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INDIAN

ECONOMY

CONCEPTS

DAY 46-60

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BASICS OF ECONOMY

National Income Definition

- National income is the total value of a country's final output of all new goods and services produced in one year. However, there are practical difficulties in estimating the national income as per this concept; hence we use the Pigouvian definition.
- A.C. Pigou has in his definition of national income included that income which can be measured in terms of money. In the words of Pigou, "National income is that part of objective income of the community, including the income derived from abroad which can be measured in monetary terms."

National Income Concepts

Gross Domestic Product at Market Prices (GDP_{MP})

- GDP is the market value of all final goods and services produced within a domestic territory of a country measured in a year.
- All production done by the national residents or the non-residents in a country gets included, regardless of whether that production is owned by a local company or a foreign entity.
- Everything is valued at market prices.
- **$GDP_{MP} = C + I + G + X - M$**

GDP at Factor Cost (GDP_{FC})

- GDP at factor cost is gross domestic product at market prices, less net product taxes.
- Market prices are the prices as paid by the consumers Market prices also include product taxes and subsides. The term factor cost refers to the prices of products as received by the producers. Thus, factor cost is equal to market prices, minus net indirect taxes. GDP at factor cost measures money value of output produced by the firms within the domestic boundaries of a country in a year.
- **$GDP_{FC} = GDP_{MP} - NIT$**

Net Domestic Product at Market Prices (NDP_{MP})

- This measure allows policy-makers to estimate how much the country has to spend just to maintain their current GDP. If the country is not able to replace the capital stock lost through depreciation, then GDP will fall.
- **$NDP_{MP} = GDP_{MP} - DEP$**

NDP at Factor Cost (NDP_{FC})

- NDP at factor cost is the income earned by the factors in the form of wages, profits, rent, interest, etc., within the domestic territory of a country.
- **$NDP_{FC} = NDP_{MP}$ -Net Product Taxes-Net Production Taxes**

Gross National Product at Market Prices (GNP_{MP})

- GNP_{MP} is the value of all the final goods and services that are produced by the normal residents of India and is measured at the market prices, in a year.
- GNP refers to all the economic output produced by a nation's normal residents, whether they are located within the national boundary or abroad.
- Everything is valued at the market prices.
- **GNP_{MP}= GDP_{MP} + NFIA**

GNP at Factor Cost (GNP_{FC})

- GNP at factor cost measures value of output received by the factors of production belonging to a country in a year.
- **GNP_{FC} =GNP_{MP} -Net Product Taxes-Net Production Taxes**

Net National Product at Market Prices (NNP_{MP})

- This is a measure of how much a country can consume in a given period of time. NNP measures output regardless of where that production has taken place (in domestic territory or abroad).
- **NNP_{MP} =GNP_{MP} –Depreciation**
- **NNP_{MP}= NDP_{MP}+ NFIA**

NNP at Factor Cost (NNP_{FC})

- NNP at factor cost is the sum of income earned by all factors in the production in the form of wages, profits, rent and interest, etc., belonging to a country during a year.
- It is the National Product and is not bound by production in the national boundaries. It is the net domestic factor income added with the net factor income from abroad.
- **NI =NNP_{MP} - Net Product Taxes-Net Production Taxes**

GVA at basic prices

- GVA_{MP} - Net Product Taxes

GVA at factor cost

- GVA at basic prices - Net Production Taxes

Three Measurements of National Income

- National Income calculated by three ways:
- Consider the following while calculating National Income through:

Value Added Method (or the Product Method)

- The value added or production method is used by economists to calculate GDP at market prices, which is the total values of outputs produced at different stages of production. It needs to be mentioned that caution should be taken to take final Goods and not Intermediate goods, as it will result in Double Counting.
- Some of the goods and services included in production are:
  - Goods and services actually sold in the market.
  - Goods and services not sold but supplied free of cost. (No Charge/Complementary
- Some of the goods and services not included in production are:
  - Second hand items and purchase and sale of the same. Sale and purchase of second cars, for example, are not a part of GDP calculation as no new production takes place in the economy.
  - Production due to unwarranted/ illegal activities.
  - Non-economic goods or natural goods such as air and water.

- Transfer Payments such as scholarships, pensions etc. are excluded as there is income received, but no good or service is produced in return.
- Imputed rental for owner-occupied housing is also excluded

Income Method

- This method emphasises on aggregating the payments made by firms to households, called factor payments.
- It is defined as total income earned by citizens and businesses of a country. There are four types of factors of production and four types of factor incomes accordingly i.e. Land, Labour, Capital and Entrepreneur/Organization as Factors of Production and Rent, Wages, Interest and Profit as Factor Incomes correspondingly.
- GDP = Wages+ Interest Income + Rental Income +Profit +Indirect Taxes-Subsidies+ Depreciation
- The term Profit can be further sub-divided into: profit tax; dividend to all those shareholders; and retained profit (or retained earnings).
- Such an approach is adopted in India to calculate the contribution of services sector to the economy.
- Any income corresponding to which there is no flow of goods and services or value added, it should not be included in calculation by Income method.

Expenditure Method

- The expenditure method measures the final expenditure on GDP. Amount of Expenditure refers to all spending on currently-produced final goods and services only in an economy. In an economy, there are three main agencies, which buy goods and services. These are: Households, Firms and the Government
- This final expenditure is made up of the sum of four expenditure items, namely:
- **Consumption (C):** Personal Consumption made by households, the payment of which is paid by households directly to the firms which produced the goods and services desired by the households.
- **Investment Expenditure (I):** Investment is an addition to capital stock of an economy in a given time period. This includes investments by firms as well as governments sectors
- **Government Expenditure (G):** This category includes the value of goods and service purchased by Government. Government expenditure on pension schemes, scholarships, unemployment allowances etc. are not included in this as all of them come under transfer payments.
- **Net Exports (X-IM):** Expenditure on foreign made products (Imports) are expenditure that escapes the system, and must be subtracted from total expenditures. In turn, goods produced by domestic firms which are demanded by foreign economies involve expenditure by other economies on our production (Exports), and are included in total expenditure. The combination of the two gives Net Exports.
  - **GDP= C+I+G+X-IM C = consumption**
  - I = Investment
  - G = Government expenditure
  - X = Export
  - IM = Import

What are the factors that affect National Income?

- Several factors affect the national income of a country. Some of them have been listed below:

Factors of Production

- Normally, the more efficient and richer the resources, higher will be the level of National Income or GNP.

- **Land**
  - Resources like coal, iron and timber are essential for heavy industries so that they must be available and accessible. In other words, the geographical location of these natural resources affects the level of GNP.
- **Capital**
  - Capital is generally determined by investment. Investment in turn depends on other factors like profitability, political stability, etc.
- **Labour**
  - The quality or productivity of human resources is more important than quantity. Manpower planning and education affect the productivity and production capacity of an economy.
- **Entreprise**
  - The size of the national income also greatly depends upon the number and skill of the entrepreneurs. If the captains of the industries! are efficient, they will combine; the various factors of production to the optimum proportion and so the volume of total production will be quite large, if managerial skill is lacking in the country, the size of the national income will be small.
- **Technology**
  - This factor is more important for Nations with fewer natural resources. The development in technology is affected by the level of invention and innovation in production.
- **Government**
  - Government can help to provide a favourable business environment for investment. It provides law and order, regulations.
- **Political Stability**
  - A stable economy and political system helps in appropriate allocation of resources. Wars, strikes and social unrests will discourage investment and business activities.

New Methodology for Calculation of GDP in India

- Earlier domestic GDP was calculated at factor or basic cost, which took into account prices of products received by producers.
- The new formula takes into account market prices paid by consumers. It is calculated by adding GDP at factor price and indirect taxes (minus subsidies). It is in line with international practice and is expected to better capture the changing structure of the Indian economy.
- The government has also changed the base year for estimating GDP from 2004-05 to 2011-12. This has been done to incorporate the changing structure of the economy, especially rural India.
- Data for the new GDP series will now be collected from 5 lakh companies (against 2,500 companies earlier). Under-represented and informal sectors as well as items such as smartphones and LED television sets will now be taken into account to calculate the gross domestic product.

Green GDP

- Green GDP is a term used generally for expressing GDP after adjusting for environmental damage. When information on economy’s use of the natural environment is integrated into the system of national accounts, it becomes green national accounts or environmental accounting.
- The process of environmental accounting involves three steps viz. Physical accounting; monetary valuation; and integration with national Income/wealth Accounts. Physical accounting determines the state of the resources, types, and extent (qualitative and quantitative) in spatial and temporal terms. Monetary valuation is done to determine its tangible and intangible components. Thereafter, the net change in natural resources in monetary terms is integrated into the Gross Domestic Product in order to reach the value of Green GDP.

