-two days during the course of the preceding Financial year but does not include :-

(a) a person who has gone out of India or who stays outside India,

(i) for or on taking up employment outside India, or

(ii) for carrying on outside India a business or vocation outside India, or

(iii) for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period;

(a) a person who has come to or stays in India, otherwise than

(i) for or on taking up employment in India, or

(ii) for carrying on in India a business or vocation in

India, or

(iii) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period;

(i) any person or body corporate registered or incorporated in India,

(ii) an office, branch or agency in India owned or controlled by a person resident outside India,

(iii) an office, branch or agency outside India owned or controlled by a person resident in India.

"Repatriate to India" means bringing into India the realized foreign exchange and

(i) the selling of such foreign exchange to an authorized person in India in exchange for rupees, or

(ii) the holding of realized amount in an account with an authorized person in India to the extent notified by the Reserve Bank, and includes use of the realized amount for discharge of a debt or liability denominated in foreign exchange and the expression "repatriation" shall be construed accordingly:

"Security" means shares, stocks, bonds and debentures, Government securities, savings certificates, deposit receipts in respect of deposits of securities and units of the Unit Trust of India or of any mutual fund and includes certificates of title to securities, but does not include bills of exchange or promissory notes other than Government promissory notes or any other instruments which may be notified by the Reserve Bank as security for the purposes of this Act;

"Service" means service of any description which is made available to potential users and includes the provision of facilities in connection with banking, financing, insurance, medical assistance, legal assistance, chit fund, real estate, transport, processing, supply of electrical or other energy, boarding or lodging or both, entertainment, amusement or the purveying of news or other information, but does not include the rendering of any service free of charge or under a contract of personal service;

"Transfer" includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien.

3.4.1 Regulation and management of foreign exchange

Except with the general or special permission of the Reserve Bank, no person can :-

(a) deal in or transfer any foreign exchange or foreign security to any person not being an authorized person;

(b) make any payment to or for the credit of any person resident outside India in any manner;

(c) receive otherwise through an authorized person, any payment by order or on behalf of any person resident outside India in any manner;

(d) Where any person in, or resident in India receives any payment by order or on behalf of any person resident outside India through any other person (including an authorized person) without a corresponding inward remittance from any place outside India, then, such person shall be deemed to have received such payment otherwise than through an authorized

(e) enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person

Financial transaction means making any payment to, or for the credit of any person, or receiving any payment for, by order or on behalf of any person, or drawing, issuing or negotiating any bill of exchange or promissory note, or transferring any security or acknowledging any debt.

No person resident in India can acquire, hold, own, possess or transfer any foreign exchange, foreign security or any immovable property situated outside India except with the general or special permission of the Reserve Bank.

Any person may sell or draw foreign exchange to or from an authorized person if such sale or drawal is a current account transaction. However, the Central Government may, in public interest and in consultation with the Reserve Bank, impose such reasonable restrictions for current account transactions as may be prescribed.

Any person may sell or draw foreign exchange to or from an authorized person for a capital account transaction. The Reserve Bank may, in consultation with the Central Government, specify :-

(a) any class or classes of capital account transactions which

are permissible;

(b) the limit up to which foreign exchange shall be admissible for such transactions:

However, the Reserve Bank cannot impose any restriction on the drawal of foreign exchange for payments due on account of amortization of loans or for depreciation of direct investments in the ordinary course of business.

The Reserve Bank can, by regulations, prohibit, restrict or regulate the following :-

(a) transfer or issue of any foreign security by a person resident in India;

(b) transfer or issue of any security by a person resident outside India;

(c) transfer or issue of any security or foreign security by any branch, office or agency in India of a person resident outside India;

(d) any borrowing or lending in foreign exchange in whatever form or by whatever name called;

(e) any borrowing or tending in rupees in whatever form or by whatever name called between a person resident in India and a person resident outside India;

(f) deposits between persons resident in India and persons resident outside India;

(g) export, import or holding of currency or currency notes;

(h) transfer of immovable property outside India, other than a lease not exceeding five years, by a person resident in India;

(i) acquisition or transfer of immovable property in India, other than a lease not exceeding five years, by a person resident outside India;

(j) giving of a guarantee or surety in respect of any debt, obligation or other liability incurred (i) by a person resident in India and owed to a person resident outside India or (ii) by a person resident outside India.

A person resident in India may hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated

outside India if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India.

A person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India.

The Reserve Bank may, by regulation, prohibit, restrict, or regulate establishment in India of a branch, office or other place of business by a person resident outside India, for carrying on any activity relating to such branch, office or other place of business.

Every exporter of goods must

(a) furnish to the Reserve Bank or to such other authority a declaration in such form and in such manner as may be specified, containing true and correct material particulars, including the amount representing the full export value or, if the full export value of the goods is not ascertainable at the time of export, the value which the exporter, having regard to the prevailing market conditions, expects to receive on the sale of the goods in a market outside India;

(b) furnish to the Reserve Bank such other information as may be required by the Reserve Bank for the purpose of ensuring the realization of the export proceeds by such exporter.

The Reserve Bank may, for the purpose of ensuring that the full export value of the goods or such reduced value of the goods as the Reserve Bank determines, having regard to the prevailing market-conditions, is received without any delay, direct any exporter to comply with such requirements as it deems fit.

Every exporter of services shall furnish to the Reserve Bank or to such other authorities a declaration in such form and in such manner as may be specified, containing the true and correct material particulars in relation to payment for such services.

Where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realize and repatriate to India such foreign exchange within such period and in such manner as may be specified by the Reserve Bank.

Now let us do another simple exercise:

SAQ II

State whether the following are true or false:

(1) The total of 300 sensitive tariff lines for the period April-December 2003 has been Rs 13,541 crore as compared to Rs 10,329 crore during the corresponding period of last year thereby showing a ©growth of 41%

(2) Import of Spices and Tea & Coffee have shown a decline at broad group level during the period 2003-04.

(3) The Foreign Exchange Management Act (FEMA) is a law to replace the draconian Foreign Exchange Regulation Act, 1973.

(4) "Currency Notes" means and includes cash in the form of coins and bank notes.

(5) "Import", with its grammatical variations and cognate expressions, means sending from India any goods or services

Check your answer with the one provided at the end of the unit.

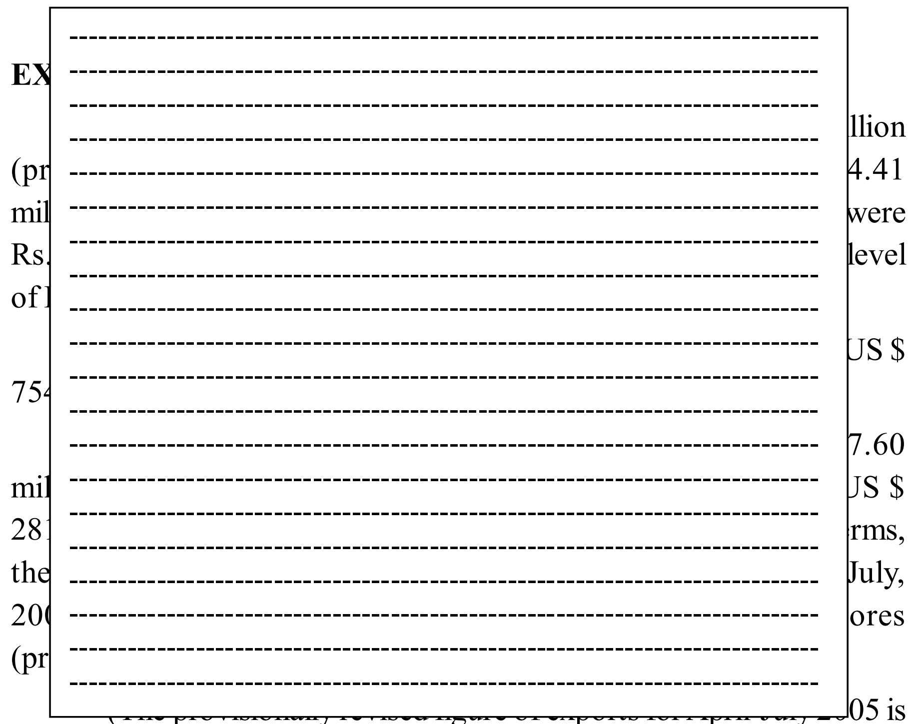
3.5 Let Us Sum Up

Well well; its your time once again to sum up the entire unit. Please use the following space to do it (within 150 words)

3.6 Appendix

Appendix I:

INDIA'S FOREIGN TRADE: APRIL-JULY 2006-2007



05 is US $ 31223.01 million/ Rs. 1368.91 crores).

IMPORTS

Imports during July, 2006 are valued at US $ 14143.06 million (provisional) representing an increase of 42.8% over the level of imports valued at US $ 9904.22 (provisional) million in July, 2005. In Rupee terms, the imports were Rs. 65703.27 crores (provisional) which is 52.38% higher than the level of Rs. 43119.09 crores (provisional) during July 2005.

(The provisionally revised figure of imports for July 2005 is US $ 11384.61 million/Rs. 49564.17 crores).

Total imports during April-July, 2006 are valued at US $ 54424.34 million (provisional) which is 29.24% higher than the level of US $ 42109.47 million (provisional) during April-July 2005. In rupee terms, the imports were Rs. 248925.88 crores (provisional) which is 35.6% higher than the level of Rs. 183537.52 crores (provisional) during April-July 2005.

(The provisionally revised figure of imports for April-July 2005 is US $ 45598.75 million/ Rs. 198735.76 crores).

Oil imports during July 2006 are valued at US $ 4642.31 million which is 32.83% higher than oil imports valued at US 3494.80 million in the corresponding period last year. Oil imports during April-July 2006 are valued at US $ 18533.53 million which is 43.23% higher than oil imports valued at US $ 12940.14 million in the corresponding period last year. Non-oil imports during July 2006 are estimated at US $ 9500.75 million which is 20.42% higher than the level of such imports valued at US $ 7889.81 million in July 2005. Non-oil imports during April-July, 2006 are estimated at US $ 35890.81 million which is 9.90% higher than the level of such imports valued at US $ 32658.61 million in April-July 2005.

TRADE BALANCE

The trade deficit for April-July, 2006 is estimated at US $ 16716.74 million (provisional) which is higher than the deficit of US $ 13974.75 million (provisional) during April-July, 2005.

3.7 Annexures

Annexure I :

	(Ratio of Refined to total edible import)					***14.6%***	***19.9%***	
8	Alcoholic Beverages	11	0.17%	0.31%	17.58	41.91	24.33	138.4%
9	Rubber	11	0.47%	1.15%	48.62	155.73	107.11	220.3%
	(Natural rubber smoked sheets, technically specifiednatural rubber,natural rubber non latexcontribution is)				***35.98***	***138.44***	***102.46***	***284.8%***
	(and their %age share to this group)				***74.0%***	***88.9%***		
10	Cotton & Silk	20	15.05%	14.72%	1554.90	1993.62	438.73	28.2%
	Significant growth in : Mulberry dupion silk and its other yarn, Yarn of mulberry silk waste, cotton (Foreign and Bengal Deshi) and their contribution is)				***1065.35***	***1586.15***	***520.80***	***48.9%***
	(and their %age share to this group)				***68.5%***	***79.6%***		
	Siginificant Shortfall in :raw silk (Mulberry and others), NOIL silk yarn and their contribution is)				***485.25***	***401.50***	***-83.75***	***-17.3%***
	(and their %age share to this group)				***31.2%***	***20.1%***		
11	Marble & Granite	9	0.41%	0.43%	42.82	58.83	16.01	37.4%
12	Automobiles	33	2.50%	2.03%	257.76	274.92	17.16	6.7%
13	Product of SSI	37	1.50%	1.58%	155.16	213.73	58.57	37.7%
	(Umbrella, locks, toys, writing instruments, tiles, glassware, etc.)							
	(Major increase are in :Glassware of lead crystel and other drinking glasses etc., combination & pad locks and other locks, Ball point & other in pen, toy weapons, all types of tiles and their contribution is)				***93.49***	***159.28***	***65.79***	***70.4%***
	(and their %age share to this group)				***60.3%***	***74.5%***		
14	Others (Wheat floor, sugar, cigarette & salt)	12	0.18%	0.42%	18.41	57.03	38.62	209.8%
	Total of Sensitive items		100.0%	100.0%	**10329.27**	**13540.60**	**3211.33**	31.1%
	%age share of Import of sensitive items to				**4.8%**	**5.3%**		
	Total Import (All Commodities) Total of All commodities (including sensitive items) as per quick estimate				**214262.2**	**255396.6**	**41134.3**	19.2%

Annexure II :

TABLE - II

EXPORT OF PRINCIPAL COMMODITIES

(Rs. in Crores)

SL.NO.	COMMODITIES	2001-2002	2002-2003	%Change	Apr-Dec'02	Apr-Dec'03	%Change
1	2	3	4	5	6	7	8
I	**PLANTATIONS**	**2814**	**2646**	**-6.0**	**1849**	**1972**	**6.7**
	1. Tea	1719	1652	-3.9	1139	1211	6.3
	2. Coffee	1095	994	-9.2	710	761	7.2
II	**AGRI & ALLIED PRODUCTS**	**18969**	**22391**	**18.0**	**16435**	**15691**	**-4.5**
	1. Cereal	4620	7682	66.3	5928	4528	-23.6
	a. Rice	3174	5831	83.7	4524	2813	-37.8
	b Wheat	1330	1760	32.3	1333	1591	19.4
	c. Others	116	91	-21.6	71	124	74.6
	1.(a) Pulses	369	345	-6.5	279	238	-14.7
	2. Tobacco	808	1022	26.5	738	736	-0.3
	a) Unmanufactured	582	733	25.9	528	540	2.3
	b) Manufacyured	226	289	27.9	210	196	-6.7
	3. Spices	1497	1655	10.6	1256	1119	-10.9
	4. Nuts and Seeds	2655	2692	1.4	2036	2005	-1.5
	a) Cashew incl. CNSL	1794	2062	14.9	1638	1211	-26.1
	b) Sesame & niger Seed	610	451	-26.1	290	489	68.6
	c) Groundnut	251	179	-28.7	108	305	182.4
	5. Oil Meals	2263	1487	-34.3	918	1459	58.9
	6. Guargum Meal	403	486	20.6	335	388	15.8
	7. Castor Oil	626	610	-2.6	456	414	-9.2
	8. Shellac	73	90	23.3	59	120	103.4
	9. Sugar & Mollasses	1782	1814	1.8	1098	1101	0.3
	10. Processes Food	2427	2831	16.6	2036	2247	10.4
	a) Fruits and Vegetables	1191	1347	13.1	946	1274	34.7
	b) Processed Fruit & Juices	512	574	12.1	445	255	-42.7
	c) Misc.Processed Items	724	910	25.7	645	718	11.3
	11. Meat and Meat Products	1193	1377	15.4	1073	1084	1.0
	12. Floriculture Produces	127	181	42.5	134	158	17.9
	13. Spirit & Beverages	126	119	-5.6	89	94	5.6
III	**MARINE PRODUCTS**	**5897**	**6928**	**17.5**	**5420**	**4785**	**-11.7**
IV	**ORES & MINERALS**	**6020**	**9659**	**60.4**	**7161**	**6644**	**-7.2**
	1. Iron Ore	2034	4200	106.5	3088	2569	-16.8
	2. Mica	56	41	-26.8	31	55	77.4
	3. Processed Minerals	1675	2663	59.0	2092	1935	-7.5