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BANKING SECTOR

A bank is a financial institution that accepts deposits from the public and creates credit. Lending activities can be performed either directly or indirectly through capital markets.

Due to their importance in the financial stability of a country, banks are highly regulated in most countries.

Most nations have institutionalized a system known as fractional reserve banking under which banks hold liquid assets equal to only a portion of their current liabilities.

In addition to other regulations intended to ensure liquidity, banks are generally subject to minimum capital requirements based on an international set of capital standards, known as the Basel Accords.

Types of Banking

- **Retail banks** deal specifically with retail consumers. These banks offer services to the general public and are also called personal or general banking institutions. Retail banks provide services such as checking and savings accounts, loan and mortgage services, financing for automobiles, and short-term loans like overdraft protection. Most retail banks also offer credit card services to their customers, and may also supply their clients with foreign currency exchange. These banks also cater to high-net-worth individuals, giving them specialty services such as private banking and wealth management. Examples of retail banks include TD Bank and Citibank.
- **Commercial or corporate banks** provide specialty services to their business clients from small business owners to large, corporate entities. Along with day-to-day business banking, these banks also provide their clients with other things such as credit services, cash management, commercial real estate services, employer services, and trade finance. JP Morgan Chase and Bank of America are two popular examples of commercial banks.
- **Investment banks** focus on providing corporate clients with complex services and financial transactions such as underwriting and assisting with merger and acquisition (M&A) activity. As such, they are known primarily as financial intermediaries in most of these transactions. Clients commonly range from large corporations, other financial institutions, pension funds, governments, and hedge funds. Morgan Stanley and Goldman Sachs are examples of U.S. investment banks.

Reserve Bank of India

- The Reserve Bank of India (RBI) is the central bank of India, which was established on **April 1, 1935, under the Reserve Bank of India Act.**
- The Reserve Bank of India uses **monetary policy to create financial stability** in India, and it is charged with **regulating the country's currency and credit systems**.
- **Located in Mumbai**, the RBI serves the financial market in many ways. The bank sets the overnight interbank lending rate. The Mumbai Interbank Offer Rate (MIBOR) serves as a benchmark for interest rate–related financial instruments in India.
- The main purpose of the RBI is to conduct **consolidated supervision of the financial sector** in India, which is made up of commercial banks, financial institutions, and non-banking finance firms.
- Initiatives adopted by the RBI include **restructuring bank inspections, introducing off-site surveillance of banks and financial institutions, and strengthening the role of auditors**.

- First and foremost, the **RBI formulates, implements, and monitors India's monetary policy**. The bank's management objective is to **maintain price stability and ensure that credit is flowing to productive economic sectors.**
- The RBI also manages all foreign exchange under the **Foreign Exchange Management Act of 1999.**
- This act allows the RBI **to facilitate external trade** and payments to promote the development and health of the foreign exchange market in India.
- The RBI acts as a **regulator and supervisor** of the **overall financial system**.
- This **injects public confidence** into the national financial system, protects interest rates, and provides positive banking alternatives to the public.
- Finally, the RBI acts as the **issuer of national currency**.
- For India, this means that currency is either issued or destroyed depending on its fit for current circulation. This provides the Indian public with a supply of currency in the form of dependable notes and coins, a lingering issue in India.
- In 2018 the RBI **banned the use of virtual currencies by the financial agencies** and banks that it regulates.

Commercial Bank

- A commercial bank is a type of financial institution that accepts deposits, offers checking account services, makes various loans, and offers basic financial products like certificates of deposit (CDs) and savings accounts to individuals and small businesses. A commercial bank is where most people do their banking, as opposed to an investment bank.
- Commercial banks make money by providing loans and earning interest income from those loans. The types of loans a commercial bank can issue vary and may include mortgages, auto loans, business loans, and personal loans. A commercial bank may specialize in just one or a few types of loans.
- Customer deposits, such as checking accounts, savings accounts, money market accounts, and CDs, provide banks with the capital to make loans. Customers who deposit money into these accounts effectively lend money to the bank and are paid interest. However, the interest rate paid by the bank on money they borrow is less than the rate charged on money they lend.

Non-Banking Financial Companies

- Non-banking financial companies (NBFCs) are financial institutions that offer various banking services but do not have a banking license. Generally, these institutions are not allowed to take traditional demand deposits—readily available funds, such as those in checking or savings accounts—from the public. This limitation keeps them outside the scope of conventional oversight from federal and state financial regulators.
- NBFCs can offer banking services such as loans and credit facilities, currency exchange, retirement planning, money markets, underwriting, and merger activities.
- NBFCs are officially classified under the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act. The Act describes them as companies "predominantly engaged in a financial activity" when more than 85% of their consolidated annual gross revenues or consolidated assets are financial in nature.
- This classification technically encompasses a wide range of companies offering bank-like financing and investing services. Examples of NBFCs include insurance companies, money market funds, asset managers, hedge funds, private equity firms, mobile payment systems, micro-lenders, and peer-to-peer lenders.

What is difference between banks & NBFCs?

NBFCs lend and make investments and hence their activities are akin to that of banks; however there are a few differences as given below:

- NBFC cannot accept demand deposits;
- NBFCs do not form part of the payment and settlement system and cannot issue cheques drawn on itself;
- Deposit insurance facility of Deposit Insurance and Credit Guarantee Corporation is not available to depositors of NBFCs, unlike in case of banks.

What are the different types/categories of NBFCs registered with RBI?

Within the broad categorization the different types of NBFCs are as follows:

- Asset Finance Company (AFC)
- Investment Company (IC)
- Loan Company (LC)
- Infrastructure Finance Company (IFC)
- Systemically Important Core Investment Company (CIC-ND-SI)
- Infrastructure Debt Fund: Non- Banking Financial Company (IDF-NBFC)
- Non-Banking Financial Company - Micro Finance Institution (NBFC-MFI)
- Non-Banking Financial Company – Factors (NBFC-Factors)
- Mortgage Guarantee Companies (MGC)
- NBFC- Non-Operative Financial Holding Company (NOFHC)

NABARD

- In NABARD the majority stake is held by the Reserve Bank. NABARD is an apex Development Bank with a mandate for:
  - Facilitating credit flow for promotion and development of agriculture, small-scale industries, cottage and village industries, handicrafts and other rural crafts.
  - Support all other allied economic activities in rural areas, promote integrated and sustainable rural development and secure prosperity of rural areas.
- NABARD acts as a regulator for co-operative banks and Regional Rural Banks (RRBs).
- NABARD also helps incapacity building of partner agencies and development institutions.
- NABARD provide facilities for training, for dissemination of information and the promotion of research including the undertaking of studies, researches, techno-economic and other surveys in the field of rural banking, agriculture and rural development. It provides technical, legal, financial, marketing and administrative assistance to any person engaged in agriculture and rural development activities.

National Housing Bank:

- National Housing Bank (NHB), a wholly owned subsidiary of Reserve Bank of India (RBI), was set up on 9 July 1988 under the National Housing Bank Act, 1987.
- NHB is an apex financial institution for housing. NHB has been established with an objective to operate as a principal agency to promote housing finance institutions both at local and regional levels and to provide financial and other support incidental to such institutions and for matters connected therewith.
- NHB registers, regulates and supervises Housing Finance Company (HFCs), keeps surveillance through On-site & Off-site Mechanisms and co-ordinates with other Regulators.

Small Industries Development Bank of India (SIDBI)

- Small Industries Development Bank of India (SIDBI) is a development financial institution in India, headquartered at Lucknow and having its offices all over the country.

- Its purpose is to provide refinance facilities and short term lending to industries, and serves as the principal financial institution in the Micro, Small and Medium Enterprises (MSME) sector.
- SIDBI also coordinates the functions of institutions engaged in similar activities. SIDBI operates under the Department of Financial Services, Government of India.
- SIDBI is one of the four All India Financial Institutions regulated and supervised by the Reserve Bank; other three are EXIM Bank, NABARD and NHB. They play a salutary role in the financial markets through credit extension and refinancing operation activities and cater to the long-term financing needs of the industrial sector.
- SIDBI is active in the development of Micro Finance Institutions through SIDBI Foundation for Micro Credit, and assists in extending microfinance through the Micro Finance Institution (MFI) route. Its promotion & development program focuses on rural enterprises promotion and entrepreneurship development.

Micro Units Development and Refinance Agency Bank (MUDRA Bank):

- It is a public sector financial institution in India. It provides loans at low rates to micro-finance institutions and non-banking financial institutions which then provide credit to MSMEs.
- The Industrial Investment Bank of India (IIBI) The Industrial Investment Bank of India was a 100% government of India-owned financial investment institution.
- It was established in 1971 by resolution of the Parliament of India u/s 617 of the Companies Act.
- The bank was headquartered at Kolkata and had presence in New Delhi, Mumbai, Chennai, Bengaluru, Ahmedabad and Guwahati.
- The Industrial Reconstruction Corporation of India Ltd., set up in 1971 for rehabilitation of sick industrial companies, was reconstituted as Industrial Reconstruction Bank of India in 1985 under the IRBI Act, 1984.
- With a view to converting the institution into a full-fledged development financial institution, IRBI was incorporated under the Companies Act 1956, as Industrial Investment Bank of India Ltd. (IIBI) in March 1997.
- IIBI offered a wide range of products and services, including term loan assistance for project finance, short duration non-project asset-backed financing, working capital/other short-term loans to companies, equity subscription, asset credit, equipment finance and investments in capital market and money market instruments.
- In 2005, a merger of IIBI, IDBI and IFCI was considered, but IIBI refused and it was decided in 2006-2007 to close the bank.
- As of 2011, the bank operated from its sole remaining office in Kolkata.
- Deloitte and Touché was appointed to dispose of IIBI’s Non-Performing assets. The bank’s closure was announced in the Budget 2012.

IFCI

- IFCI, previously Industrial Finance Corporation of India, is a Non-Banking Finance Company in the public sector.
- Established in 1948 as a statutory corporation, IFCI is currently a company listed on BSE and NSE.
- IFCI manages seven numbers of subsidiaries and one associate under its fold.
- It provides financial support for the diversified growth of Industries across the spectrum.
- The financing activities cover various kinds of projects such as airports, roads, telecom, power, real estate, manufacturing, services sector and such other allied industries.
- The company has played a pivotal role in setting up various market intermediaries of repute in several niche areas like stock exchanges, entrepreneurship development organizations, consultancy organizations, educational and skill development institutes across the length and breadth of the country.

Export-Import Bank of India:

- Export–Import Bank of India is the premier export finance institution in India, established in 1982 under Export-Import Bank of India Act 1981.
- Since its inception, Exim Bank of India has been both a catalyst and a key player in the promotion of cross border trade and investment.
- Commencing operations as a purveyor of export credit, like other export credit agencies in the world, Exim Bank India has, over the period, evolved into an institution that plays a major role in partnering Indian industries, particularly the Small and Medium Enterprises, in their globalization efforts, through a wide range of products and services offered at all stages of the business cycle, starting from import of technology and export product development to export production, export marketing, pre-shipment and post-shipment and overseas investment.

Co-operative banks:

- Co-operative banks are small-sized units organized in the co-operative sector which operate both in urban and non-urban centers.
- Co-operative Banks in India are registered under the Co-operative Societies Act.
- The cooperative bank is also regulated by the RBI.
- They are governed by the Banking Regulations Act 1949 and Banking Laws (Co-operative Societies) Act, 1965.
- Cooperative Banks in India have become an integral part of the success of Indian Financial Inclusion story.
- They have achieved many landmarks since their creation and have helped a normal rural Indian to feel empowered and secure. The story has not been smooth and has its share of procedural glitches and woes placed at various pockets

Extent of Cooperative Banking

- Indian cooperative structures are one of the largest such networks in the world with more than 200 million members. It has about 67% penetration in villages and fund 46% of the total rural credit. It also stands for 36% of the total distribution of rural fertilizers and 28% of rural fair price shops.

Structure of Cooperative Banking in India

- The structure of cooperative network in India can be divided into 2 broad segments-
  - Urban Cooperative Banks
  - Rural Cooperatives

Urban Cooperatives

- Urban Cooperatives can be further divided into scheduled and non-scheduled.
- Both the categories are further divided into multi-state and single-state.
- Majority of these banks fall in the non-scheduled and single-state category.
- Banking activities of Urban Cooperative Banks are monitored by RBI.
- Registration and Management activities are managed by Registrar of Cooperative Societies (RCS).
- These RCS operate in single-state and Central RCS (CRCS) operate in multiple state.

Rural Cooperatives

- The rural cooperatives are further divided into short-term and long-term structures.
- The short-term cooperative banks are three tiered operating in different states. These are
  - State Cooperative Banks- They operate at the apex level in states

- District Central Cooperative Banks-They operate at the district levels
- Primary Agricultural Credit Societies-They operate at the village or grass-root level.

- Likewise, the long-term structures are further divided into –
  - State Cooperative Agriculture and Rural Development Banks (SCARDS) - These operate at state-level.
  - Primary Cooperative Agriculture and Rural Development Banks (PCARDBS)-They operate at district/ block level.
- The rural banking cooperatives have a complex monitoring structure as they have a dual control which has led to many problems. A Forum called State Level Task Force on Cooperative Urban Banks (TAFCUB) has been set-up to look into issues related to duality in control.
  - All banking activities are regulated by a shared arrangement between RBI and NABARD.
  - All management and registration activities are managed by RCS

Public Sector Bank recapitalization

- The Government approved to provide an additional amount of Rs. 6000 crore, in addition to the Rs. 15000 crore already provided in the Budget 2010-11, to ensure Tier I CRAR (Capital to Risk Weighted Assets) of Public Sector Banks (PSBs) and also to raise Government of India holding in all PSBs to 58%. The proposed capital infusion would enhance the lending capacity of the PSBs to meet the credit requirement of the economy in order to maintain and accelerate the economic growth momentum. This additional, availability of capital is likely to benefit employment oriented sectors, especially agriculture, micro & small enterprises, export, entrepreneurs etc.
- During the recent global financial crisis, the Public Sector Banks (PSBs) played a pivotal role in the economy by extending credit to all the productive sectors of the economy. These banks, in this backdrop, would require capital commensurate with the increase in there. Risk Weighted Assets (RWAs). Though the minimum regulatory requirement of Capital to Risk Weighted Assets (CRAR) for the banks is 9%, the Government has mandated a total CRAR of 12% with 8% Tier I Capital. Keeping, all other factors, the Finance Minister, in his Budget speech for the year 2010-11 announced that capital would be infused in the PSBs so that these are able to attain a minimum & percent Tier I Capital by 31st March, 2011.
- There are many PSBs where the Government of India’s holding is close to 51%. This implies that in case of need, these banks cannot access the capital market for raising additional capital by dilution of Government holding. The present capitalization process of the PSBs has presented an opportunity to the Government to raise its shareholding in the PSBs, especially in those PSBs where the Government’s holding is close to 51%. This will enable the PSBs to raise additional capital from the market, in future, without depending upon the Government.
- Recapitalization is a process of changing a firm’s capital structure by altering the mix of debt and equity financing without changing the total amount of capital.

Differential Banks

Small Finance Banks and Payment Banks Criteria

- The Reserve Bank of India (RBI) issues licenses to entities to carry on the business of banking and other business in which banking companies may engage, as defined and described in Sections 5 (b) and 6 (1) (a) to (o) of the Banking Regulation Act, 1949, respectively.
- RBI has come up with guidelines for two new categories of banks- **‘small and payments banks’** and states that these can improve financial inclusion.

Small Finance Banks

- The objectives of setting up of small finance banks will be to further financial inclusion by (a) provision of savings vehicles, and (ii) supply of credit to small business units; small and marginal farmers; micro and small industries; and other unorganized sector entities, through high technology-low cost operations.

- Eligible Promoters: Resident individuals/professionals with 10 years of experience in banking and finance; and companies and societies owned and controlled by residents will be eligible to set up small finance banks. Existing Non-Banking Finance Companies (NBFCs), Micro Finance Institutions (MFIs), and Local Area Banks (LABs) that are owned and controlled by residents can also opt for conversion into small finance banks. Promoter/promoter groups should be 'fit and proper' with a sound track record of professional experience or of running their businesses for at least a period of five years in order to be eligible to promote small finance banks.

Payment Banks:

- The primary objective of setting up of Payments Banks will be to further financial inclusion by providing (i) small savings accounts and (ii) payments / remittance services to migrant labour workforce, low income households, small businesses, other unorganised sector entities and other users, by enabling high volume low value transactions in deposits and payments / remittance services in a secured technology-driven environment.