	4. Others Ores & Minerals	1965	2497	27.1	1793	1913	6.7
	5. Coal	290	258	-11.0	157	172	9.6
V	**LEATHER MANUFACTURES**	**9110**	**8943**	**-1.8**	**6808**	**6661**	**-2.2**
	1. Footwear	3002	2895	-3.6	2085	2099	0.7
	2. Leather and Mfrs.	6108	6048	-1.0	4723	4562	-3.4
VI	**GEMS & JEWELLERY**	**34845**	**43701**	**25.4**	**31745**	**35975**	**13.3**
VII	**SPORTS GOODS**	**328**	**351**	**7.0**	**259**	**327**	**26.3**
VIII	**CHEMICAL & ALLIED PRDCTS**	**28860**	**36080**	**25.0**	**26462**	**29794**	**12.6**
	1. Basic Chemls, Pharma and Cosmetics	17630	22545	27.9	16471	18571	12.7
	2. Plastic and Linoleum	4709	5912	25.5	4425	4955	12.0
	3. Rubber, Glass and other Products*	4695	5799	23.5	4250	5057	19.0
	4. Residual Chemicals and allied Products	1826	1824	-0.1	1316	1211	-8.0
IX	**ENGINEERING GOODS**	**27406**	**37208**	**35.8**	**26356**	**32980**	**25.1**
X	**ELECTRONICS GOODS**	**5586**	**6063**	**8.5**	**4455**	**5641**	**26.6**
XI	**PROJECT GOODS**	**88**	**239**	**171.6**	**208**	**117**	**-43.8**
XII	**TEXTILES**	**46094**	**53404**	**15.9**	**39097**	**36752**	**-6.0**
	1. Readymade Garments	23877	27536	15.3	19789	18348	-7.3
	2. Cotton yarn, fabrics Made-ups etc.	14655	16217	10.7	12203	10328	-15.4
	3. Manmade textiles made-ups etc.	5079	6639	30.7	4833	5631	16.5
	4. Natural Silk textiles	1327	1504	13.3	1134	1205	6.3
	5. Wool & Woolen manufactures	249	246	-1.2	184	195	5.98
	6. Coir & Coir manufactures	295	355	20.3	280	255	-8.93
	7. Jute manufactures	612	907	48.2	674	790	17.21
XIII	**HANDICRAFTS**	**2618**	**3801**	**45.2**	**2809**	**1367**	**-51.33**
XIV	**CARPETS**	**2433**	**2578**	**6.0**	**1933**	**1870**	**-3.26**
	1. Hand-made (excl.silk	1788	1941	8.6	1467	1783	21.54
	2. Mill made (excl.silk)	473	541	14.4	400		-100.00
	3. Silk Carpet	172	96	-44.2	66	87	31.82
XV	**COTTON RAW INCL. WASTE**	**43**	**50**	**16.3**	**24**	**123**	**412.50**
XVI	**PETROLEUM PRODUCTS**	**10107**	**12469**	**23.4**	**8198**	**11383**	**38.85**
XVII	**UNCLASSIFIED ITEM S**	**7800**	**8626**	**10.6**	**5798**	**8936**	**54.12**
	GRAND TOTAL	**209018**	**255137**	**22.1**	**185017**	**201018**	**8.65**

(P) = PROVISIONAL

*** Includes Paints, Enamels & Varnish**

Annexure III:

TABLE - III

IMPORT OF PRINCIPAL COMMODITIES

(Value Rs. In Crores)

Sl. No.		Commodities	2001-2002	2002-2003	% Change	Apr-Dec.'02	Apr-Dec.'03(P)	% Change
I.		**Total Imports**	**245200**	**297206**	**21.21**	**216544**	**256020**	**18.23**
II.		**Bulk Imports**	**115330**	**135343**	**17.35**	**100907**	**118817**	**17.75**
	1	**Cereals & Preparations**	**86**	**119**	**38.37**	**91**	**58**	**36.26**
		a. Rice	..	1		10	..	..
		b. Wheat	..	..		..	..	..
		c. Other Cereals	3	..		..	1	..
		d. Cereals Preparations	83	118	42.17	81	57	-29.63
	2	**Fertilizers**	**3238**	**3028**	**-6.49**	**2372**	**2742**	**15.60**
		a. Crude	796	894	12.31	685	510	-25.55
		b. Sulphur & Unroasted Pyrites	274	403	47.08	251	289	15.14
		c. Manufactured	2168	1731	-20.16	1436	1943	35.31
	3	Edible Oil	6465	8779	35.79	6464	8837	36.71
	4	Sugar	33	33	0.00	33	20	..
	5	Pulp & Waste Paper	1405	1662	18.29	1243	1414	13.76
	6	Paper Board & Manufactures	961	1040	8.22	704	1039	47.59
	7	Newsprint	1170	1135	-2.99	885	1148	29.72
	8	Crude Rubber incl. Synthetic	831	883	6.26	658	943	43.31
	9	Non-Ferrous Metals	24941	23978	-3.86	19220	25577	33.07
	10	Metalliferrous Ore & Scrap	5455	5022	-7.94	3739	4175	11.66
	11	Iron & Steel	3976	4297	8.07	3439	4944	43.76
	12	Petroleum Crude & Products	66769	85367	27.85	62059	67920	9.44
III.		**Pearls, Precious, Semi-Precious Stones**	**22046**	**29341**	**33.09**	**21893**	**23109**	**5.55**
IV.		**Machinery**	**23405**	**30848**	**31.80**	**19772**	**26333**	**33.18**
	1	Macine Tools	920	1195	29.89	834	1368	64.03
	2	Non-Electrical Machinery $	14168	17256	21.80	12494	15514	24.17
	3	Electrical Machinery $	2835	3214	13.37	2322	2771	19.34
	4	Transport Equipment	5482	9183	67.51	4122	6680	62.06
V.		**Project Goods**	**2714**	**2626**	**-3.24**	**1807**	**1221**	**-32.43**
VI.		**Others of which**	**81705**	**99048**	**21.23**	**72165**	**86540**	**19.92**
	1	Cashew Nuts	431	1236	186.77	998	1083	8.52
	2	Fruits & Nuts	757	642	-15.19	464	558	20.26

3	Wool Raw	624	802	28.53	614	633	3.09
4	Silk Raw	625	647	3.52	513	500	-2.53
5	Synthetic & Regenerated Fibres	272	364	33.82	295	201	-31.86
6	Pulses	3160	2737	-13.39	2172	1756	-19.15
7	Raw Hides & Skins	311	270	-13.18	211	176	-16.59
8	Leather	714	688	-3.64	526	604	14.83
9	Coal, Coke & Briquettes	5452	5999	10.03	4384	4854	10.72
10	Non-Metal Mineral Manufactures	1049	1136	8.29	869	1098	26.35
11	Other Raw Minerals	489	499	2.04	378	434	14.81
12	Organic & Inorganic Chemicals	13352	14640	9.65	10794	13149	21.82
13	Dyeing, Tanning Material	1133	1340	18.27	1020	1183	15.98
14	Medicinal & Pharma Products	2027	2865	41.34	2087	2073	-0.67
15	Artificial Resins etc.	3215	3784	17.70	2784	3652	31.18
16	Chemical Products	2119	2187	3.21	1692	2033	20.15
17	Textile Yarn, Fabrics, Made-up, Art. Etc.	3392	4580	35.02	3462	4144	19.70
18	Metal Manufactures	1941	2363	21.74	1745	2275	30.37
19	Professional Instruments etc. $	4965	5484	10.45	4048	4111	1.56
20	Electronic goods incl. Computer Software	19070	29488	54.63	20698	24958	20.58

N.B. $ = Other than Electronic

Grand Total for the year April, 2002 to March, 2003 has been revised as per reference reply received from the Custom Authority.

(..) = NIL or Negligable

Annexure IV:

TABLE - IV

INDIA'S EXPORTS BY REGIONS/SUB-REGIONS

(Value in Rs. Crores)

SL NO.	REGION/SUB-REGION	2001-2002	2002-2003	%Change 2002-03 / 2001-02	Apr-Dec.02	Apr-Dec'03 (P)	%Change Apr-Dec'03 / Apr-Dec'02
I	**WEST EUROPE**	**50436**	**60061**	**19.1**	**43064**	**47664**	**10.7**
	a. European Union	46957	55763	18.8	40037	43670	9.1
	b. EFTA Countries	2234	2235	0.0	1485	1852	24.7
	c. Rest of Europe	1245	2063	65.7	1542	2142	38.9
II	**ASIA AND OCEANIA**	**80587**	**110182**	**36.7**	**78978**	**91910**	**16.4**
	a. ESCAP	55045	76282	38.6	54323	63978	17.8
	b. Rest of Asia & Ocenia	25542	33900	32.7	24655	27932	13.3
III	**AFRICA**	**13769**	**15156**	**10.1**	**11254**	**12244**	**8.8**
IV	**AMERICA**	**48214**	**62680**	**30.0**	**46068**	**44017**	**-4.5**
	a. North America	43392	56110	29.3	41508	40149	-3.3
	b. South America	2657	3877	45.9	2693	2112	-21.6
	c. Other American Countries	2165	2693	24.4	1867	1756	-5.9
V	**EAST EUROPE**	**5995**	**6061**	**1.1**	**4621**	**4953**	**7.2**
	a. Former RPA Countries	5007	5037	0.6	3886	4007	3.1
	b. Other East European Countries	988	1024	3.6	735	946	28.7
	TOTAL OF THE ABOVE*	**199001**	**254140**	**27.7**	**183985**	**200788**	**9.1**
	GRAND TOTAL	**209018**	**255137**	**22.1**	**185017**	**201018**	**8.6**

NOTE : 1. The total exports figures of regions and sub-regions do not include exports of Crude Oil and Petroleum Products.

2. Figures in brackets indicate percentage share of individual region-sub-region with respect to total of all regions at (*)

3. (P) = Provisional

Annexure V :

TABLE - V

INDIA'S IMPORTS BY REGIONS AND SUB-REGIONS

(Value in Rs. Crores)

SL NO.	REGIONS & PRINCIPAL COUNTRIES	2001-2002	2002-2003	% Change 2002-2003 / 2001-2002	Apr-Dec.'02	Apr-Dec.'03(P)	% Change Apr-Dec.'03 / Apr-Dec.'02
1	**WEST EUROPE**	**64067**	**72812**	**13.65**	**53356**	**60978**	**14.29**
	(i) E.C.M. Countries	49774	60696	21.94	44054	47919	8.77
	(ii) EFTA Countries	13931	11810	-15.23	9051	12790	41.31
	(iii) Rest of Europe	362	306	-15.47	251	269	7.17
2	**ASIA AND OCEANIA**	**74709**	**86855**	**16.26**	**62578**	**86158**	**37.68**
	(i) ESCAP	60603	70078	15.63	50777	70951	39.73
	(ii) Rest of Asia & Ocenia	14106	16777	18.94	11801	15207	28.86
3	**AFRICA**	**12435**	**16636**	**33.78**	**13158**	**11627**	**-11.64**
4	**AMERICA**	**22348**	**29322**	**31.21**	**20567**	**23112**	**12.37**
	(i) North America	17546	24245	38.18	16891	18886	11.81
	(ii) South America	4310	4506	4.55	3247	3857	18.79
	(iii) Other American and Caribean Countries	492	571	16.06	429	369	-13.99
5	**EAST EUROPE**	**4516**	**5516**	**22.14**	**4271**	**5457**	**27.77**
	(i) Former R.P.A. Countries	4028	4820	19.66	3760	4860	29.26
	(ii) Other East European Countries	488	696	42.62	511	597	16.83
6	**OTHERS**	**67125**	**86065**	**28.22**	**62614**	**68688**	**9.70**
7	**GRAND TOTAL**	**245200**	**297206**	**21.21**	**216544**	**256020**	**18.23**

NOTE : (a) Others : Unspecified and under reference.

(b) Figures shown below the figures for the Economic Regions indicate % to Grand Total.

(c) (P) = Provisional

3.8 Key Words

Export means goods sent to a foreign country to be sold.
Import means goods brought into a country from abroad for sale.
Foreign Exchange means exchanging the money of one country for that of another.
Trade Balance means international trading position of a country excluding invisible trade.

3.9 Probable Answers :

SAQI :	(i) 2003-04	(ii) Agricultural	(iii)USA
	(iv) Machinery	(v) chemical	
SAQII:	(i) False	(ii)True	(iii)True
	(iv) True	(v) False	

3.10 Reflective Questions:

- Define Foreign Exchange. Why is it so necessary for a country?
- Discuss the trends of India's foreign trade during the recent years.
- Analyze the export -import matrix in India? Do you think that it is really trade off?
- Establish the problems of Indian foreign trade. Suggest some unique measures for removing those hurdles.
- Critically argue on the relevance of FEMA.

3.11 Suggested Readings for Unit 3 :

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.) (Chapter 9,10 &11)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004) (Chapter 8)
- Dewett K.K., Verma J.D. & Sharma M.L., Indian Economics, S.Chand & Company Ltd., New Delhi (Chapter 27,28 & 49)
- Chidambaram K; Alagappan ; Business Environment, Vikas Publishing house pvt. Ltd. (Chapter 5,7&12)

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PART - III

BLOCK 5

STRUCTURAL REFORMS AND I.T. REVOLUTION

INTRODUCTION

Till the last block you have learned about lot of things; basically conceptual in nature; related to Business environment and by now I am sure that you have started realizing the fact that this subject definitely has several dimensions. The bottom-line theory is almost related to changes occurred in the environment. That is why I believe that this block which focuses on the emerging trends of business environment means a lot for you to coupe up with the changes in the environment.

This block has been divided into two units so as to enable you to grasp the idea of structural reforms in Indian economy with special emphasis on the India's foreign trade policies and at the same time with the impact of globalization the IT revolution and its impact on the business. These units have been designed to enable you to understand in details about:

- Structural reforms in Indian economy
- India's foreign trade policy
- Globalization
- Digital Cash & e-commerce.
- Evolution, growth and functioning of Indian Capital Market
- Application of Foreign Exchange Management Act.

In sum this block will equip you with the broad understanding of issues and dimensions of structural reforms that has been undertaken by India in support of liberalization of the economy and also to venture into the IT world.

While going through these units you are suppose to answer the Self Assessment Questions provided within each of the units to assess yourself about your understanding of the subject matter. In order to update yourself, it is always better if you read business magazines, news paper etc. regularly.

Especially for this block, I would like to suggest you to have a computer with internet connectivity to understand the e-commerce concepts. Are you worried? Do not worry, as you have to follow very few simple steps to accustom yourself with internet. Even if you do not have such facilities near by you, still you need not have to worry as the material is written in such a way that at least you will be through with the theoretical aspects of IT revolution and as and when you got the practical exposure, I am sure you would love to go through this block time and again!