Registration, Licensing and Regulations

- The Payments Bank will be registered as a public limited company under the Companies Act, 2013, and licensed under Section 22 of the Banking Regulation Act, 1949, with specific licensing conditions restricting its activities to acceptance of demand deposits and provision of payments and remittance services.

Eligibility Criteria

- The existing non-bank PPI issuers authorized under the Payment and Settlement Systems Act, 2007 (PSS Act) and other entities such as Non-Banking Finance Companies (NBFCs), corporate BCs, mobile telephone companies, super-market chains, companies, real sector cooperatives and public sector entities may apply to set up a Payments Bank. Even banks can take equity stake in a Payments Bank to the extent permitted under Section 19 (2) of the Banking Regulation Act, 1949.

Scope of Activities

- The Payments Bank will be set up as a differentiated bank and shall confine its activities to further the objectives for which it is set up. Therefore, the Payments Bank would be permitted to undertake only certain restricted activities permitted to banks under the Banking Regulation Act, 1949, as given below:
- Acceptance of demand deposits, i.e., current deposits, and savings bank deposits. The eligible deposits mobilized by the Payments Bank would be covered under the deposit insurance scheme of the Deposit Insurance and Credit Guarantee Corporation of India (DICGC). Given that their primary role is to provide payments and remittance services and demand deposit products to small businesses and low-income households, Payments Banks will initially be restricted to holding a maximum balance of Rs. 100,000 per customer.
- Payments and remittance services through various channels including branches, BCs and mobile banking. The payments remittance services would include acceptance of funds at one end through various channels including branches and BCs and payments of cash at the other end, through branches, BCs, and Automated Teller Machines (ATMs). Cash-out can also be permitted at Point-of Sale terminal locations as per extant instructions issued under the PSS Act. In the case of walk-in customers, the bank should follow the extant KYC guidelines issued by the RBI.
- Issuance of PPIs as per instructions issued from time to time under the PSS Act.
- **Internet banking** - The RBI is also open to applicants transacting primarily using the Internet. The Payments Bank is expected to leverage technology to offer low cost banking solutions. Such a bank should ensure that it has all enabling systems in place including business partners, third party service providers and risk managements systems and controls to enable offering transactional services on the internet. While offering such services, the Payments Bank will be required to comply with RBI instructions on information security, electronic banking, technology risk management and cyber frauds.

- FunctiowRs 20,000 crore would be injected in a month. Over the next four years, the government plans to inject Rs 70,000 crore.
  - **De-stressing:** The government will concentrate on distressing the banks' bad loans.
  - **Empowerment:** The government will strive to make it easier for PSBs to hire. The government is looking at introducing Employee Stock Ownership Plan (ESOPs) for the PSU bank managements.
  - **Framework of Accountability:** The government also announced a new framework of key performance indicators for state-run lenders to boost efficiency in functioning while assuring them of independence in decision making on purely commercial considerations.
  - **Governance Reforms:** The process of governance reforms started with "Gyan Sangam" - a conclave of PSBs and FIs organized at the beginning of 2015 in Pune which was attended by all stake-holders including Prime Minister, Finance Minister, MoS (Finance), Governor, RBI and CMDs of all PSBs and FIs. There was focus group discussion on six different topics which resulted in specific decisions on optimizing capital, digitizing processes, strengthening risk management, improving managerial performance and financial inclusion.

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MONETARY POLICY

- Monetary Policy refers to the measures pertaining to policy undertaken by the Central Bank (RBI) to influence the availability; determine the size and rate of growth of the money supply in the economy.
- In other words, monetary policy can be defined as a process of managing a nation's money supply to contain/control the inflation, achieving higher growth rates and achieving full employment.
- Generally, all across the globe, monetary policy is announced by the central banking body of the country, for example the RBI announces it in India. India entered into the era of economic planning in 1951.
- The Monetary and Fiscal Policies had to be adjusted to the requirements of the planned development in the country and accordingly, the economic policy of the Reserve Bank was emphasized on two objectives:
  - To speed up the economic development of the nation and raise the national income and standard of living of the people.
  - Control and reduce the "Inflationary" pressure on the economy.

Monetary policy is of two kinds:

- **Expansionary Monetary Policy:** It increases the supply of money in an economy by making credit supply easily available. Money produced through such a policy is called as cheap money. An expansionary monetary policy is required when an economy goes through a phase of recession accompanied by lower levels of growth/high levels of unemployment. But risk associated with EMP is inflation.
- **Contractionary Monetary Policy:** It decreases the supply of money in the economy. Contractionary monetary is used to tackle the menace of inflation in the economy by raising the interest rates.

Objectives of Monetary Polity

- In India, as defined by former RBI governor C. Rangarajan, broad objectives of monetary policy are:
  - To regulate monetary expansion so as to maintain a reasonable degree of price stability; and
  - To ensure adequate expansion in credit to assist economic growth
- Further the objectives of Monetary Policy are:
  - **It leads to economic growth**: The monetary policy can influence economic growth by controlling real interest rates and its resultant impact on the investment. If the RBI opts for a cheap credit policy by reducing interest rates, the investment level in the economy can be encouraged. This increased investment can speed up economic growth.
  - **Price Stability:** Inflation and deflation both are not suitable for an economy. Price stability is defined as a low and stable order of inflation. Thus, the monetary policy having an objective of price stability tries to keep the value of money stable.

- **Exchange Rate Stability:** If exchange rate of an economy is stable it shows that economic condition of the country is stable. Monetary policy aims at maintaining the relative stability in the exchange rate. The RBI by altering the foreign exchange reserves tries to influence the demand for foreign exchange and tries to maintain the exchange rate stability.
- **It generates employment:** Monetary policy can be used for generating employment. If the monetary policy is expansionary then credit supply can be encouraged. It would thus help in creating more jobs in different sector of the economy.
- **Equitable distribution of income:** Earlier many economists used to justify the role of the fiscal policy in maintaining economic equality. However, in recent years economists have given the opinion that the monetary policy can play a supplementary role in attainting economic equality.

Methods for Regulation of Monetary Policy

- The methodology can be classified into two categories:

Quantitative Credit Control Methods:

- These are the instruments of monetary policy that affect over all supply of money/credit in the economy. Some are as follows:

Statutory Liquidity Ratio:

- The Statutory Liquidity Ratio refers to that proportion of total deposits which the commercial banks are required to keep with themselves in a liquid form. The commercial banks generally make use of this money to purchase the government securities.
- Thus, the Statutory Liquidity Ratio, on the one hand, is used to siphon off the excess liquidity of the banking system, and on the other, it is used to mobilize revenue for the government.
- The Reserve Bank of India is empowered to raise this ratio up to 40 per cent of aggregate deposits of commercial banks. At present it is 18.5 per cent. It used to be as high as 38.5 percent at one point of time.

Cash Reserve Ratio:

- The Cash Reserve Ratio (CRR) is the ratio fixed by the RBI of the total deposits of a bank in India, which is kept with the RBI in cash form.
- CRR deposits do not earn any interest for banks.
- Initially, limits of 4% (lower) and 20% (upper) were set for CRR, but respective amendments removed the limits, therefore providing RBI with much needed operational flexibility. The more the CRR the less the money available for lending by the banks to players in the economy. RBI increases CRR to tighten many supple and lowers CRR to expand credit in the economy.
- CRR as a tool of monetary policy is used when there is a relatively serious need to manage credit and inflation.
- Otherwise, RBI relies on signaling its intent through the policy rates of repo and reverse repo. At present it is 4 percent.

Bank Rate:

- In basic terms, bank rate is the interest rate at which RBI provides long term credit facility to commercial banks. A change in bank rate affects the other market rates of interest. An increase in bank rate leads to an increase in other rates of interest, and conversely, a decrease in bank rate results in a fall in other rates of interest. Bank rate is also referred to as the discount rate. A deliberate manipulation of the bank rate by the Reserve Bank to influence the flow of credit created by the commercial banks is known as bank rate policy.
- An increase in bank rate results in an increase in the cost of credit or cost of borrowing. This in turn leads to a contraction in demand for credit. A contraction in demand for credit restricts the total

availability of money in the economy, and hence results as an anti-inflationary measure of control.

- Likewise, a fall in the bank rate causes other rates of interest to come down. The cost of credit falls, i.e., borrowing becomes cheaper. Cheap credit may induce a higher demand both for investment and consumption purposes. More money through increased flow of credit comes into circulation. A fall in bank rate may, thus, prove an anti-deflationary instrument of control. Penal rates are linked with Bank Rates. For instance if a bank does not maintain the required levels of CRR and SLR, then RBI can impose penalty on such banks. Currently Bank Rate is 7%.
- Nowadays, bank rate is not used as a tool to control money supply, rather Liquidity Adjustment Facility (LAF) (Repo Rate) is used to control the money supply in economy.

Repo Rate:

- If the RBI wants to make it more expensive for the banks to borrow money, it increases the repo rate.
- Similarly, if RBI wants to make it cheaper for banks to borrow money, it reduces the repo rate. Repo rate stood at 5.75%.

Reverse Repo Rate:

- Reverse Repo is the rate at which the Central Bank (RBI) borrows from the market. This is called as reverse repo as it the reverse of repo operation. Reverse repo rate at present is 50 basis points (or 0.5%) lower than the Repo Rate. Repo and Reverse
- Repo Rates are also referred to as the Policy rates and are often used by the Central Bank (RBI) to send single to the financial system to adjust their lending and borrowing operations.
- Repo rates and reverse repo rates form a part of the liquid adjustment facility.

Open Market Operations (OMOs):

- It refers to buying and selling of government securities in open market in order to expand or contract the amount of money in the banking system. This technique is superior to bank rate policy. Purchases inject money into the banking system while sale of securities do the opposite.
- It is a common misconception that OMOs change the total stock of government securities, but in reality they only change the proportion of Government Securities held by the RBI, commercial and co-operative banks.
- The Reserve Bank of India has frequently resorted to the sale of government securities to which the commercial banks have been generously contributing. Thus, open market operations in India have served, on the one hand as an instrument to make available more budgetary resources and on the other as an instrument to siphon off the excess liquidity in the system.

Marginal Standing Facility:

- Marginal Standing Facility is a liquidity support arrangement provided by RBI to commercial banks if the latter doesn't have the required eligible securities above the SLR limit.
- It is a window for banks to borrow from the Reserve Bank of India in an emergency situation when inter-bank liquidity dries up completely.
- The MSF was introduced by the RBI in its monetary policy for 2011-12.
- Under MSF, a bank can borrow one-day loans from the RBI, even if it doesn't have any eligible securities excess of its SLR requirement (maintains only the SLR). This means that the bank can't borrow under the repo facility.
- In the case of MSF, the bank can borrow up to 1% (can be changed by the RBI) below the SLR (means 1% of Net Demand and Time Liabilities or liabilities simply).
- The working of MSF is thus related with SLR. For example, imagine that a bank has securities holding of just 19.5 % (of NDTL). This is equal to its mandatory SLR holding. The bank can't borrow using the repo facility. But as per the MSF, the bank can borrow 1 % of its liabilities from the RBI. Sometimes

the RBI increases the limit of borrowings to 2% of NDTL. As in the case of repo, the bank has to mortgage the securities with the RBI.

- MSF rate and the Repo rate: The bank has to give higher interest rate to the RBI. The interest rate for MSF borrowing was originally set at one percent higher than the repo rate. As on November 2017, the RBI has lowered the difference between repo rate and MSF to 0.25%. The MSF rate and Bank rate are equal.

Qualitative Credit Control Methods

- These are those tools through which the Central Bank not only controls the value of loans but also the purpose for which these loans are assigned by the commercial banks. Some of these are:

Moral Suasion:

- Moral suasion means persuasion and request. To arrest inflationary situation Central Bank persuades and requests the commercial banks to refrain from giving loans for speculative and non-essential purposes. On the other hand, to counter deflation Central Bank persuades the commercial banks to extend credit for different purposes.
- Under Moral Suasion, RBI issues periodical letters to bank to exercise control over credit in general or advances against particular commodities.
- Periodic discussions are held with authorities of commercial banks in this respect.
- In India, from 1949 onwards the Reserve Bank has been successful in using the method of moral suasion to bring the commercial banks to fall in line with its policies regarding credit.

Rationing of credit:

- Rationing of credit is a method by which the Reserve Bank seeks to limit the maximum amount of loans and advances, and also in certain cases fix ceiling for specific categories of loans and advances. RBI also makes credit flow to certain priority or weaker sectors by charging concessional rates of interest. This is at times also referred to as Priority Sector Lending.

Regulation of Consumer Credit:

- Now-a-days, most of the consumer durables like Cars, Televisions, and Laptops, etc. are available on installment basis financed through bank credit. Such credit made available by commercial banks for the purchase of consumer durables is known as consumer credit.
- If there is excess demand for certain consumer durables leading to their high prices, Central Bank can reduce consumer credit by (a) increasing down payment, and (b) reducing the number of installments of repayment of such credit.
- On the other hand, if there is deficient demand for certain specific commodities causing deflationary situation, Central Bank can increase consumer credit by (a) reducing down payment and (b) increasing the number of installments of repayment of such credit.

Direct action:

- This method is adopted when a commercial bank does not co-operate with the central bank in achieving its desirable objectives. Direct action may be as:
  - Central banks may charge a penal rate of interest over and above the bank rate upon the defaulting banks;
  - Central bank may refuse to rediscount the bills of those banks which are not following its directives;
  - Central bank may refuse to grant further accommodation to those banks whose borrowings are in excess of their capital and reserves.

Margin Requirements:

- Generally, commercial banks give loan against ‘stocks or ‘securities’. While giving loans against stocks or securities they keep margin. Margin is the difference between the market value of a security and its maximum loan value. Let us assume, a commercial bank grants a loan of Rs. 8000 against a security worth Rs. 10,000. Here, margin is Rs. 2000 or 20%.

- If central bank feels that prices of some goods are rising due to the speculative activities of businessmen and traders of such goods, it wants to discourage the flow of credit to such speculative activities. Therefore, it increases the margin requirement in case of borrowing for speculative business and thereby discourages borrowing. This leads to reduction is money supply for undertaking speculative activities and thus inflationary situation is arrested.

Limitations of Monetary Policy

- The monetary policy of Reserve bank has played only a limited role in controlling the inflationary pressure. It has not succeeded in achieving the objective of growth with stability.
- The existence of black money in the economy limits the working of the monetary policy. Black money is not recorded since the borrowers and lenders keep their transactions secret.
- Informal money lenders on a large scale in countries like India but they are not under the control of the monetary authority. This factor limits the effectiveness of monetary policy in such countries.
- An important limitation of monetary policy arises from its conflicting objectives. To achieve the objective of economic development, the monetary policy is to be expansionary but contrary to it is to achieve the objective of price stability and curb on inflation. It can be realized by contracting the money supply. The monetary policy generally fails to achieve a proper coordination between these two objectives.
- Another limitation of monetary policy in India is underdeveloped money market. The weak money market limits the coverage, as also the efficient working of the monetary policy.

Monetary Policy Committee

- The Monetary Policy Committee (MPC) is a committee of the Central Bank in India (Reserve Bank of India), headed by its Governor, which is entrusted with the task of fixing the benchmark policy interest rate (repo rate) to contain inflation within the specified target level.
- The MPC replaces the current system where the RBI governor, with the aid and advice of his internal team and a technical advisory committee, has complete control over monetary policy decisions.
- A Committee-based approach will add lot of value and transparency to monetary policy decisions.
- Prior to MPC, the RBI governor, with the aid and advice of his internal team and a technical advisory committee, had complete control over monetary policy decisions. This lacked clear objective, accountability and transparency in decision making.
- All the important committees of namely the Y. V. Reddy Committee (2002), Tarapore Committee (in 2006), Percy Mistry Committee (2007), Raghuram Rajan Committee (2009), Dr. Urjit R. Patel (URP) Committee (2013) (discussed below) recommended for a MPC to decide policy actions.
- They all opinioned that "Heightened public interest and scrutiny of monetary policy decisions and outcomes has propelled a worldwide movement towards a committee based approach to decision making with a view to bringing in greater transparency and accountability in India.
- Monetary Policy Committee (MPC) as a statutory committee of the Central Bank in India (Reserve Bank of India), headed by its Governor, which is entrusted with the task of fixing the benchmark policy interest rate (repo rate) to contain inflation within the specified target level. The MPC replaces the current system.
- The MPC will have six members; - the RBI Governor (Chairperson), the RBI Deputy Governor in charge of monetary policy, one official nominated by the RBI Board and the remaining three members would represent the Government of India. These Government of India nominees are appointed by the Central Government based on the recommendations of a search cum selection committee
- Government nominees of the MPC will hold office for a period of four years and will not be eligible for re-appointment. These three central government nominees in MPC are mandated to be persons of ability, integrity and standing, having knowledge and experience in the field of economics or banking or finance or monetary policy.