UNIT 1
STRUCTURAL REFORMS

Structure

1.0 Objectives
1.1 Introduction
1.2 Structural reforms in Indian economy
1.2.1 Impact on Terms of Trade and Prices
1.2.2 Impact on Household Income
1.2.3 Poverty and Food Security
1.3 India's foreign Policy (Globalization and Trade Promotion)
1.4 Let us sum up

1.0 Objectives

After going through this unit you will be able to:

- Discuss the structural reforms in Indian economy
- Analyze the importance of household income in the economy
- Establish the problems of poverty and food security.
- Develop a paper on globalization and trade promotion in India.

1.1. Introduction

"There is nothing permanent except change in this world"- accordingly Indian economy has been changing dramatically after the globalization. So the structural reforms draws much attention to the masses as well as to the business houses. This unit will enable you to understand the stages of reforms as well as the impact of globalization in trade promotion.

1.2 Structural Reforms in Indian Economy

India's role in world trade and India's export performance have been relatively new areas where the whole world is focusing upon. Even less well understood is the performance of large Indian firms

and their role in overseas markets. A balance of payments crisis and India's subsequent trade liberalisation (1991) brought to an abrupt end decades of Nehruvian socialist ideas. The result has been a profound reassessment of economic strategy for growth and the role of state along with a realization of the need for institutional transformation. Economic realities have had a deep impact on the political economy of growth and the political economy of trade in India. These developments have been accompanied by fundamental changes in India's institutional framework, as the economy has transformed from an autarky to a relatively open economy. Let us discuss some of the areas where the structural reforms has an impact:

- ***Agriculture***

Indian agriculture has undergone significant changes and transformation during the last fifty years. The underlying factors for these changes were different in different periods. During 1950s and 1960s institutional reforms like land reforms and development of irrigation and other infrastructure played a major role in output growth. Technological breakthrough has been the prime mover during 1970s and spread of technological changes to wider areas and crops has been the main factor during 1980s. The decades of 1960s and 1970s also witnessed high growth in public investments in agriculture which improved infrastructural base for growth of agricultural output in the country in the following decade. The decade of 1980s show decline in public investments in agriculture and sharp rise in level of input subsidies. The declining trend in public investments for infrastructure development for agriculture continued during 1990s along with rising trend in the input subsidies. The same period (since 1991) has been marked by reforms involving, among other things, change in exchange rate and liberalization of external trade. Measures have been taken to promote integration of domestic economy with global economy. These changes in turn have affected domestic prices of several commodities and, terms of trade for agriculture have undergone changes during the decade of 1990s.

Along with liberalization of trade, private sector has been allowed and encouraged to participate in the import and export of

major agricultural products. Two, domestic prices of cereals, through government intervention in minimum support prices and open market operations, were given substantial hikes to reduce dis-protection to agriculture because of domestic prices being lower than the international prices of several commodities. This way, prices have become the major driving force for growth and development of agriculture sector during 1990s. The process of reforms, particularly trade reforms, further intensified since 1995 following implementation of WTO agreement on agriculture. There is lot of concern about the impact of trade and other reforms followed since 1991 on growth rate of agricultural output, food security, nutrition, regional equity, price stability, farm income, welfare of consumers and producers as affected by changes in prices brought about by reforms. This paper looks at some of these aspects. This has been seen by using both national level as well as household data.

- ***Agricultural Trade Before and After Reforms***

India's total agricultural exports were at $ 3.35 billion during 1990-91 which corresponds to 4.13 percent of GDP of agriculture sector. Devaluation of exchange rate by 22.5 percent in one go in 1991 followed by subsequent depreciation in the exchange rate, coupled with lifting of some restrictions on export, helped the country to double its exports in next six years (Table 1). Imports also moved on a rising trend in the same period but increase in export was much higher than the increase in agricultural imports. Consequently, the net exports increased from $ 2.67 billion during 1990-91 to $ 4.94 billion by 1996-97.The increase in export and import raised the proportion of trade in agricultural GDP from less than 5 percent in the beginning of reforms to close to nine and a half percent by 1995-96. After 1996-97, value of export started shrinking as international prices started falling (Chand 2003). Due to falling international prices imports into the country became more attractive and were facilitated due to liberalization of imports followed due to WTO commitments.

Table 1 : India's agriculture trade in post reforms and post WTO period

Year	Exports $ million	Imports $ million	Net exports $ million	Trade as % of GDP Agriculture@ Export	Import	Total
1990-91	3352	672	2679	4.13	0.83	4.95
1991-92	3203	604	2599	4.59	0.87	5.46
1992-93	2950	938	2011	4.73	1.50	6.23
1993-94	4013	742	3271	5.67	1.05	6.72
1994-95	4211	1891	2320	5.18	2.33	7.51
1995-96	6098	1761	4337	7.34	2.12	9.46
1996-97	6806	1863	4943	7.23	1.98	9.21
1997-98	6685	2364	4321	7.02	2.48	9.51
1998-99	6064	3462	2601	6.28	3.58	9.86
1999-00	5842	3708	2134	6.01	3.81	9.82
2000-01	6273	2646	3627	6.59	2.78	9.36
2001-02	6183	3408	2775	6.28	3.43	9.71

Source : Agricultural Statistics at a Glance, Ministry of Agriculture, GOI, various issues.

@ Besed Rupees value at curent prices.

Thus, after 1996-97 imports kept increasing further and were doubled in the next three years. This way the net earning from agriculture trade in the post WTO period dropped to a very low level. The post WTO period showed increase in ratio of imports to GDP whereas ratio of exports to GDP for agriculture sector followed small decline. This shows that post WTO period has been adverse to export but favourable for imports. This pattern shows sharp contrast with the first five years of reforms period when share of exports in GDP experienced sizable increase.

- Marine products are the most important items of agricultural exports from India and oilmeal/cake remained the second most important item in most of the years (Table 2). Export of marine products got a big boost with economic reforms in the initial years. During the past WTO period marine products export did not show much increase. India has registered its presence in a very big way in rice export in some years however these exports show very large year to year fluctuations. Export of oil meal increased from $ 377 million in 1991-92 to $ 985 in 1996-97. Since then export have fallen to less than half. In the case of commodities like cotton, wheat, and sugar, India occasionally export large quantity but there is no

consistent trend in these exports. Exports of traditional items from India like spices, tea and coffee and groundnut could not keep pace with the past after 1997-98. Export of horticultural products maintained upward trend during post WTO period but total export of these products is low.

Trends in export show that India has not been able to maintain steady flow of export of commodities like non-basmati rice, wheat, cotton, sugar. In the post WTO period export of oil, groundnut, spices, tea, coffee has been affected adversely. In the case of high value horticultural and livestock products, exports, in general, maintained rising trend even during the post WTO period of depressed international prices. Export of guargum meal, castor oil show the possibility of exploiting inches in export. Trend in export of caster oil is a pointer to the important role of technology that enabled India to raise castor yield in some states which equipped it with advantage in export.

Table 2 : Export of selected agricultural commodities during reforms and post WTO period, $ million

Commodity	1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02
Basmati rice	204	276	338	276	255	352	454	446	411	472	387
Non basmati rice	105	60	72	108	1113	543	454	1046	311	170	279
Wheat	52	3.5	0.07	13.5	110	197	0.11	*	*	91	280
Cotton raw inc. waste	125	63	208	45	61	444	221	49	18	48	9
Pulses	* *	18	23	29	39	37	97	53	97	118	77
Oil meal	377	534	740	573	703	985	925	461	378	448	474
Sugar and mollases	64	122	57	20	152	304	69	6	9	111	375
Marine Products	590	602	813	1127	1012	1129	1207	1038	1184	1396	1218
Groundnut	3	3	54	32	69	92	153	33	86	69	53
Spices	152	136	182	195	238	339	380	388	408	355	312
Tea	495	337	337	311	351	292	505	538	412	392	360
Coffee	136	130	174	335	450	402	457	411	332	260	229
Tobacco Mfd. &	154	164	147	81	134	213	288	181	233	190	170
Cashew	274	257	333	369	370	362	377	387	368	449	374
Castrol Oil	57	40	92	141	222	177	155	160	247	209	131
Guargnm meal	38	36	45	45	68	100	147	173	188	130	84
Poultry & dairy prod.	* *	* *	* *	* *	18	35	32	23	28	47	73
Meat & prep.	94	89	110	128	188	200	218	187	189	322	251
Floriculture product	6	5	6	10	18	18	23	25	27	26	27
Fresh fruits	* *	* *	* *	60	69	69	75	63	71	85	85
Fresh vegetables	143	108	132	79	89	94	84	65	77	100	121
Processed fruit/veg.	36	41	49	79	104	92	105	109	129	172	152

*** Less than 0.5 million $.   * * Data not avaliable**

Changes in import of major agricultural commodities during the reform period can be seen from Table 3. Import of food and related items increased three times in a short span of four years in the beginning of economic reforms. Imports of food and related items increased at a very sharp rate during post WTO period also, which raised the imports from $ 1.1 billion in 1995-96 to $2.7 billion during 1998-99. In the last two years some check has been put on these imports.

Table 3 : Import of selected agricultural commodities during reforms and post WTO period, $ million

Item	1991/ 92	1992/ 93	1993/ 94	1994/ 95	1995/ 96	1996/ 97	1997/ 98	1998/ 99	1999/ 00	2000/ 01	2001/ 02
Food and related items	321	555	426	1263	1103	1372	1678	2757	2655	1687	2332
Fruit and nuts	41	62	69	100	99	129	155	159	137	175	160
Pulses	104	109	181	189	205	251	322	168	82	109	664
Sugar	0	0	0	727	65	1	127	264	257	7	7
Edible oil	101	54	53	199	677	826	745	1803	1859	1310	1362
Cottol raw & waste		71	6	161	156	9	22	91	290	260	432

Import of edible oil accounts for major increase in food import. Till 1994-95 import of edible oil did not exceed $200 million. During 1998-99 and 1999-2000 edible oil import have risen to more than $1.8 billion. This has raised Indian's dependence on import for edible oil close to 40 per cent (Chand and Pal 2003) and is causing adverse impact on domestic oilseed growers (Chand et.al 2003). Import of cotton (raw and waste) has also witnessed quantum jump after 1998-99. Despite having large surplus of sugar for export, India witnessed import shock whenever tariffs on sugar imports were low. The trend in India's import and export during reforms period show that decline in India's agricultural exports after 1997 is consistent with the trend in global trade in agricultural products largely attributable to decline in the international prices. However, India's farm imports rose sharply during post WTO period despite decline in global agricultural trade. Thus India's agricultural imports during post WTO period did not

follow the trend in the global trade. Second, in the post WTO period trade liberalization has led to sharp rise in import of edible oil and cotton. Horticulture sub sector has seen favourable impact on export during the decade of reforms.

1.2.1 Impact on Terms of Trade and Prices

Reforms initiated in 1991 affected agricultural prices mainly in two ways. One, by giving steep hikes to domestic support prices particularly of rice and wheat to reduce gap between domestic and international prices. Two, through liberalisation of trade. The overall impact of reforms on agricultural, food and manufacturing prices for the country as a whole can be seen from the index numbers and their growth rates presented in Annexure I for one decade before and one decade during the reforms.

Terms of trade is commonly used to see whether direction of price change has remained favourable or adverse to a particular sector. There are several ways to compute TOT between two series or sectors. One of the simplest but quite revealing and appealing index of TOT for agriculture is given by the ratio of prices received by agriculture relative to prices paid for by the sector. This ratio, as computed and reported by Ministry of Agriculture, for the sector as a whole is presented in Table 4 for the last two decades. This ratio with base triennium ending 1990-91 reveals that during 1980s prices received by agriculture increased at a much faster rate than the prices paid by agriculture. In other words, TOT moved in favour of agriculture during 1981-82 to 1990-91. This way by 1990-91 a favourable pricing environment was created for agriculture sector. With the beginning of economic reforms there was further improvement in the already favourable situation of TOT for agriculture. Prices received by agriculture relative to prices paid by it reached a peak level by 1994-95 (Fig 1) and fluctuated at that level for about four years. Last three years i.e. 1999-00 to 2001-02 have witnessed some decline in TOT for agriculture but still TOT are more favourable to agriculture compared to the period before reforms.

Rate of increase in prices was also examined for different foodstuffs. During the decade preceding reforms prices of cereals

show lowest growth among selected groups of food commodities (Table 5). The rate of increase was 5.76 percent which was smaller than rate of inflation in overall economy and cereal prices in real terms declined by about one percent per year before reforms. During the decade after economic reforms were started, trend rate of increase in cereal prices turned out to be more than 9 percent. In real terms cereal prices during the decade of reforms increased annually by 1.5 percent whereas prices of non cereal foods put in one group followed decline in real terms as is implied by negative growth rate in food articles. This implies that during the reform period prices have caused adverse effect on consumption of cereals and favourable effect on non-cereal foods. Growth rate in nominal prices of all the commodities was much lower in post WTO period compared to the five years period of domestic reforms before WTO. Growth rate in nominal cereal prices during post WTO period was half of the growth rate recorded during reforms before WTO. Similarly growth rate in prices of pulses, fruits and vegetables and meat products during post WTO period was one third of the growth rate in reform period before WTO. Nominal prices of edible oil followed decline after 1996-97. In fact, it is felt that had government not taken measures to keep a check on cereal imports their prices in post WTO period would have followed decline due to decline in international prices. Growth rate in overall price index in the country declined from 10.55 percent per annum during 1990-91 to 1996-97 to 5.01 percent during 1996-97 to 2001-02. Deflating agricultural prices by this index shows that cereal prices despite significant slowdown in nominal terms continued to rise at a more or less same rate in real term during pre and post WTO reform period. However, in the case of edible oils, pulses, and fruits and vegetables the growth rate in real prices after 1996-97 was negative. In the post WTO period rate of increase in nominal cereal prices is found to be the same as observed during pre-reform decade but in real terms cereal prices kept increasing at 0.67 percent per annum. Real prices of food as a group show rising trend in the post WTO period.

Table 4 : Index of price received and paid by agriculture and terms of trade, bese TE 1990-91 = 100

Year	Index of prices received	Index of prices paid	Terms of trade
1981-82	54.9	61.9	88.7
1982-83	60.3	66.0	91.4
1983-84	64.2	70.1	91.6
1984-85	68.0	72.4	93.9
1985-86	70.4	75.2	93.6
1986-87	76.7	80.2	95.6
1987-88	86.0	88.3	97.4
1988-89	90.3	91.8	98.4
1989-90	97.5	98.1	99.4
1990-91	112.3	110.2	101.9
1991-92	130.8	123.8	105.7
1992-93	138.7	133.5	103.9
1993-94	151.4	146.1	103.6
1994-95	171.1	160.5	106.6
1995-96	182.9	173.7	105.3
1996-97	190.6	184.8	103.1
1997-98	205.9	194.9	105.6
1998-99	220.8	209.9	105.6
1999-00	219.8	214.0	102.7
2000-01	225.0	218.9	102.8
2001-02	229.4	224.3	102.3
Growth rates :			
1981-82 to 1990-91	7.74	6.23	1.42
1990-91 to 1999-00	7.83	7.77	0.06
1990-91 to 1995-96	9.99	9.40	0.54
1995-96 to 2001-02	3.92	4.38	-0.44

Source : *Agricultural Statistics at a Glance*, August 2003, Ministry of Ariculture, GOI, New Delhi

An econometric exercise was carried out to see definite impact of liberalization on domestic prices. This was done by estimating effect of international prices, real exchange rate and trade liberalization during 1990s (measured by dummy variable) and import duty on domestic price index of agricultural commodities measured in $. The results are presented in Table 6.

Fig 1.A : Terms of trade for agriculture

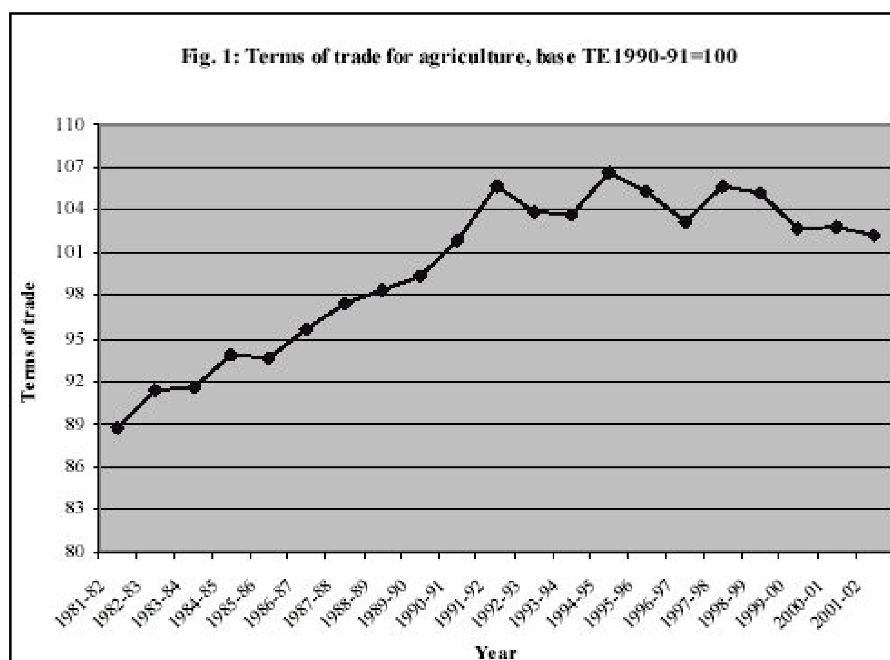

Table 5 : Growth rate in prices of various food commodity groups before and during reforms

Price/Period	Cereal	Pulses	Edible Oil	Fruit & vegetable	Milk & its products	Meat, Egg & fish	All food articles	All Commodities
Nominal Prices								
1981-82 to 1990-91	5.76	10.35	8.83	7.45	8.57	7.27	9.14	6.75
1990-91 to 2000-01	9.45	9.77	2.68	8.65	7.31	11.10	7.77	7.87
1990-91 to 1996-97	11.33	13.58	4.39	10.96	8.06	13.79	8.01	10.55
1996-97 to 2001-02	5.72	4.15	-0.76	3.55	7.89	5.87	5.45	5.01
Real Prices								
1981-82 to 1990-91	-0.93	3.37	1.95	0.65	1.70	0.49	2.24	
1990-91 to 2000-01	1.47	1.77	-4.81	0.72	-0.52	3.00	-0.09	
1990-91 to 1996-97	0.71	2.74	-5.57	0.37	-2.25	2.93	-2.30	
1996-97 to 2001-02	0.67	-0.83	-5.50	-1.39	2.74	0.81	0.42	

Computed from Index Number of Wholsale Prices in India, Government of India, various Issues.

All the four variables explained 68 percent variation in index of food prices (expressed in $) in India. In the first round, containing all the explanatory variables, effect of international price was significant at 11 percent and dummy variable was significant at less

than 2 percent. The impact of import duty showed negative but highly non significant impact. Dropping of some variables show that international price, real exchange rate and trade liberalization as seen through dummy caused significant effect on domestic prices. The analysis showed that domestic prices of agricultural commodities are affected by international prices and level of real exchange rate. Import duty in most cases has not been effective in protecting domestic prices from international prices. The reason for this seems to be that non tariff measures have been used more effectively by India to regulate trade. Removal of control on imports and exports during 1990s has brought down the level of agricultural prices in general.

Table 6 : Effect of International Prices, Import Duty, Real Exchange rate and Trade Liberalisation on Domestic Wholsale Price of Food Articles, 1980-81 to 1999-00.

Regression runs	Constant	International Price	Real Exchange Rate	Import Duty	Dummy	R-Square
I						
Coefficient	3.646	0.310	-0.068	-0.014	-0.225	0.682
t-statistics/F stat	2.091	1.664	-0.300	-0.256	-2.652	-9.121
Significance	0.052	0.114	0.768	0.801	0.017	0.000
II						
Coefficient	3.519	0.306	-0.048		-0.210	0.681
t-statistics/F stat	2.162	1.693	-0.232		-3.426	12.804
Significance	0.044	0.108	0.819		0.003	0.000
III						
Coefficient	-0.255	0.540	0.553			0.473
t-statistics/F stat	-0.170	2.579	3.903			8.522
Significance	0.867	0.018	0.001			0.002
IV						
Coefficient	3.162	0.337			-0.198	0.680
t-statistics/F stat	6.068	2.853			-6.114	20.183
Significance	0.000	0.010			0.000	0.000

Source : Chand et. al. 2003b

1.2.2 Impact on Household Income

There are no surveys available at national or regional level in India to find out changes in income of farm households due to changes in policy during the decade of reforms. However, National Sample Surveys on consumer expenditure conducted by National Sample Survey Organization, Government of India, provide authentic data on total household expenditure, which has been often used as a

proxy for income. In the absence of any other source for estimating changes in income of farm households this paper also use total expenditure as a proxy for income. This includes income coming from all sources that is farm and non-farm. This proxy has been used to estimate growth in income (total expenditure) during 1993-94 to 1999-2000. These two years correspond to nation wide main sample survey during the reforms period. Nominal income was deflated by Consumer Price Index for Agricultural Labour for rural households. Changes in income of farm and labour households in rural India can be seen from the information furnished in Table 7.

During 1993-94 to 1999-00 real per capita income of rural households increased 2.01 percent. Per capita income as measured by total expenditure in real prices at cultivator and labour households increased at the rate of 2.17 and 2.59 percent annually. Table 7 also contains information on growth rate in income of different farm size categories over time. This shows that per capita real income from all sources increased at a slightly higher rate at sub marginal and marginal holdings compared to the other farm size holdings. Going further down the economic ladder, per capita income of landless labour has grown at a higher rate compared to farm households. The reason for this could be the growth rate in real wage rates for agricultural labour.

Table 7: Growth rate in real income and level of income at current prices for different sections of rural population during 1987-88 to 1999-00

Household category	Compound growth rate in income at 1987-88 prices % / year		Per capita nominal income Rs./ year		
	1987-88 to1993-94	1993-94 to 1999-00	1987-88	1993-94	1999-2000
Landless labour	-0.26	2.59	1532	2661	4831
Cultivators					
All size classes	-0.40	2.17	2180	3755	6652
Sub-marginal	-0.19	2.71	1887	3292	6019
Marginal	-0.37	2.73	1974	3407	6234
Small	-0.34	2.20	2097	3652	6430
Medium	0.10	2.57	2273	4036	7319
Large	-0.63	2.46	2772	4710	8487
All rural	-0.24	2.01	2122	3692	6478

Note : Basic information drawn from NSSO household data.

Source : Chand et. al. 2003b

It is interesting to compare the growth rate in total household income with growth rate in income derived from agricultural sector but comparable information is not available from the two sources. However, some crude comparison can be attempted. GDP agriculture during the decade of reforms show annual trend growth rate of 3.28 percent and rural population during the same period increased at the rate of 1.67 percent. Deducting population growth rate from growth rate of GDP agriculture shows that agriculture income per rural person increased at the rate of 1.6 percent. This is lower than the per capita total household income which increased at the rate of 2.01 percent during the reforms years. These results show that income derived from non farm sources by rural households increased at a faster rate than agricultural income during the reforms period.

1.2.3 Poverty and Food Security

Change in poverty and household food security were seen during the period 1983 to 1999-00. The reason for including year 1983 in the analysis was to compare the change process before reforms as observed from the data for year 1983 and 1987-88 with the change process during reforms as revealed by comparing 1987-88 situation with 1993-94 and 1999- 00. Level of energy intake and protein intake and per cent of population consuming less than suggested norm of calorie and protein[1] were used as indicators of food security. Average per capita calorie intake at cultivator households in India during the year 1983 was 2289 kcal, which increased to 2423 during 1987-88. With the beginning of economic reforms calorie intake declined to 2277 and remained at this level

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[1]. **2** Minimum (threshold) food-energy requirement is taken as 1800 kcal/ person/day for rural households and 1575 kcal for the urban households. These requirements represent 75% of the recommended calorie which is 2400 kcal / person / day for rural and 2100 kcal/person/day for urban (V.M. Dandekar, 1996 Chapter 6 Poverty Debate). An intake below this threshold is not sufficient to maintain health and body mass, and nor to support light physical activity. The threshold level of food-protein intake is taken 48 gram per person per day for the average Indian. Below this level of protein the persons of the household are treated as malnourished.

during the year 1999-2000 (Table 8). Protein intake increased between 1983 and 1987-88 and declined thereafter in 1993-94 and 1999-00. Among different size classes calorie intake showed decline in the beginning of reforms and increase thereafter except in the case of large farm size group which recorded decline. In all the survey years per capita calorie intake increased with the increase in size of farm, which represents economic class.

Calorie intake at labour households dropped sharply in the beginning of reforms and recovered subsequently. Calorie intake at labour households during 1999-00 is slightly higher as compared to the year 1983 but lower as compared to 1987-88.

There was a sharp reduction in percent of population consuming less than minimum level of calorie suggested for a healthy person between 1983 and 1987-88. The process got reversed in the beginning of economic reforms. With further progress in reforms, undernourished population (i.e. population deficit in calorie) among farm households increased but there was a sharp decline in the case of labour households.

Incidence of malnourishment (protein deficiency) showed a sharp decline before reforms. With the beginning of economic reforms farm population deficit in protein showed a slight increase. Intensification of reforms with trade liberalization however was accompanied by sharp increase in malnourishment of farm population. The situation is somewhat different in the case of labour households. Their protein deficit population increased substantially in the beginning of reforms and dropped subsequently. According to the estimate for the year 1999-2000 more than 26 percent farm population and more than 45 percent of rural labours are suffering from energy and protein deficiency.

Table 8: Nutrition and poverty among agricultural labour and farm households of various size groups

Aspect/Year	Agriculture labour	Farms househols
Population under poverty %		
1983	64.6	42.6
1987-88	55.3	31.6
1993-94	54.6	30.1
1999-00	39.7	21.0
Undernourished population %		
1983	48.6	29.0
1987-88	41.2	21.9
1993-94	53.6	24.0
1999-00	45.5	26.2
Malnourished population		
1983	44.1	27.7
1987-88	38.0	21.1
1993-94	50.0	22.3
1999-00	48.7	28.2
Calorie intake/person/day		
1983	1908	2289
1987-88	2010	2423
1993-94	1819	2277
1999-00	1948	2278
Protein intake/person/day : gram		
1983	54.0	64.7
1987-88	56.9	69.2
1993-94	50.7	65.3
1999-00	51.9	62.7
Sample households		
1983	11074	47582
1987-88	4909	52945
1993-94	9013	40418
1999-00	10627	40611

It would be seen from the results presented in Table 8 that reduction in poverty before reforms was associated with sharp reduction in under nourishment and malnourishment. However, after 1987-88, reduction in poverty did not reduce undernourishment. There was no significant reduction in poverty between 1987-88 and 1993-94 but during 1993-94 and 1999-2000 percent of population under poverty came down from 30.1 percent to 21 percent at farm households and from 54.6 percent to 39.6 percent at labour

households. In a sharp contrast to reduction in poverty, incidence of undernourishment show small increase and malnourishment show large increase at farm households. However, at labour households reduction in poverty between 1993-94 and 1999-00 reduced incidence of undernourishment to a considerable extent even though undernourished population was higher during 1999-00 compared to 1987-88.

The reason for this differential impact on labour and farm households is related to dietary pattern presented in Table 9. There was a very small decline in cereal intake and moderate to large increase in consumption of pulses, fruits and vegetables, milk, meat etc at labour households. Thus, the impact of small decline in cereals was more than offset by increased consumption of the other foods. Moreover, there was no decline in food grain (cereal plus pulses) consumption at labour households. This helped in reducing undernourishment and malnourishment among rural agricultural labour. In contrast to this, there was a sharp drop in per capita consumption of cereals and total food grains at farm households, even after 1993-94, which could not be compensated by increased consumption of horticultural and livestock products. This caused increase in nutritional deficiency at farm households.

Table 9: Changes in consumption pattern of rural households as revealed by quantity (kg) consumed per person per year, 1983 to 1999-2000

Household Category	Year	Cereals	Palses	Edible oil	Fruits & Veg.	Milk	Meat	Sugar
Landless labure								
	1983	166.2	8.2	2.7	39.4	16.8	3.3	8.1
	1987-88	162.6	8.7	3.5	47.0	26.2	3.6	9.5
	1993-94	149.3	7.4	3.8	61.4	23.9	4.4	7.4
	1999-00	148.4	8.5	5.1	70.3	25.5	4.7	8.0
Farm households								
	1983	187.5	11.7	3.6	50.2	41.4	3.7	11.2
	1987-88	186.2	12.4	4.4	60.3	56.6	4.7	11.8
	1993-94	171.3	10.2	4.8	74.4	65.8	4.4	10.6
	1999-00	161.2	10.9	79.3	79.3	68.1	5.4	11.0

These patterns in poverty, nutrition and cereal intake show that poverty and cereal intake plays important role in nutritional security of rural households in India. These changes also show that high growth rate in output of fruits and vegetables and livestock products in India during 1990s did not help Indian masses to improve nutrition. As cereals constitute the major share in the food and the decade of 1990s witnessed their reduced consumption the net result has been increase in proportion of population deficit in calorie. Similarly, pulses are the main source of protein in India, stagnation in their production is the cause of protein deficiency.

There is a strong feeling among some researchers that decline in cereal consumption in India is the result of structural shifts in demand or dietary diversification away from cereals caused by changes in life style, tastes and preferences and it should not be seen as causing adverse effect on nutrition. However, the decline in cereal consumption during 1990s was much higher than what was accounted for by dietary diversification (Chand et.al. 2003b). The rate of decline in cereal consumption was small during 1970s and 1980s - the period during which real prices of cereals were also falling. During 1990s rate of decline in cereal consumption accelerated by about 70 percent. The reason for this acceleration in the rate of decline in cereal consumption was sharp increase in real prices of cereals in the same period.