- RBI Act prohibits appointing any Member of Parliament or Legislature or public servant, or any employee / Board / committee member of RBI or anyone with a conflict of interest with RBI or anybody above the age of 70 to the MPC.
- Central government also retains powers to remove any of its nominated members from MPC subject to certain conditions and if the situation warrants the same.

Financial Stability and Development Council

- Background: Since April 2009, India was a member of the international agency looking into the issue, namely, Financial Stability Board.
- High Level Coordination Committee on Financial Markets (HLCCFM), was the agency facilitating regulatory coordination, informally
- HLCCFM was the forum to deal with inter-regulatory issues arising in the financial and capital markets, as India follows a multi-regulatory regime for financial sector. It functioned under the Chairmanship of Governor (RBI), with Chairman (SEBI) Secretary (Economic Affairs, Ministry of Finance), Chairman (Insurance Regulatory and Development Authority) and Chairman (Pension Fund Regulatory Development Authority- PFRDA) as members.
- However, it was an informal body and had its own limitations despite being a good mechanism. In the absence of formal instruments, clear specifications as to its functions/powers and an empowered secretariat to nominate and follow up on the decisions of the HLCCFM, its effectiveness has been limited.
- The markets that are regulated by members of the HLCCFM have dramatically changed since 1992. Over time, markets have become more complex and converged and are becoming increasingly integrated. In such a scenario, if the regulators do not take an integrated and holistic view, it was felt that outcomes will be sub-optimal.
- Various Governmental Committees, as given below, have also recommended such an approach to regulation:
  - RBI’s Advisory Group on Securities Market Regulation (RBI-AGSMR 2001);
  - High Level Expert Committee on Making Mumbai an International Financial Centre (MIFC 2007);
  - Committee on Financial Sector Reforms (CFSR 2008);
  - Committee on Financial Sector Assessment (CFSA 2009).
- With a view to strengthen and institutionalize the mechanism for maintaining financial stability and enhancing inter-regulatory coordination, Indian Government setup an apex-level Financial Stability and Development Council (FSDC), in the Union Budget 2010–11.
- Composition:
- The Chairman of the FSDC is the Finance Minister of India and its members include the heads of the financial sector regulatory authorities (i.e, SEBI, IRDA, RBI, PFRDA and FMC) , Finance Secretary and/or Secretary, Department of Economic Affairs (Ministry of Finance), Secretary, (Department of Financial Services, Ministry of Finance) and the Chief Economic Adviser.
- The commodities markets regulator, Forward Markets Commission (FMC) was added to the FSDC in December 2013 subsequent to shifting of administrative jurisdiction of commodities market regulation from Ministry of Consumer Affairs to Ministry of Finance.
- Mandate: The Council would monitor macro prudential supervision of the economy, including the functioning of large financial conglomerates. It will address inter-regulatory coordination issues and thus spur financial sector development. It will also focus on financial literacy and financial inclusion. What distinguishes FSDC from other such similarly situated organizations across the globe is the additional mandate given for development of financial sector.

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INFLATION

- Inflation is a quantitative measure of the rate at which the average price level of a basket of selected goods and services in an economy increases over a period of time.
- It is the constant rise in the general level of prices where a unit of currency buys less than it did in prior periods.
- Often expressed as a percentage, inflation indicates a decrease in the purchasing power of a nation's currency.
- Inflation can be viewed positively or negatively depending on the individual viewpoint.
- Those with tangible assets, like property or stocked commodities, may like to see some inflation as that raises the value of their assets.
- People holding cash may not like inflation, as it erodes the value of their cash holdings.
- Ideally, an optimum level of inflation is required to promote spending to a certain extent instead of saving, thereby nurturing economic growth.

Understanding Inflation

- As prices rise, a single unit of currency loses value as it buys fewer goods and services. This loss of purchasing power impacts the general cost of living for the common public which ultimately leads to a deceleration in economic growth. The consensus view among economists is that sustained inflation occurs when a nation's money supply growth outpaces economic growth.
- To combat this, a country's appropriate monetary authority, like the central bank, then takes the necessary measures to keep inflation within permissible limits and keep the economy running smoothly.
- Inflation is measured in a variety of ways depending upon the types of goods and a service considered and is the opposite of deflation which indicates a general decline occurring in prices for goods and services when the inflation rate falls below 0%.

Causes of Inflation

- Rising prices are the root of inflation, though this can be attributed to different factors. In the context of causes, inflation is classified into three types: Demand-Pull inflation, Cost-Push inflation, and Built-In inflation.

Demand Pull factors:

These are those set of factors due to which there may be an increase in the demand for goods and services in the economy. Increase in government expenditure:

- **Increased government expenditure** results in increased demand for goods and services and consequent increase in prices. This is because increased government expenditure results in putting large money in the hands of public, thereby putting to affect too much money chasing too few goods.
- **Rising population:** Increasing population also acts as an important factor in pushing up prices because of increased demand especially when the supply is unable to meet the demand.

- **Black Money:** A large part of the black money is used in buying and selling of real estate in urban areas, extensive hoarding and black marketing in essential wage goods, such as cereals, pulses, etc. Black money, therefore, fuels demands and leads to rise in prices.
- **Changing consumption patterns:** Reserve Bank of India (RBI) put forward the theory that the inflation problem in India has its roots in a sharp increase in demand for certain food items that people eat more frequently as incomes rise. One example is protein-rich food. Increased consumption of pulses, eggs, fish and poultry were apparently driving up their prices in the economy.

Cost- Push Factors:

The reasons are:

- At times rise in wages, if greater than rise in productivity, increases the costs therefore increasing the prices too.
- Increase in indirect taxes also leads to cost side inflation. Taxes such as custom and excise duty raise the cost of production as these taxes are levied on commodities.
- Increase in administered prices such as the MSP (Minimum Support Price) for the food grains, petroleum products, etc. also leads to inflation as they have a huge share in budget of common citizens.
- Infrastructural bottlenecks such as the lack of proper roads, electricity, water, etc rise per unit cost of production. This is one of the prime reasons for inflation in the context of Indian economy.
- Owing to events such as failed monsoons there is a drop in agricultural productivity, which inevitably results in inflation at times.

Types of Inflation

On the Basis of Causes:

- **Currency inflation:**
  - This type of inflation is caused by the printing of currency notes.
- **Credit inflation:**
  - Being profit-making institutions, commercial banks sanction more loans and advances to the public than what the economy needs. Such credit expansion leads to a rise in price level.
- **Deficit-induced inflation:**
  - The budget of the government reflects a deficit when expenditure exceeds revenue. To meet this gap, the government may ask the central bank to print additional money. Since pumping of additional money is required to meet the budget deficit, any price rise may be called the deficit-induced inflation.
- **Demand- Pull inflation:**
  - An increase in aggregate demand over the available output leads to a rise in the price level. Such inflation is called demand-pull inflation (henceforth DPI). But why does aggregate demand rise? Classical economists attribute this rise in aggregate demand to money supply. If the supply of money in an economy exceeds the available goods and services, DPI appears. It has been described by Coulborn as a situation of “too much money chasing too few goods.”
- **Cost-push inflation:**
  - Inflation in an economy may arise from the overall increase in the cost of production. This type of inflation is known as cost-push inflation (henceforth CPI). Cost of production may rise due to an increase in the prices of raw materials, wages, etc. Often trade unions are blamed for wage rise since wage rate is not completely market-determined. Higher wage means high cost of production. Prices of commodities are thereby increased.

On the Basis of Speed or Intensity:

- **Creeping or Mild Inflation:**
  - If the speed of upward thrust in prices is slow but small then we have creeping inflation. What speed of annual price rise is a creeping one has not been stated by the economists. To some, a creeping or mild inflation is one when annual price rise varies between 2 p.c. and 3 p.c. If a rate of price rise is kept at this level, it is considered to be helpful for economic development. Others argue that if annual price rise goes slightly beyond 3 p.c. mark, still then it is considered to be of no danger.
- **Walking Inflation:**
  - If the rate of annual price increase lies between 3% and 4%, then we have a situation of walking inflation. When mild inflation is allowed to fan out, walking inflation appears. These two types of inflation may be described as 'moderate inflation'.
  - Often, one-digit inflation rate is called 'moderate inflation' which is not only predictable, but also keeps people's faith on the monetary system of the country. Peoples' confidence gets lost once moderately maintained rate of inflation goes out of control and the economy is then caught with the galloping inflation.
- **Galloping and Hyperinflation:**
  - Walking inflation may be converted into running inflation. Running inflation is dangerous. If it is not controlled, it may ultimately be converted to galloping or hyperinflation. It is an extreme form of inflation when an economy gets shattered. "Inflation in the double or triple digit range of 20, 100 or 200% a year is labeled "galloping inflation".
- **Hyper Inflation:**
  - Hyperinflation is when the prices of goods and services rise more than 50 percent a month. It is fortunately very rare. In fact, most examples of hyperinflation have occurred when the government printed money recklessly to pay for war. Examples of hyperinflation include Germany in the 1920s, Zimbabwe in the 2000s, and during the American Civil War.
- **Stagflation**
- Stagflation is when the economy experiences stagnant economic growth, high unemployment, and high inflation. It is unusual because policies to reduce inflation make life difficult for the unemployed, while steps to alleviate unemployment raise inflation.
- **Core Inflation**
  - This shows price rise in all goods and services except food and energy due to high prices fluctuations. Oil is a highly volatile commodity, with daily price variations. Food prices change based on gas prices (it heavily reflects on transportation costs), which are directly linked to oil prices. As the government needs a fairly stable and true picture of inflation, core inflation is calculated.
- **Headline Inflation**
  - This measure considers total inflation in an economy, including food and energy prices, which are more volatile.

How is Inflation Measured?

The inflation rate is calculated as a percentage change in a price index. The price indices widely used for this are the Consumer Price Index (CPI) - adopted by countries such as US, UK, Japan and China, and the Wholesale Price Index (WPI).

Wholesale Price Index (WPI)

- Wholesale Price Index, or WPI, measures the changes in the prices of goods sold and traded in bulk by wholesale businesses to other businesses.
- Analysts use the numbers to track the supply and demand dynamics in industry, manufacturing and construction.

- The numbers are released by the Economic Advisor in the Ministry of Commerce and Industry.
- An upward surge in the WPI print indicates inflationary pressure in the economy and vice versa.
- The quantum of rise in the WPI month-after-month is used to measure the level of wholesale inflation in the economy.

New series of WPI

- With an aim to align the index with the base year of other important economic indicators such as GDP and IIP, the base year was updated to 2011-12 from 2004-05 for the new series of Wholesale Price Index (WPI), effective from April 2017.

Major components of WPI

- Primary articles are a major component of WPI, further subdivided into Food Articles and Non-Food Articles.
- Food Articles include items such as Cereals, Paddy, Wheat, Pulses, Vegetables, Fruits, Milk, Eggs, Meat & Fish, etc.
- Non-Food Articles include Oil Seeds, Minerals and Crude Petroleum
- The next major basket in WPI is Fuel & Power, which tracks price movements in Petrol, Diesel and LPG
- The biggest basket is Manufactured Goods. It spans across a variety of manufactured products such as Textiles, Apparels, Paper, Chemicals, Plastic, Cement, Metals, and more.
- Manufactured Goods basket also includes manufactured food products such as Sugar, Tobacco Products, Vegetable and Animal Oils, and Fats.

How do you calculate Wholesale Price Index?

- The monthly WPI number shows the average price changes of goods usually expressed in ratios or percentages.
- The index is based on the **wholesale prices of a few relevant commodities** available.
- The commodities are chosen based on their significance in the region. These represent different strata of the economy and are expected to provide a comprehensive WPI value.
- The advanced base year **2011-12** adopted recently uses 697 items.

Problem/limitation

- One of the major limitations of WPI is that it does not include services such as the health, IT, Education, transport etc.
- Another problem with the WPI is that it does not account for the products of the unorganized sector in India, which constitutes about 35% of the manufactured output of the Indian economy.

Weightage in WPI

- **Manufacturing products:** 64.97%
- **Primary and food articles:** 20.12%
- **Fuel and electricity:** 14.91

Consumer Price Index

- Consumer Price Index or CPI as it is commonly called is an index measuring retail inflation in the economy by collecting the change in prices of most common goods and services. Called market basket, CPI is calculated for a fixed list of items including food, housing, apparel, transportation, electronics, medical care, education, etc. Note that the price data is collected periodically, and thus, the CPI is used to calculate the inflation levels in an economy. This can be further used to compute the cost of living. This also provides insights as to how much a consumer can spend to be on par with the price change.

Who maintains Consumer Price Index in India?

In India, there are four consumer price index numbers, which are calculated, and these are as follows:

- **CPI for Industrial Workers (IW)**
  - The Consumer Price Index for the industrial workers (CPI-IW) has 260 items (plus the services) in its basket with 2001 as the base year (the first base year was 1958-59). The data is collected at 76 centres with one month's frequency and the index has a time lag of one month. It contains 120-160 commodities in its basket. Basically, this index specifies the government employees (other than banks' and embassies' personnel). The wages/salaries of the central government employees are revised on the basis of the changes occurring in this index, the dearness allowance (DA) is announced twice a year. When the Pay Commissions recommend pay revisions, the base is the CPI (IW).
- **CPI for Agricultural Labourers (AL)**
  - The Consumer Price Index for Agricultural Labourers (CPI-AL) has 1986-87 as its base year with 260 commodities in its basket. The data is collected in 600 villages with a monthly frequency and has three weeks' time lag. This index is used for revising minimum wages for agricultural labourers in different states.
- **CPI for Rural Labourers (RL)**
  - There is yet another Consumer Price Index for the Rural Labourers (CPI-RL) with 1983 as the base year, data is collected at 600 villages on monthly frequency with three weeks' time lag, and its basket contains 260 commodities.
  - In 2011 the CSO brought out a revised CPI, which was CPI (Urban), CPI (Rural) and CPI (Urban + Rural) with 2010 as the base price. The combined one would take into account the data from both the indices taking appropriate weights.
  - When compared to the WPI, CPI has much larger weightage of primary articles which is 57%. What this essentially means is that food inflation is reflected much more appropriately in the CPI when compared to the WPI which gives only 20% weightage to primary articles.
  - To compile the database for CPI-urban, the federal statistics office has been collecting data from retail outlets in more than 100 cities, and for CPI-rural data collection is underway in more than 1,200 villages. Due to a shortage of staff, the statistics department has roped in officials from various departments including the postal department. More than 2,400 postmen were engaged in collection of retail prices from villages across the country. Currently, the labor ministry and the commerce and industry ministry are involved in compiling and releasing inflation figures. The ministry is also awaiting the cabinet's approval for a single nodal agency for compiling data.
- **CPI for Urban Non-Manual Employees (UNME)**
  - This index depicts the changes in the level of average retail prices of goods and services consumed by the urban segment of the population.
  - The target group of this index was urban families who derived major portion of their income from non-manual occupations in the non-agricultural sector.
  - This index had a limited use as it was used for determining dearness allowances of employees of some foreign companies working in India in service sectors such as airlines, communications, banking, insurance and other financial services.

While the **Ministry of Statistics and Program Implementation collects CPI (UNME)** data and compiles it, the remaining three are collected by **the Labour Bureau in the Ministry of Labour**.

How does Consumer Price Index help?

- The Reserve Bank of India and other statistical agencies study CPI so as to understand the price change of various commodities and keep a tab on inflation. CPI is also a helpful pointer in understanding the real value of wages, salaries and pensions, the purchasing power of a country's currency; and regulating prices.

- Economists are in charge of collecting data by surveying households on their buying patterns, most purchased items, and daily expenses.

Changes in methodology of measuring inflation

- Reserve Bank of India (RBI) had adopted the new Consumer Price Index (CPI) (combined) as the key measure of inflation. The national CPI is meant to measure retail inflation. This index will combine urban and rural CPIs, both under preparation and to be released simultaneously. Unlike many other countries, India does not have a unified CPI and uses the WPI as a benchmark. The unified CPI will usher in a fundamental shift in the way the Reserve Bank of India (RBI) targets inflation.

Effects of Inflation:

- People’s desires are inconsistent. When they act as buyers they want prices of goods and services to remain stable but as sellers they expect the prices of goods and services should go up. Such a happy outcome may arise for some individuals; “but, when this happens, others will be getting the worst of both worlds.”
- When price level goes up, there is both a gainer and a loser. To evaluate the consequence of inflation, one must identify the nature of inflation which may be anticipated and unanticipated. If inflation is anticipated, people can adjust with the new situation and costs of inflation to the society will be smaller.