Agriculture sector witnessed sharp improvement in terms of trade during initial years of reforms. In the post WTO period though TOT remained favourable compared to the period before reforms but there is decline in them. Second, among different crop groups rice and wheat have enjoyed most favourable price environment because of strong government support in raising their support prices. However, growth rate in cereal prices has not helped in growth of their output because price support actually benefited agriculturally developed region which have exhausted their production potential. And this support was missing in the regions which have low yield and high potential for growth.

Growth rate in GDP of agriculture sector showed almost no change during the pre reform decade and post reform period. Division

of agriculture sector into crop and livestock sub-sectors shows a clear acceleration in growth rate of output of crop sector and a clear deceleration in the growth rate of output of livestock sector during the reform period. There is also deceleration in output of fishing sector during reforms. Acceleration in output of crop sector is solely due to very sharp rise in growth rate of fruits and vegetables and almost all other crops show moderate to high decline in growth rate during reforms period. When reform period is divided into pre WTO reforms and post WTO reforms the growth rates present very depressing scenario - sharp deceleration and negative growth rates in some cases. Similarly, exports have been adversely affected and imports have seen fast growth after WTO. There is modest increase in per capita income of farm and labour households during reforms, contributed more by non farm incomes than farm incomes. There is also significant reduction in poverty. However, household food security and nutrition have worsened during reforms, the reason for which seems to be high growth in prices of cereals caused due to government policy to give substantial hikes to cereal prices during reforms.

● ***Financial sector***

The financial sector is in a process of rapid transformation. Reforms are continuing as part of the overall structural reforms aimed at improving the productivity and efficiency of the economy. The role of an integrated financial infrastructure is to stimulate and sustain economic growth.

The US$ 28 billion Indian financial sector has grown at around 15 per cent and has displayed stability for the last several years, even when other markets in the Asian region were facing a crisis. This stability was ensured through the resilience that has been built into the system over time. The financial sector has kept pace with the growing needs of corporate and other borrowers. Banks, capital market participants and insurers have developed a wide range of products and services to suit varied customer requirements. The Reserve Bank of India (RBI) has successfully introduced a regime where interest rates are more in line with market forces.

Financial institutions have combated the reduction in interest rates and pressure on their margins by constantly innovating and targeting attractive consumer segments. Banks and trade financiers have also played an important role in promoting foreign trade of the country.

● ***Banks***

The Indian banking system has a large geographic and functional coverage. Presently the total asset size of the Indian banking sector is US$ 270 billion while the total deposits amount to US$ 220 billion with a branch network exceeding 66,000 branches across the country. Revenues of the banking sector have grown at 6 per cent CAGR over the past few years to reach a size of US$ 15 billion. While commercial banks cater to short and medium term financing requirements, national level and state level financial institutions meet longer-term requirements. This distinction is getting blurred with commercial banks extending project finance. The total disbursements of the financial institutions in 2001 were US$ 14 billion.

Banking today has transformed into a technology intensive and customer friendly model with a focus on convenience. The sector is set to witness the emergence of financial supermarkets in the form of universal banks providing a suite of services from retail to corporate banking and industrial lending to investment banking. While corporate banking is clearly the largest segment, personal financial services is the highest growth segment.

The recent favourable government policies for enhancing limits of foreign investments to 49 per cent among other key initiatives have encouraged such activity. Larger banks will be able to mobilize sufficient capital to finance asset expansion and fund investments in technology.

● ***Capital Market***

The Indian capital markets have witnessed a transformation over the last decade. India is now placed among the mature markets of the world. Key progressive initiatives in recent years include:

- The depository and share dematerialization systems that have enhanced the efficiency of the transaction cycle
- Replacing the flexible, but often exploited, forward trading mechanism with rolling settlement, to bring about transparency
- The infotech-driven National Stock Exchange (NSE) with a national presence (for the benefit of investors across locations) and other initiatives to enhance the quality of financial disclosures.
- Corporatisation of stock exchanges.
- The Securities and Exchange Board of India (SEBI) has effectively been functioning as an independent regulator with statutory powers.
- Indian capital markets have rewarded Foreign Institutional Investors (FIIs) with attractive valuations and increasing returns.
- Many new instruments have been introduced in the markets, including index futures, index options, derivatives and options and futures in select stocks.

- ***Insurance***

With the opening of the market, foreign and private Indian players are keen to convert untapped market potential into opportunities by providing tailor-made products:

- The presence of a host of new players in the sector has resulted in a shift in approach and the launch of innovative products, services and value-added benefits. Foreign majors have entered the country and announced joint ventures in both life and non-life areas. Major foreign players include New York Life, Aviva, Tokio Marine, Allianz, Standard Life, Lombard General, AIG, AMP and Sun Life among others.
- With competition, the erstwhile state sector companies have become aggressive in terms of product offerings, marketing and distribution.
- The Insurance Regulatory and Development Authority (IRDA) has played a proactive role as a regulator and a facilitator in the sector's development.

- The size of the market presents immense opportunities to new players with only 20 per cent of the country's insurable population currently insured.
- The state sector Life Insurance Corporation (LIC), the largest life insurer in 2000, sold close to 20 million new policies with a turnover of US$ 5 billion.
- There are four public sector and nine private sector insurance companies operating in general/non-life insurance business with a premium income of over US$ 2.58 billion.
- The market's potential has been estimated to have a premium income of US$ 80 billion with a potential size of over 300 million people.

- ***Venture Capital***

Technology and knowledge have been and continue to drive the global economy. Given the inherent strength by way of its human capital, technical skills, cost competitive workforce, research and entrepreneurship, India is positioned for rapid economic growth in a sustainable manner. To realize the potential, there is a need for risk finance and venture capital (VC) funding to leverage innovation, promote technology and harness knowledge based ideas.

- The Indian venture capital sector has been active despite facing a challenging external environment in 2001 and a competitive market scenario.
- There were 34 VCFs and 2 Foreign VCFs registered with SEBI in March 2002.
- According to a survey conducted by Thomson Financial and Prime Database, India ranked as the third most active venture capital market in Asia Pacific (excluding Japan).
- There is an increased interest in India: 70 VC funds operate in India with the total assets under management worth about US$ 6 billion.

a. Opportunities

- There is no tax on distributed income of VCFs. The income distributed by the funds is only taxed at the hands of the investors.

- Increase in incomes with potentially high penetration of both banking and insurance products to increase the market size, will be the powerful drivers of growth in the sector.
- Continued de-regulation and increased competition is expected to result in the Indian financial services reach US$ 51 billion by 2007.

Now let us do a simple exercise:

SAQ I

Fill up the blanks:

(1) A balance of payments crisis and India's subsequent trade liberalisation (1991) brought to an abrupt end decades of Nehruvian -------- ideas.

(2) The decades of 1960s and 1970s also witnessed ------ growth in public investments in agriculture

(3) Trends in ------show that India has not been able to maintain steady flow of export of commodities like non-basmati rice, wheat, cotton, sugar.

(4) Import of edible oil accounts for major increase in ----- import.

(5) During 1993-94 to 1999-00 real per capita income of rural households increased ------- percent

Check your answer with the one provided at the end of the unit.

1.3 India's foreign Policy (Globalization and Trade Promotion)

Globalisation is seen to be the world's "mega-trend" over the next 15 years, causing the global economy to grow by about 80% compared with 2000, and raising average income per head worldwide by about 50% over the same period. The benefits will be unevenly distributed but there will be a much richer world.

Economists world over believe, that most of this growth will be in Asia, especially in China and India, driving Asia to displace the west over the next 15 years as the focus of global economic dynamism. The impact of that shift will be economic and political, pulling Washington's attention away from Europe and the Middle East and towards the emerging 21st century superpowers.

In this backdrop, it is important to carefully examine the issues underlying India and the global economy.

If we look at the Indian experience since independence, we find that export pessimism permeated the policy stance throughout the early decades of our planning. Import substitution was the principal instrument of trade policy and was regarded in the early years as not only the correct strategy but also inevitable in a continental economy like India. The gulf crisis and its impact on India provided several lessons for us, and one of them was that a relatively closed economy does not provide immunity from a foreign exchange crisis. Incidentally, India excelled in managing the crisis and emerged as one of the very few countries in the world, amongst both the developed and the developing, to have never defaulted on its external obligations. In the aftermath of the Gulf crisis, policy actions were initiated as part of the overall macroeconomic management well coordinated to simultaneously achieve stabilization and structural change. External sector policies designed to progressively open up the Indian economy formed an integral part of the strategy for structural reforms.

In this context, improvement in exports, both merchandise and invisibles were recommended. Suggestions were made regarding modulation of import demand on the basis of the availability of current receipts to ensure a level of current account deficit consistent with normal capital flows. Further, Indian policy makers took up measures to enhance non-debt creating flows to limit the debt service burden. A switch over to market-determined exchange rate; building up the foreign exchange reserves to avoid liquidity crises and elimination of the dependence on short-term debt were some of the most important changes that were suggested. It is evident that these changes in the external sector policies of the 1990s, paid rich dividends in terms of growth and resilience to a series of external and domestic shocks.

● ***India's approach in the new millennium***

In the 21st century, there has been a dramatic shift in India's approach to external sector management in tune with the changing

circumstances. First, with the emergence of marginal current account surplus, the sustainability of India's current account deficit may not be a problem though the deficit on her trade account persists and has been increasing. Second, the main contributors to the positive outcome in India's current account are workers' remittances and export of software, both being a result of process of global integration. Third, the exchange rate regime as well as external debt management has served India well, especially the avoidance of sovereign debt through commercial borrowings. The new policy regime helped India withstand several global crises while maintaining a respectable growth. Fourth, the management of capital account has acquired the primary focus rather than the current account. Fifth, a judicious integration with the global trade regime has imparted some competitive efficiency and confidence to the domestic industry and perhaps, even to commercial agriculture though to a limited extent. Finally, it has become evident that the management of the external sector is closely linked to the domestic sector and the major thrust of Indian public policy is now on managing the integration.

In brief, India has moved from managing external sector to implementing an optimal integration of domestic and external sectors, and the global economy.

More recently, however, a debate in the rest of the world has been in evidence on the challenges likely to be faced by the global economy on account of progressively increasing global integration of the Indian economy. There is a need to have an ongoing appreciation of how the global economy is responding to the challenges of our integration while we move forward with our own agenda of securing an optimal integration.

Currently, the major issue in the global economy appears to be the significant build up of current account imbalances. The current account deficit of U.S.A. has been rising and is around 5% of GDP, while current account surpluses are noticed in Asia and to some extent in Latin America and Russia. The external financing of the US deficit moved away from equity in the late nineties to debt in the recent years, possibly reflecting a perception of productivity growth in the

former period and fiscal stress in the latter. The official reserves played a greater role than in the past in financing the US current account deficit in recent years.

Further, the simultaneous emergence of China and India with significant competitive strengths in trade in goods as well as services will have to be accommodated by the global economy. Thus, the issue for the immediate future is that both, correcting current global imbalances and integrating the two Asian giants, may have to take place simultaneously in the global economy. Let us have an account of the latest Indian Exim Policy 2002-07 :

- ***Service Exports***

Duty free import facility for service sector having a minimum foreign exchange earning of Rs.10 lakhs.

The duty free entitlement shall be 10% of the average foreign exchange earned in the preceding three licensing years. However, for hotels, the same shall be 5% of the average foreign exchange earned in the preceding three licensing years. This entitlement can be used for import of office equipments, professional equipments, spares and consumables. However, imports of agriculture and dairy products shall not be allowed for imports against the entitlement. The entitlement and the goods imported against such entitlement shall be non-transferable.

- ***Agro Exports***

(a) Corporate sector with proven credential will be encouraged to sponsor Agri Export Zone for boosting agro exports. The corporates to provide services such as provision of pre/post harvest treatment and operations, plant protection, processing, packaging, storage and related R&D.

(b) DEPB rate for selected agro products to factor in the cost of pre-production inputs such as fertiliser, pesticides and seeds.

- ***Status Holders***

(a) Duty-free import entitlement for status holders having incremental growth of more than 25% in FOB value of exports (in free foreign exchange).

This facility shall however be available to status holders having a minimum export turnover of Rs.25 crore (in free foreign exchange). The duty free entitlement shall be 10% of the incremental growth in exports and can be used for import of capital goods, office equipment and inputs for their own factory or the factory of the associate/ supporting manufacturer/job worker. The entitlement/ goods shall not be transferable. This facility shall be available on the exports made from 1.4.2003.

(b) Annual Advance Licence facility for status holders to be introduced to enable them to plan for their imports of raw material and components on an annual basis and take advantage of bulk purchases.

(c) The Input-Output norms for status holders to be fixed on priority basis within a period of 60 days.

(d) Status holders in STPI shall be permitted free movement of professional equipments like laptop/computer.

● ***Hardware/Software***

(e) To give a boost to electronic hardware industry, supplies of all 217 ITA-1 items from EHTP units to DTA shall qualify for fulfillment of export obligation.

(f) To promote growth of exports in embedded software, hardware shall be admissible for duty free import for testing and development purposes. Hardware upto a value of US$ 10,000 shall be allowed to be disposed off subject to STPI certification.

(g) 100% depreciation to be available over a period of 3 years to computer and computer peripherals for units in EOU/EHTP/STP/ SEZ.

● ***Gem & Jewellery Sector***

(h) Diamond & Jewellery Dollar Account for exporters dealing in purchase/sale of diamonds and diamond studded jewellery.

(i) Nominated agencies to accept payment in dollars for cost of import of precious metals from EEFC account of exporter.

(j) Gem & Jewellery units in SEZ and EOUs can receive precious metal i.e Gold/silver/platinum prior to exports or post exports equivalent to value of jewellery exported. This means that

they can bring export proceeds in kind against the present provision of bringing in cash only.

● ***Export Clusters***

8. Upgradation of infrastructure in existing clusters/ industrial locations under the Department of Industrial Policy & Promotion (DIPP) scheme to increase overall competitiveness of the export clusters.

9. Supplemental efforts to be made under the ASIDE scheme and similar schemes of other Ministries to bridge technology and productivity gaps in identified clusters.

10. 10 such clusters with high growth potential to be reinvigorated based on a participatory approach.

● ***Rehabilitation of Sick Units***

For revival of sick units, extension of export obligation period to be allowed to such units based on BIFR rehabilitation schemes. This facility shall also be available to units outside the purview of BIFR but operating under the State rehabilitation programme.

● ***Removal of Quantitative Restrictions***

7. Import of 69 items covering animal products, vegetables and spices, antibiotics and films removed from restricted list.
8. Export of 5 items namely paddy except basmati, cotton linters, rare earth, silk cocoons, family planning devices except condoms removed from restricted list.

● ***Special Economic Zones Scheme***

7. Sales from Domestic Tariff Area (DTA) to SEZs to be treated as export. This would now entitle domestic suppliers to Drawback/ DEPB benefits, CST exemption and Service Tax exemption.
8. Agriculture/Horticulture processing SEZ units will now be allowed to provide inputs and equipments to contract farmers in DTA to promote production of goods as per the requirement of importing countries. This is expected

to integrate the production and processing and help in promoting SEZs specialising in agro exports.

9. Foreign bound passengers will now be allowed to take goods from SEZs to promote trade, tourism and exports.
10. Domestic sales by SEZ units will now be exempt from SAD.
11. Restriction of one year period for remittance of export proceeds removed for SEZ units.
12. Netting of export permitted for SEZ unit provided it is between same exporter and importer over a period of 12 months.
13. SEZ units permitted to take job work abroad and exports goods from there only.
14. SEZ units can capitalize import payables.
15. Wastage for subcontracting/exchange by gem and jewellery units in transactions between SEZ and DTA will now be allowed.
16. Export/import of all products through post parcel/courier by SEZ units will now be allowed.
17. The value of capital goods imported by SEZ units will now be amortised uniformly over 10 years.
18. SEZ units will now be allowed to sell all products including gems and jewellery through exhibitions and duty free shops or shops set up abroad
19. Goods required for operation and maintenance of SEZ units will now be allowed duty free.

● ***EOU Scheme***

7. Agriculture/Horticulture processing EOUs will now be allowed to provide inputs and equipments to contract farmers in DTA to promote production of goods as per the requirement of importing countries. This is expected to integrate the production and processing and help in promoting agro exports.
8. EOUs are now required to be only net positive foreign exchange earner and there will now be no export performance requirement.

9. Foreign bound passengers will now be allowed to take goods from EOUs to promote trade, tourism and exports.
10. The value of capital goods imported by EOUs will now be amortized uniformly over 10 years.
11. Period of utilisation of raw materials prescribed for EOUs increased from 1 year to 3 years.
12. Gems and jewellery EOUs are now being permitted sub-contracting in DTA.
13. Wastage for subcontracting/exchange by gem and jewellery units in transactions between EOUs and DTA will now be allowed as per norms.
14. Export/import of all products through post parcel/courier by EOUs will now be allowed.
15. EOUs will now be allowed to sell all products including gems and jewellery through exhibitions and duty free shops or shops set up abroad
16. Gems and jewellery EOUs will now be entitled to advance domestic sales.

● ***EPCG Scheme***

7. The scheme shall now allow import of capital goods for pre-production and post-production facilities also.
8. The Export Obligation under the scheme shall now be linked to the duty saved and shall be 8 times the duty saved.
9. To facilitate upgradation of existing plant and machinery, import of spares shall also be allowed under the scheme.
10. To promote higher value addition in exports, the existing condition of imposing an additional Export Obligation of 50% for products in the higher product chain to be done away with.
11. Greater flexibility for fulfillment of export obligation under the scheme by allowing export of any other product manufactured by the exporter. This shall take care of the dynamics of international market.
12. Capital goods upto 10 years old shall also be allowed under the scheme.

13. To facilitate diversification into the software sector, existing manufacturer exporters will be allowed to fulfill export obligation arising out of import of capital goods under the scheme for setting up of software units through export of manufactured goods of the same company.
14. Royalty payments received from abroad and testing charges received in free foreign exchange to be counted for discharge of export obligation under EPCG scheme.

● ***DEPB Scheme***

7. Facility for provisional DEPB rate introduced to encourage diversification and promote export of new products.
8. DEPB rates rationalized in line with general reduction in Customs duty.

● ***Advance Licence***

7. Standard Input Output Norms for 403 new products notified.
8. Anti-dumping and safeguard duty exemption to advance licence for deemed exports for supplies to EOU/SEZ/EHTP/STP.

● ***DFRC Scheme***

7. Duty Free Replenishment Certificate scheme extended to deemed exports to provide a boost to domestic manufacturer.
8. Value addition under DFRC scheme reduced from 33% to 25%.

● ***Reduction of Transaction Cost***

7. High priority being accorded to the EDI implementation programme covering all major community partners in order to minimise transaction cost, time and discretion. We are now gearing ourselves to provide on line approvals to exporters where exports have been effected from 23 EDI ports.

8. Online issuance of Importer-Exporter Code(IEC) number by linking the DGFT EDI network with the Income Tax PAN database is under progress.
9. Applications filed electronically (through website www.nic.in/eximpol) shall have a 50% lower processing fee as compared to manual applications.

- ***Miscellaneous***

7. Actual user condition for import of second hand capital goods upto 10 years old dispensed with.
8. Reduction in penal interest rate from 24% to 15% for all old cases of default under Exim Policy.
9. Restriction on export of warranty spares removed.
10. IEC holder to furnish online return of imports/exports made on yearly basis.
11. Export of free of cost goods for export promotion @ 2% of average annual exports in preceding three years subject to ceiling of Rs.5 lakh permitted.

It is evident that China and India will have to give a high priority to generating employment. Both these emerging economies are poised for substantial increases in productivity. Consequently, the global economy will have to consider the implications of these developments on prices, exchange rates, wages and structures of employment in industrialised countries. Over the medium term, it is felt that outsourcing will grow in geometric progression, particularly to India, and may also cover high-end research and development. One sector where the industrialised economies continue to show considerable strength and dominance is the financial sector, partly attributable to the confidence factor in financial markets that favours the industrialised economies and traditional international financial centres. It is essential for India to carefully monitor the developments in both real and financial sectors, and to modulate her policies in accordance with the global developments so that global integration continues to be a positive sum game for all the countries. Global economic integration is technology induced and policy-managed. While the economic integration of India with the global economy will continue to take place, a successful integration, with due regard

to the interests of a vast majority particularly, the poor would be possible only through sound public policies - evolved and redesigned from time to time. The BRIC report reflects considerable confidence in the future of the Indian economy, though it is necessary to see the fine print to realise that while India would be a super power in 2050, "if development proceeds successfully", the per capita income would still not be at a high end. What is important to recognise is that the report leans on the demographic strength that India derives from its huge workforce. In order to harness the demographic advantages, the quality of labour force, (in terms of relevant skills which need to be sustained, reoriented and upgraded in a globally competitive era) and the physical health of the workforce become crucial. Education and health, therefore, provide the link between supply and demand for labour through increases in productivity.

- ***Financial integration- the third side of global integration***

Unlike in the case of trade integration where benefits to all countries are demonstrable, in case of financial integration, a "threshold" is important for a country to get full benefits. Fortunately, India, has been adhering to a cautious and calibrated approach in our reforms so far and there is merit in adopting a 'road map approach' building on the strengths that we have already developed.

One of the major concerns for developing countries in proceeding with financial integration appears to be the financial stability. Hence, the role of cross-border linkages in this regard should not be ignored.

It is noteworthy that financial integration complicates the conduct of monetary management. The growing cross-border integration of financial markets enables massive movements of capital, which quickly arbitrage interest rate differentials across national boundaries. This is reinforced by the ever-widening impact of the information technology revolution. Real long-term interest rates in industrialised countries have been converging since the late 1980s. Financial integration has also brought with it shocks common to several countries since the "confidence channel" transmits financial crises across countries swiftly. In a world of generalised uncertainty, monetary policy in several countries is faced with a progressive loss of discretion. For developing countries, in particular, considerations

relating to maximizing output and employment weigh equally upon monetary authorities as maintaining the price stability.

It is also useful to recognize a close link between the extent of capital account liberalisation and the presence of foreign financial enterprises in a country. One of the important considerations for encouraging the presence of foreign financial enterprises is to ensure adequate and healthy competition. The compulsion to expand foreign enterprises would thus depend on quality of competition that is already existing in a country. In any case, the consensus appears to be that process of liberalization in financial sector has to be carefully calibrated and sequenced.

● ***Licensing foreign banks in the emerging economies***

The pros relate to (a) increasing and diversifying available funds; (b) enhancing banking competition and efficiency; (c) developing financial markets and market infrastructure; (d) helping with recapitalisation and wider diversification of banks; and (e) reducing sensitivity of the host country banking system to local business cycles and changing financial market conditions. The arguments against foreign banks' entry encompass (i) weakening infant domestic banks; (ii) servicing only the 'best' customers and neglect of Small and Medium Enterprises; (iii) likelihood of bringing instability; (iv) concerns that majority of banking assets will become foreign owned; and above all (v) challenges to financial supervisors in the emerging markets.

India's approach to financial sector reforms, in general, and to the management of the external sector, in particular, has served the country well, in terms of aiding growth, avoiding crises, enhancing efficiency and imparting resilience to the system. The development of financial markets has been, by and large, healthy. The basic features of the Indian approach are gradualism; co-ordination with other economic policies; pragmatism rather than ideology; relevance to the context; consultative processes; dynamism and good sequencing so as to be able to meet the emerging domestic and international trends. The intention to move over to capital account convertibility was announced in 1997 and its achievement is still an ongoing process - which differentiates the roles of individuals, corporate and financial intermediaries.

In the banking system, diversified ownership of public sector banks has been promoted over the years and the performance of their listed stocks in the face of intense competition indicates improvements in the system. Foreign banks have been operating in India for decades with a few of them having operations in India for over a century. The number of foreign bank branches in India has increased significantly in recent years since RBI issued a number of licenses - well beyond the commitments made to the World Trade Organisation. The presence of foreign banks in India has benefited the financial system by enhancing competition, resulting in higher efficiency. There has also been transfer of technology and specialised skills which has had some "demonstration effect" as Indian banks too have upgraded their skills, improved their scale of operations and diversified into other activities. At a time when access to foreign currency funds was a constraint for the Indian companies, the presence of foreign banks in India enabled large Indian companies to access foreign currency resources from the overseas branches of these banks. Also with the presence of foreign banks, as borrowers in the money market and their operation in the foreign exchange market has resulted in the creation and deepening of the inter-bank money market. Now, it is the challenge for the supervisors to maximize the advantages and minimize the disadvantages of the foreign banks' local presence.

The liberalisation measures would need to take into account several imperatives, such as, consolidation of domestic banking sector; restructuring of Development Finance Institutions; and appropriate timing for the significant entry of foreign banks so as to be co-terminus with the transition to greater capital account convertibility while being consistent with our continuing obligation under the WTO commitments. The Reserve Bank of India intends to formulate the guidelines, through an ongoing process of consultation, as in the past. The proposed guidelines in this regard are expected to carry forward the process of financial integration of India in a carefully calibrated and transparent manner.

Thus, in this background India's global integration has to be a two way process, encompassing movement of people with some caveats, trade in a free and equitable manner and financial integration on a specially sequenced basis.

Now let us do another simple exercise:

SAQ II

State whether the following are true or false:

(1) Economists world over believe, that most of the economic growth will be in Asia, especially in Bangladesh and India.

(2) Indian policy makers took up measures to enhance non-debt creating flows to limit the debt service burden.

(3) India has moved from managing external sector to implementing an optimal integration of domestic and external sectors, and the club economy.

(4) It is evident that China and India will have to give a high priority to generating employment.

Check your answer with the one provided at the end of the unit.

1.4 Let Us Sum Up

This time I want to give you an activity in terms of summing the unit within 150 words. You can use the following space for the same.

1.5 Annexure

Annexure 1 :

PRESS RELEASE

INDIA'S FOREIGN TRADE: APRIL-JULY 2006-2007

EXPORTS

Exports during July, 2006 are valued at US $ 10176.80 million (provisional) which is 40.67% higher than the level of US $ 7234.41 million (provisional) during July, 2005. In rupee terms, the exports were Rs.47277.53 crores (provisional) which is 50.11% higher than the level of Rs. 31495.81crores (provisional) during July, 2005.

(The provisionally revised figure of exports for July 2005 is US $ 7546.89 million/Rs. 32856.21 crores).

Exports during April-July, 2006 are valued at US $ 37707.60 million (provisional) which is 34.03% higher than the level of US $ 28134.72 million (provisional) during April-July, 2005. In rupee terms, the exports were Rs.172542.53 cores (provisional) during April-July, 2006 which is 40.71% higher than the level of Rs. 122622.01 crores (provisional) during April-July, 2005.

(The provisionally revised figure of exports for April-July 2005 is US $ 31223.01 million/ Rs. 136088.91 crores).

IMPORTS

Imports during July, 2006 are valued at US $ 14143.06 million (provisional) representing an increase of 42.8% over the level of imports valued at US $ 9904.22 (provisional) million in July, 2005. In Rupee terms, the imports were Rs. 65703.27 crores (provisional) which is 52.38% higher than the level of Rs. 43119.09 crores (provisional) during July 2005.

(The provisionally revised figure of imports for July 2005 is US $ 11384.61 million/Rs. 49564.17 crores).

Total imports during April-July, 2006 are valued at US $ 54424.34 million (provisional) which is 29.24% higher than the level of US $ 42109.47 million (provisional) during April-July 2005. In rupee terms, the imports were Rs. 248925.88 crores (provisional) which is 35.6% higher than the level of Rs. 183537.52 crores (provisional) during April- July 2005.

(The provisionally revised figure of imports for April-July 2005 is US $ 45598.75 million/ Rs. 198735.76 crores).

Oil imports during July 2006 are valued at US $ 4642.31 million which is 32.83% higher than oil imports valued at US 3494.80 million in the corresponding period last year. Oil imports during April-July 2006 are valued at US $ 18533.53 million which is 43.23% higher than oil imports valued at US $ 12940.14 million in the corresponding period last year. Non-oil imports during July 2006 are estimated at US $ 9500.75 million which is 20.42% higher than the level of such imports valued at US $ 7889.81 million in July 2005. Non-oil imports during April-July, 2006 are estimated at US $ 35890.81 million which is 9.90% higher than the level of such imports valued at US $ 32658.61 million in April-July 2005.

TRADE BALANCE

The trade deficit for April-July, 2006 is estimated at US $ 16716.74 million (provisional) which is higher than the deficit of US $ 13974.75 million (provisional) during April-July, 2005.

DEPARTMENT OF COMMERCE
ECONOMIC DIVISION

IMPORTS & EXPORTS : (PROVISIONAL) **(US $ Million)**

	July		April-July	
	Provisional	Revised**	Provisional	Revised**
EXPORTS				
2005-06*	7234.41	7546.89	28134.72	31223.01
2006-07*	10176		37707.60	
% Growth 2006-07 / 2005-06	40.67	34.85	34.03	20.77
IMPORTS				
2005-06*	9904.22	11348.61	42109.47	45598.75
2006-07*	14143.06		54424.34	
% Growth				
2006-07 / 2005-06	42.8	24.23	29.24	19.35
TRADE BALANCE				
2005-06*	-2669.81	-3837.72	-13974.75	-14375.75
2006-07*	-3966.26		-16716.74	

***Provisional figures reported in Press Note for July 2005.**

DEPARTMENT OF COMMERCE ECONOMIC DIVISION				
IMPORTS & EXPORTS : (PROVISIONAL)				(Rs Crores)
	July		April-July	
	Provisional	Revised**	Provisional	Revised**
EXPORTS				
2005-06*	31495.81	32856.21	122622.01	136088.91
2006-07	47277.53		172542.53	
% Growth 2006-07 / 2005-06	50.11	43.89	40.71	26.79
IMPORTS				
2005-06*	43119.09	49564.17	183537.52	198735.76
2006-07	6503.27		248925.88	
% Growth 2006-07 / 2005-06	52.38	32.56	35.63	25.25
TRADE BALANCE				
2005-06*	-11623.28	-16707.96	-60915.51	-62646.85
2006-07	-18425.74		-76383.35	
*Provisional figures reported in Press Note for July 2005.				
**Revised figures are the latest available figures of the year unadjuted for the late returns				

1.6 Key Words

Trade - business of buying and selling ; export trade and import trade-the business of buying from other countries or selling in other countries.

Economic Zones - promoting exports.

1.7 Probable Answers :

SAQI : (i)socialist (ii) high (iii) export
(iv) food (v) 2.01

SAQII: (i) False (ii)True (iii)True
(iv) False

1.8 Reflective Questions:

- Discuss the structural reforms in Indian economy.
- Analyze the importance of household income in the economy.
- Establish the problems of poverty and food security.
- Develop a paper on globalization and trade promotion in India.

1.9 Suggested Readings for Unit 1:

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004)
- Dewett K.K., Verma J.D. & Sharma M.L., Indian Economics, S.Chand & Company Ltd., New Delhi
- Chidambaram K; Alagappan ; Business Environment, Vikas Publishing house pvt. Ltd.
- Khan F.A; Business and Society, S.Chand & co., Delhi.

UNIT 2
I.T. REVOLUTION

Structure

2.0 Objectives
2.1 Introduction
2.2 Globalization
2.2.1 Indian stand in terms of Global Integration
2.3 Digital Cash
2.4 E-commerce
2.5 Impact of globalization, WTO, etc.
2.6 Let us sum up

2.0 Objectives

After going through this unit you will be able to:

- Discuss the problems of globalization
- Analyze the importance of globalization in Indian economy.
- Establish the problems of implementing Digicash.
- Argue on the effectiveness of e-commerce in India
- Write a seminar paper on the e-commerce entities.

2.1 Introduction

The importance of Information and Technology in an economy can not simply be ignored. After the globalization, the importance of IT even receives more importance because of the volatile applicability in countries like India. In this unit the role of globalization in India, role of Digital Cash, e-commerce etc. has been detailed elaborately.

2.2 Globalisation

Globalisation is the new buzzword that has come to dominate the world since the nineties of the last century with the end of the cold war

and the break-up of the former Soviet Union and the global trend towards the rolling ball. The frontiers of the state with increased reliance on the market economy and renewed faith in the private capital and resources, a process of structural adjustment spurred by the studies and influences of the World Bank and other International organisations have started in many of the developing countries. Also Globalisation has brought in new opportunities to developing countries. Greater access to developed country markets and technology transfer hold out promise improved productivity and higher living standard. But globalisation has also thrown up new challenges like growing inequality across and within nations, volatility in financial market and environmental deteriorations. Another negative aspect of globalisation is that a great majority of developing countries remain removed from the process. Till the nineties the process of globalisation of the Indian economy was constrained by the barriers to trade and investment liberalisation of trade, investment and financial flows initiated in the nineties has progressively lowered the barriers to competition and hastened the pace of globalisation

Globalization is a relatively new term used to describe a very old process. It is a historical process that began with our human ancestors moving out of Africa to spread all over the globe. In the millennia that have followed, distance has been largely overcome and human-made barriers lowered or removed to facilitate the exchange of goods and ideas. Propelled by the desire to improve one's life and helped along by technology, both the interconnectedness and interdependence have grown. This increasing integration of the world or 'globalization' has enriched life but also created new problems.

Globalised World - What does it mean?

- Does it mean the fast movement of people which results in greater interaction?
- Does it mean that because of IT revolution people can be in touch with each other in any part of the world?
- Does it mean trade and economy of each country is open in Non-Intrusive way so that all varieties are available to consumer of his choice?

- Does it mean that mankind has achieved emancipation to a level of where we can say it means a social, economic and political globalisation?

Though the precise definition of globalisation is still unavailable a few definitions worth viewing, Stephen Gill: defines globalisation as the reduction of transaction cost of transborder movements of capital and goods thus of factors of production and goods. Guy Brainbant: says that the process of globalisation not only includes opening up of world trade, development of advanced means of communication, internationalization of financial markets, growing importance of MNC's, population migrations and more generally increased mobility of persons, goods, capital, data and ideas but also infections, diseases and pollution.

- ***Impact on India***

India opened up the economy in the early nineties following a major crisis that led by a foreign exchange crunch that dragged the economy close to defaulting on loans. The response was a slew of Domestic and external sector policy measures partly prompted by the immediate needs and partly by the demand of the multilateral organisations. The new policy regime radically pushed forward in favour of amore open and market oriented economy.

Major measures initiated as a part of the liberalisation and globalisation strategy in the early nineties included scrapping of the industrial licensing regime, reduction in the number of areas reserved for the public sector, amendment of the monopolies and the restrictive trade practices act, start of the privatisation programme, reduction in tariff rates and change over to market determined exchange rates.

Over the years there has been a steady liberalisation of the current account transactions, more and more sectors opened up for foreign direct investments and portfolio investments facilitating entry of foreign investors in telecom, roads, ports, airports, insurance and other major sectors.

The Indian tariff rates reduced sharply over the decade from a weighted average of 72.5% in 1991-92 to 24.6 in 1996-97.Though tariff

rates went up slowly in the late nineties it touched 35.1% in 2001-02. India is committed to reduced tariff rates. Peak tariff rates are to be reduced to be reduced to the minimum with a peak rate of 20%, in another 2 years most non-tariff barriers have been dismantled by march 2002, including almost all quantitative restrictions.

- ***India is Global***

The liberalisation of the domestic economy and the increasing integration of India with the global economy have helped step up GDP growth rates, which picked up from 5.6% in 1990-91 to a peak level of 77.8% in 1996-97. Growth rates have slowed down since the country has still bee able to achieve 5-6% growth rate in three of the last six years. Though growth rates has slumped to the lowest level 4.3% in 2002-03 mainly because of the worst droughts in two decades the growth rates are expected to go up close to 70% in 2003-04. A Global comparison shows that India is now the fastest growing just after China.

This is major improvement given that India is growth rate in the 1970's was very low at 3% and GDP growth in countries like Brazil, Indonesia, Korea, and Mexico was more than twice that of India. Though India's average annual growth rate almost doubled in the eighties to 5.9% it was still lower than the growth rate in China, Korea and Indonesia. The pick up in GDP growth has helped improve India's global position. Consequently India's position in the global economy has improved from the 8th position in 1991 to 4th place in 2001. When GDP is calculated on a purchasing power parity basis.

- ***Globalisation and Poverty***

Globalisation in the form of increased integration though trade and investment is an important reason why much progress has been made in reducing poverty and global inequality over recent decades. But it is not the only reason for this often unrecognized progress, good national polices , sound institutions and domestic political stability also matter.

Despite this progress, poverty remains one of the most serious international challenges we face up to 1.2 billion of the developing world 4.8 billion people still live in extreme poverty.

But the proportion of the world population living in poverty has been steadily declining and since 1980 the absolute number of poor people has stopped rising and appears to have fallen in recent years despite strong population growth in poor countries. If the proportion living in poverty had not fallen since 1987 alone a further 215million people would be living in extreme poverty today.

India has to concentrate on five important areas or things to follow to achieve this goal. The areas like technological entrepreneurship, new business openings for small and medium enterprises, importance of quality management, new prospects in rural areas and privatisation of financial institutions. The manufacturing of technology and management of technology are two different significant areas in the country.

There will be new prospects in rural India. The growth of Indian economy very much depends upon rural participation in the global race. After implementing the new economic policy the role of villages got its own significance because of its unique outlook and branding methods. For example food processing and packaging are the one of the area where new entrepreneurs can enter into a big way. It may be organized in a collective way with the help of co-operatives to meet the global demand.

Understanding the current status of globalisation is necessary for setting course for future. For all nations to reap the full benefits of globalisation it is essential to create a level playing field. President Bush's recent proposal to eliminate all tariffs on all manufactured goods by 2015 will do it. In fact it may exacerbate the prevalent inequalities. According to this proposal, tariffs of 5% or less on all manufactured goods will be eliminated by 2005 and higher than 5% will be lowered to 8%. Starting 2010 the 8% tariffs will be lowered each year until they are eliminated by 2015.

- ***GDP Growth rate***

The Indian economy is passing through a difficult phase caused by several unfavourable domestic and external developments; Domestic output and Demand conditions were adversely affected by poor performance in agriculture in the past two years. The global economy experienced an overall deceleration and recorded an output growth of 2.4% during the past year growth in real GDP in 2001-02 was 5.4% as

per the Economic Survey in 2000-01. The performance in the first quarter of the financial year is5.8% and second quarter is 6.1%.

● ***Export and Import***

India's Export and Import in the year 2001-02 was to the extent of 32,572 and 38,362 million respectively. Many Indian companies have started becoming respectable players in the International scene. Agriculture exports account for about 13 to 18% of total annual of annual export of the country. In 2000-01 Agricultural products valued at more than US $ 6million were exported from the country 23% of which was contributed by the marine products alone. Marine products in recent years have emerged as the single largest contributor to the total agricultural export from the country accounting for over one fifth of the total agricultural exports. Cereals (mostly basmati rice and non-basmati rice), oil seeds, tea and coffee are the other prominent products each of which accounts fro nearly 5 to 10% of the countries total agricultural exports.

2.2.1 Indian stand in terms of Global Integration

India clearly lags in globalisation. Number of countries has a clear lead among them China, large part of east and far east Asia and Eastern Europe. Let's look at a few indicators how much we lag.

● Over the past decade FDI flows into India have averaged around 0.5% of GDP against 5% for China 5.5% for Brazil. Whereas FDI inflows into China now exceeds US $ 50 billion annually. It is only US $ 4billion in the case of India

● Consider global trade - India's share of world merchandise exports increased from .05% to .07% over the pat 20 years. Over the same period China's share has tripled to almost 4%.

● India's share of global trade is similar to that of the Philippines an economy 6 times smaller according to IMF estimates. India under trades by 70-80% given its size, proximity to markets and labour cost advantages.

● It is interesting to note the remark made by Mr. Bimal Jalan, Governor of RBI. Despite all the talk, we are now where ever close being Globalised in terms of any commonly used indicator of

globalisation. In fact we are one of the least Globalised among the major countries - however we look at it.

● As Amartya Sen and many other have pointed out that India, as a geographical, politico-cultural entity has been interacting with the outside world throughout history and still continues to do so. It has to adapt, assimilate and contribute. This goes without saying even as we move into what is called a Globalised world which is distinguished from previous eras from by faster travel and communication, greater trade linkages, denting of political and economic sovereignty and greater acceptance of democracy as a way of life.

● ***Globalised India: how much effective?***

The implications of globalisation for a national economy are many. Globalisation has intensified interdependence and competition between economies in the world market. This is reflected in Interdependence in regard to trading in goods and services and in movement of capital. As a result domestic economic developments are not determined entirely by domestic policies and market conditions. Rather, they are influenced by both domestic and international policies and economic conditions. It is thus clear that a globalizing economy, while formulating and evaluating its domestic policy cannot afford to ignore the possible actions and reactions of policies and developments in the rest of the world. This constrained the policy option available to the government which implies loss of policy autonomy to some extent, in decision-making at the national level.

Simply put, globalization will be more enduring and successful if it can give reasons to most citizens to go along with it. Cooperation is most productive when it is voluntary, not manipulated or coerced. It is difficult to imagine sustaining voluntary cooperation without going through democracy. Globalizers often throw reasons at people, rather than address reasons to them, as democracy requires. A politics of resentment against globalization is fuelled, not because people (except for the few ideologically over-committed ones) are incapable of understanding its benefits. The resentment stems from a sense that the terms of globalization are often being created in an arbitrary way. To

take a prosaic example, very few countries have ratification procedures that subject international treaties to extensive discussion before signing, and they often present them to their legislatures as fait accompli. Democracy, messy and slow as it is, is the only way of ensuring that all the relevant considerations have been taken into account in creating a new architecture for the world. Whether globalization is seen as a process open to continual negotiation at all levels or as a force of nature to be passively endured will make a world of difference to its prospects for the future.

The modern world is animated by two important passions. The first is the possibility of creating a more interdependent and prosperous world that globalizers promise. The second is the desire to inhabit a particular kind of social world that democrats insist on. This is a social world whose important contours are ones that people inhabiting it can freely accept. Successful globalization requires that it be seen as part of a process that creates such a world. In short, it requires the legitimacy only democracy can give. Democracy in turn, will be strengthened if it is exercised in full awareness of the preconditions of a more prosperous and secure world. The two aspirations are often in tension with one another. But the concrete work of politics is to align them as fully as possible. Globalization without democracy will be alienating; democracy without globalization will be imprudent.

- ***Politicalisation of the concept***

Globalization creates new risks as well as opportunities. Voters expressing dissatisfaction with their economies are not simply opposing globalization per se, but rather asking legitimate questions about the distribution of risks this process entails. Why should particular classes of labor be made more vulnerable by globalization than holders of capital? Why should the low-yield, but risk-averse farming strategies of an Indian farmer with a small plot of land give way to large-scale commercial farming that takes the land away from him? If banks and big creditors can be insured against economic shocks, why can't self-employed workers? Democracy is one of the more effective ways of bringing to light the risks and vulnerabilities that need to be taken into account. Closed societies with settled social patterns need less open

discussion, because the pace of change is slow. The more rapid and far-reaching the change (even for the better), the more important it is to bring to light new risks and vulnerabilities. Any version of globalization that is impatient with democracy is selling itself short on two counts. It is foreclosing the flow of vital information about the effects of globalization. And it is conceding the anti-globalization case that globalization cuts down the possibility of creative solutions to real problems.

Now let us do a small exercise :

SAQ I

Fill up the blanks :

(1) -----------has brought in new opportunities to developing countries.

(2) Globalisation as the reduction of transaction cost of transborder movements of capital and goods thus of factors of --------- and goods.

(3) Major measures initiated as a part of the liberalisation and globalisation strategy in the early nineties included scrapping of the industrial ---------- regime

(4) While formulating and evaluating its domestic policy------- cannot afford to ignore the possible actions and reactions of policies and developments in the rest of the world.

Check your answer with the one provided at the end of the unit.

2.3 Digital Cash

Digital cash has been pioneered by DigiCash. Its founder, David Chaum, is an expert in financial cryptography and is the inventor of more than half a dozen cryptographic processes covered by US Patents. DigiCash has created and markets a software program called "ecash", which basically creates DBCs that represent units of various currencies.

Currently, US Dollars, Finnish Markkas and Australian Dollars circulate on the Internet using the ecash system, with several other

currencies to be introduced in the near future. Although DigiCash is the only company with a working product that is now available for use, there are other companies and independent developers who are working on digital cash systems as well.

Digital cash is ideal for what is known as micropayments, or transactions of less than US$10 in value. Micropayments are generally not economical with credit cards or electronic fund transfers, primarily because of the high overhead costs in processing those transactions. Digital cash makes small payments of just a few cents possible and profitable for both the merchant receiving the payment and the issuer of the digital cash.

One of the interesting features of digital cash is that it allows for relative degrees of privacy in monetary transactions. DigiCash's ecash only provides privacy (anonymity) for the payer in the transaction. The payee reveals himself when he verifies the authenticity of the ecash with the issuer. Other types of digital cash involve anonymity for both parties or neither party. Ideally, individuals will be able to choose between these different systems to decide the level of privacy they wish to maintain in any transaction.

● ***Why monetary freedom is important***

If all that digital cash permits is the ability to trade and store dollars, francs, and other governmental units of account, then we have not come very far. Even the major card associations, such as Visa and MasterCard, are limited to clearing settling governmental units of account. For in an age of inflation and government ineptness, the value of what is being transacted and saved can be seriously devalued. Who wants a hard drive full of worthless "cash"? True, this can happen in a privately-managed digital cash system, but at least then it is determined by the market and individuals have choices between multiple providers.

● ***Key elements of a private digital cash system***

This section compares and contrasts true digital cash to paper cash as we know it today. Each of the following key elements will be defined and explored within the bounds of electronic commerce:

- Secure
- Anonymous
- Portable (physical independence)
- Infinite duration (until destroyed)
- Two-way (unrestricted)
- Off-line capable
- Divisible (fungible)
- Wide acceptability (trust)
- User-friendly (simple)
- Unit-of-value freedom

The transition to a privately-operated digital cash system will require a period of brand-name recognition and long-term trust. Some firms may at first have an advantage over lesser-known name-brands, but that will soon be overcome if the early leaders fall victim to monetary instability. It may be that the smaller firms can devise a unit of value that will enjoy wide acceptance and stability (or appreciation).

True digital cash as an enabling mechanism for electronic commerce depends upon the marriage of economics and cryptography. Independent academic advancement in either discipline alone will not facilitate what is needed for electronic commerce to flourish. There must be a synergy between the field of economics which emphasizes that the market will dictate the best monetary unit of value and cryptography which enhances individual privacy and security to the point of choosing between several monetary providers. It is money, the lifeblood of an economy, that ultimately symbolizes what commercial structure we operate within.

2.4 E-Commerce

Technological collaboration, information interchange, internet facilities or world wide web(www) are some of the buzz words in today's e-oriented world. With the inception of e-commerce concept, the overall business environment has received a boon to explore the Internet facilities to a profitable proposition. Of course in many parts of the third world countries, the business set up is still in a process of transforming to the e-world.

The likely advantages that one can derive from the internet usage includes :

- Lasting structural changes and a catalyst for change.
- Shifting the composition of work from transactional to creative.
- Reduced inefficiencies.
- New customers and enhanced customer focus.
- Lower transaction and purchasing lists.
- Better communication - both internal and external.

e- commerce per se'; is unlikely to fulfill all its promised advantages and benefits. For instance, "Hoechst Marion Russell, a multinational corporation in the pharmaceutical industry, considers organizing internal processes the zero step, preceding any e-commerce initiative. Automating and integrating business process via back office functions is a key pre requisite. A web- based front end, designed to be a customer self service application, demands that the internal customer database and transactional history be automated first and made accessible through the internet. Such demand necessitates an all around assessment of the enterprise and its environment. E-marketing enables companies to leverage the potential of their internal resources along with the external resources."

Out of the several entities of e-commerce, only the two portals plays an important role and also receives popularity. These Two portals are B-to - B (Business to Business) and B- to - C (Business to Customers).

Business to Business or B-2-B in e-marketing is the exchange of services, products or information between marketing business houses. B-2-B term can represent functions that provide information, facilitate transactions or execute transactions or completely integrate shared business process into separate ERP systems. The B-2-B portal is more effective when it comes to international service marketing. In fig 2A different types of B-2-B e-marketing has been highlighted:

Fig 2A

Types of B to B e-marketing	
Type of B-2-B	Created By
Customer - Controlled	A Consortium of Customers aggregates their orders.
Service provider - Controlled	Service providers who cater to fragmented market places come together to create a common trading place.
Third party logistic provider - controlled	Also called as neutral market place created & controlled by matchmakers.

B-2-C e-marketing facilitate transactions of commodities, products & services between business enterprises and retail customers. For the vendor, B-2-C e-marketing offers the benefits of 24X7 anytime, anywhere, facilitating wider reach and cost - savings arising from reduction of intermediaries. Although B-2-C in e-marketing attracts infrastructural requirements which are little complex - as only one side of the transaction process demands complex technology - related integration, the buyer only requires an online connectivity. The procurement and fulfillment issues are less complicated.

Though the performances of these portals are not upto the level as it is expected. So where lies the factors, which affects the development of e-commerce in Third World countries. From a recent study it was found that the possible success outcome of e-commerce is as high as 94%. Naturally a study is desired to analyze the factors, which affects the growth of e-marketing.

Of course while analyzing the e-commerce system there exists a lot of subsystems like e-accounting, e-logistics, e-auditing, e-marketing, e-laws related to marketing, so on and so forth. Still we believe that the e-payment system is one of the aspect which actually determines the success of a e-marketing programs. Currency conversion and payment options are basically two difficult aspects that a e-international marketers

has to face. Payments through credit cards are often being treated as obsolete mode of payment. In the emerging field of electronic commerce, novel buzzwords like smartcards, online banking, digital cash, and electronic cheque are being used to discuss money.

For having a prompt and effective e-commerce system, the players must follow the following road map:

Stage I: Track the trend :

- Computerization of various departments.
- Basic internal networking.
- Implementing function - specific application package.
- Adopting e-mail and the Internet.
- Installing GroupWare.
- Installing complete Internet; integrating business processes.
- Providing email and Internet usage to all levels of employees - increasing Internet usage.
- Developing own website in stages.

Stage II: Structure follows Strategy:

- Increasing the use of the internet/e-mail for basic business communication, customer services etc.
- Start using / trying out external portals - registering with the portals.
- Installing extranets, starting to connect branches / plants and channel partners.
- Implementing enterprise solutions, ERP, MRP.
- Linking up with the extranets / WANs of major user companies.
- Enabling the company web site for order taking, order placement, customer services, etc.

Stage III: Implement, Manage & Monitor :

- Making the company website e-marketing enabled.
- Implementing e-marketing for OEM Supplies.

- Implementing e-marketing for distributor / dealer supplies.

The world is at a stage where all trends suggest an imminent surge in e-commerce. The IT act, convergence, e-governance initiatives, the globalization of the economy, the distinct drive within public and private sector firms for efficiency a nd the use of technology to achieve these are good signs. But in most of the third world countries infrastructure is definitely not quite in place. This is not just in terms of bandwidth, connectivity, processing, etc. there is much more to infrastructure; the entire "management" dimension of technology needs to be recognized for sustainable e-commerce.

The B -2 -B e-commerce is catching up the entire world. Transaction fees are major revenue source for almost 90% of the portals, in an attempt to replicate the entire range of transaction categories. Other major contributory are the Membership Subscription and Revenue Sharing with other groups. For B -to -B transaction, all dealers need to be integrated. There must be a common vision, which will lead to the integration and synergy for the benefits of all. For B -to -C, payment gateway deployment will play a critical role and appropriate portal deployment too.

However the success of B -2 -C portals of e-commerce in general is yet to be ascertained. The multitude of marketplaces and their multifaceted business models notwithstanding, industry analysts believe B -2 -C transactions in e-marketing will need sometime to take off. This is primarily because of the small Net population, owing to the dismal infrastructure in terms of PC Penetration and availability and cost of Internet connectivity in some parts of the world.

Customization of digital currencies and payment procedures, thanks to e-banking has a positive impact on the e-marketing business as the concept of 'business online payment offline' has been waived off with the introduction of EBPP. EBPP costs just about a sixth of that of a cheque. Yet payments were almost entirely offline for all the marketing companies in India and other developing countries. Indian companies are still not comfortable with payment gateways. Most of them are still skeptical about the legal and operational viability of payment gateways. There is a definite lack of awareness about the actual functioning and utility of payment gateways. The primary mode for e-marketing transactions for most companies will be tie-ups with banks. Options the

such as smart cards and debit/credit cards are perceived to be relevant only to B -2 -C segment. However, the e-marketing companies reported only 30% of online payments. This is on expected lines such as the shipping and air cargo sectors which are moving towards full- fledged EDI systems in line with government /customs stipulations.

2.5 Impact of Globalization, WTO etc.

The impact of Globalization on e-commerce is tremendous and basically the economic environment has changed dramatically after the globalization concept emerges. The economic reforms which are being carried out in USSR, East European Countries, Cuba, etc. which were so revolutionary some years ago, one could not even imagine such changes taking place in these countries. In the People Republic of China, which had been following one of the most conservative policies, economic reforms began as early as 1970s. Marketization, Privatization and Internationalization have been progressing in these countries at a amazing speed. Several of these countries have effectively eliminated state monopoly of foreign trade and have drastically reduced import controls. There has been an influx of foreign private capital and technology. Thus barrier of political ideology to business, particularly to international business is fast disappearing.

Far reaching reforms have been established in many non-communist countries too, particular in developing ones. Economic liberalization encompassing greater scope and freedom for private enterprise, both domestic and foreign and trade liberalization has the center point of these reforms.

The basic objectives as can be derived from several reports of WTO are to provide market access, domestic support and export platform for its members. Apart from these, the basic aims of WTO is to

- Higher growth rate resulting into higher level of economic activity worldwide.
- Stable Dollar prices, and
- Changes in Key currencies.

Now question arises how will e-commerce players fledgling the industry to redefine itself under this new regime? And how will it shape

solutions to one's business needs? The changing scenario has lead to certain marketing issues that an international marketer must understand and design their strategies accordingly.

- With the growing competition, product differentiation and positioning will become more important.
- Companies will have to forgo the Cost Plus concept will pay more attention to quality and price to survive in the competitive market.
- The variety of the product forms available will entirely be depending upon the consumers' choice.
- Licensing, franchising and multi-level marketing will become the order of the day.
- Abundant entrepreneurial chances will be provided by the fast growing international service marketing sector.

Let us do another small exercise:

SAQ II

State whether the following are true or false :

(1) David Chaum, is an expert in economic cryptography

(2) Digital cash is ideal for what is known as micro payments, or transactions of less than US$01 in value.

(3) True digital cash as an enabling mechanism for electronic commerce depends upon the marriage of finance and cryptography.

(4) Business to Business or B-2-B in e-marketing is the exchange of services, products or information between marketing individuals.

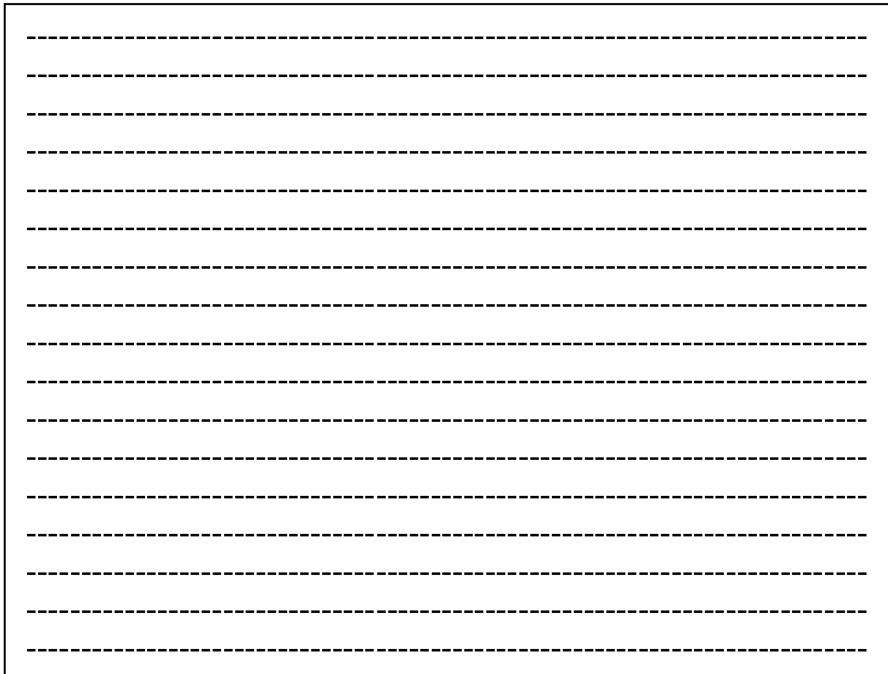
(5) The IT act, convergence, e-governance initiatives, the globalization of the economy, the distinct drive within public and private sector firms for efficiency and the use of technology to achieve these are worst signs.

(6) the basic aims of WTO is to higher growth rate resulting into higher level of financial activity worldwide.

Check your answer with the one provided at the end of the unit.

2.6 Let Us Sum Up

So to wrap up the show, why not you take the initiative to sum the unit in your own words. You can utilize the following space for the same:



2.7 Key words

Globalization is a process by which an activity or undertaking becomes world wide in scope.

Digital Cash arises in an age of remote or anonymous exchange made possible by telecommunication. If I send electronic cash to a location you designate (not necessarily where you are), you send goods to another location I designate (not necessarily where I am), and we both trust the procedure (or protocol) that we go through in effecting this transaction. But however dispersed in space, digital cash transactions--like monetary transactions in general--rely on security, trust, and reliability.

E-commerce refers to anything involving transactions made by exchanging electronic data over telecommunication lines. The monetary basis of electronic commerce can be thought of as an ***electronic check***, which we can define by analogy to an ordinary check. An ordinary check

is a piece of paper with a handwritten signature that is cleared through a third party (bank). In the same way, an electronic check is a computer message with a digital signature that is cleared through a third party. Just as an ordinary check can be sent through the U.S. postal system to another person in payment of a bill, so can an electronic check be sent over a computer network--such as Internet email or the World Wide Web. Just as a physical signature can be verified against a handwritten prototype, so can a digital signature be verified by a mathematical relationship. And just as an ordinary check (or a traveler's check) represents the liability of a bank or company, so does an electronic check represent the liability of a bank or company. As we shall see, what is often called "digital cash" is more properly viewed as an electronic check.

WTO (World Trade Organisation) which was officially launched on January 1, 1995 replaced the GATT to administer a unified package of agreements to which all members are committed. The coverage of WTO includes TRIPS and GATS, etc. under its purview.

2.8 Probable Answers :

SAQI :	i) Globalization	ii)production
	iii) licensing	iv) India/one
SAQII:	i) False	ii)False
	iii)False	iv) False
	v) False	vi)False

2.9 Reflective Questions :

- Discuss the problems of globalization. Suggest some measures to overcome such problems.
- Analyze the importance of globalization in Indian economy. How far they are practicable in Indian situation?
- Establish the problems of implementing Digicash in countries like India.
- Argue on the effectiveness of e-commerce in India.
- Write a seminar paper on the e-commerce entities.

2.10 Suggested Readings for Unit 2 :

- Cherunilam Francis, Business environment, Himalaya Publishing House, New Delhi, (Mill.edn.)
- Ghosh A.; Indian Economy, World press, Calcutta; (2004)
- Dewett K.K., Verma J.D. & Sharma M.L., Indian Economics, S.Chand & Company Ltd., New Delhi
- Chidambaram K; Alagappan ; Business Environment, Vikas Publishing house pvt. Ltd.
- Khan F.A; Business and Society, S.Chand & co., Delhi.
- Visit search engine : www.ask.com
- www.google.com

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