One can study the effects of unanticipated inflation under two broad headings:

Effects of Inflation on Distribution of Income and Wealth:

- During inflation, usually people experience rise in incomes. But some people gain during inflation at the expense of others. Some individuals gain because their money incomes rise more rapidly than the prices and some lose because prices rise more rapidly than their incomes during inflation. Thus, it redistributes income and wealth.
- Though no conclusive evidence can be cited, it can be asserted that following categories of people are affected by inflation differently:
    - **Creditors and debtors:**
        - **Borrowers gain and lenders lose during inflation** because debts are fixed in rupee terms. When debts are repaid their real value declines by the price level increase and, hence, creditors lose. An individual may be interested in buying a house by taking loan of Rs. 7 lakh from an institution for 7 years.
        - The borrower now welcomes inflation since he will have to pay less in real terms than when it was borrowed. Lender, in the process, loses since the rate of interest payable remains unaltered as per agreement. Because of inflation, the borrower is given ‘dear’ rupees, but pays back ‘cheap’ rupees. However, if in an inflation-ridden economy creditors chronically loose, it is wise not to advance loans or to shut down business.
        - Never does it happen. Rather, the loan-giving institution makes adequate safeguard against the erosion of real value. Above all, banks do not pay any interest on current account but charges interest on loans.
    - **Bond and debenture-holders:**
        - **In an economy, there are some people who live on interest income—they suffer most.** Bondholders earn fixed interest income: These people suffer a reduction in real income when prices rise. In other words, the value of one’s savings decline if the interest rate falls short of inflation rate. Similarly, beneficiaries from life insurance programmes are also hit badly by inflation since real value of savings deteriorate.
    - **Investors:**
        - **People who put their money in shares during inflation are expected to gain** since the possibility of earning of business profit brightens. Higher profit induces owners of firm to distribute profit among investors or shareholders.

- **Salaried people and wage-earners:**
  - **Anyone earning a fixed income is damaged by inflation.** Sometimes, unionized worker succeeds in raising wage rates of white-collar workers as compensation against price rise. But wage rate changes with a long time lag. In other words, wage rate increases always lag behind price increases. Naturally, inflation results in a reduction in real purchasing power of fixed income-earners.
  - On the other hand, **people earning flexible incomes may gain during inflation.** The nominal incomes of such people outstrip the general price rise. As a result, real incomes of this income group increase.
- **Profit-earners, speculators and black marketers:**
  - It is argued that **profit-earners gain from inflation**. Profit tends to rise during inflation. Seeing inflation, businessmen raise the prices of their products. This results in a bigger profit. Profit margin, **however, may not be high when the rate of inflation climbs to a high level.**
  - However, speculators dealing in business in essential commodities usually stand to **gain by inflation. Black marketers are also benefited by inflation.**
- **Effect on Production and Economic Growth:**
  - **Inflation may or may not result in higher output**. Below the full employment stage, inflation has a favourable effect on production.
  - In general, profit is a rising function of the price level.
  - An inflationary situation gives an incentive to businessmen to raise prices of their products so as to earn higher volume of profit.
  - Rising price and rising profit encourage firms to make larger investments.

How can Inflation be curbed?

Monetary, fiscal and administrative measures are taken to control inflation to an optimal level in the economy.

Monetary Measures

- The governments may take recourse to tighter monetary policy to cool down either the demand-pull or the cost-push inflation. For example, the RBI may increase the bank rates/repo rates etc. to curb the supply of money in the market.
- Because of such a step, the public may want to invest more in the banks and lead to a drop in the consumption, thereby driving down the inflation in the economy.
- It may also use qualitative control methods such as raise margins on loans for commodities for which traders have a tendency to speculate and hoard.
- Reserve Bank may also resort to other operations such as the Open Market Operations to mop out the liquidity from the market by selling government securities and bonds.
- But monetary steps can only be successful if inflation is due to demand pull factors and not structural in nature.
- Some of the limitations of raising interest rates to curb inflation have been discussed below:
  - It has been observed several times in the past that the increase in bank rate by the RBI may not translate into a commensurate increase in interest rates by the banks.
  - Banks necessarily do not raise their own interest rates at times even if the correct signals have been given by the RBI thereby defeating the entire purpose of the move.
  - Another issue, which is important in a country like India, is the large presence of unorganized banking. Because of this RBI is not able to control a large part of the banking sector in the economy.

Fiscal Measures

- As far as fiscal measures are concerned the government can take two routes to bring down the prices.
- Firstly, it can cut down its own spending on various schemes, projects, etc. and secondly it can increase the taxes (either direct or indirect).
- As far as the first option is concerned most of the governments across the world do not employ this method for two simple reasons, first they cannot suddenly reduce the money, which is being spent on several critical projects pertaining to infrastructure, etc. as it would not only bring down the image of the country but also create a negative market sentiment.
- Secondly, if they cut down spending on several important welfare schemes, etc. then it may politically harm them in the next elections. So cutting down government expenditure is not considered feasible because of a mix of reasons. The second method is raising the taxes to discourage spending.
- The government may increase the private direct taxes to reduce the incomes and thereby decreasing the consumption tendencies among the public.
- It may also increase the indirect taxes on commodities raising their prices and thereby discouraging spending on them by the public.

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DAY - 50

ECONOMIC REFORMS

- The economic reforms were initiated in 1991.
- Economic reforms denote the process in which a government prescribes declining role for the state and expanding role for the private sector in an economy.
- It is safer to see economic reform as a policy shift in an economy from one to another or '**alternative development strategies'**.

Economic reforms In India

- On July 23, 1991, India launched a process of economic reforms in response to a fiscal and balance-of-payment (BoP) crisis.
- The reforms were historic and were going to change the very face and the nature of the economy in the coming times.
- The reforms and the related programmes are still going on with changing emphasis and dimensions.
- Back in the mid-1980s, the governments had taken its first steps to economic reforms.
- While the reforms of the 1980s **witnessed rather limited deregulation and 'partial liberalization** of only a few aspects of the existing control regime, the reforms started in early **1990s in the fields of industries, trade, investment and later to include agriculture, were much 'wider and deeper'.**
- Though liberal policies were announced by the governments during the reforms of the 1980s itself, with the slogan of 'economic reforms', it **was only launched with full conviction in the early 1990s.**
- But the reforms of the 1980s, which were under the influence of the **famous 'Washington Consensus' ideology had a crippling impact on the economy.**
- The whole Seventh Plan (1985–90**) promoted further relaxation of market regulations** with heavy external borrowings to increase exports (as the thrust of the policy reform).
- By now as the benefits of the reforms have accrued to many, the criticism has somewhat calmed down, but still the reform process is considered as **'anti-poor' and 'pro-rich'.**
- **The need of the hour is to go for 'distributive growth', though the reform has led the economy to a higher growth path.**

Reform measures

The economic reform programme, that India launched, consisted of two categories of measures:

- **Macroeconomic Stabilization Measures**
  - It includes all those economic policies which intend to boost the aggregate demand in the economy—be it domestic or external.
  - For the enhanced domestic demand, the focus has to be on increasing the purchasing power of the masses, which entails an emphasis on the creation of gainful and quality employment opportunities.

- **Structural Reform Measures**
  - It includes all the policy reforms which have been initiated by the government to boost the aggregate supply of goods and services in the economy.
  - It naturally entails unshackling the economy so that it may search for its own potential of enhanced productivity.
  - For the purchasing capacity of the people to be increased, the economy needs increased income, which comes from increased levels of activities.
  - Income so increased is later distributed among the people whose purchasing power has to be increased
  - **This will take place by properly initiating a suitable set of macroeconomic policies.**

The LPG

- The process of reforms in India has to be completed via three other processes namely, **liberalization, privatization and globalization**, known popularly by their short-form, the LPG.
- These three processes specify the characteristics of the reform process India initiated.
- Precisely seen, **liberalization** shows the **direction of reform**,
- **Privatization** shows **the path of reform** and **globalization** shows the **ultimate goal of the reform**.

Liberalization

- The ideology was the product of **the breakdown of feudalism** and the **growth of a market or capitalist society in its place**, which became popular in economics via the writings of **Adam Smith** and got identified as a principle of **laissez-faire.**
- **Pro-market or pro-capitalistic** inclination in the economic policies of an economy is the process of liberalization.
- The most suitable example of this process could be **China** of the mid-1980s when it announced its **'open door policy'.**
- The process of decreasing traits of a state economy and increasing traits of a market economy is liberalization.
- In the Indian case the term liberalisation is used to show the **direction of the economic reforms**— with decreasing influence of the state or the planned or the command economy and increasing influence of free market or the capitalistic economy.
- It is a move towards capitalism. India is attempting to strike its own balance of **the 'state-market mix'**.
- It means, even if the economic reforms have the direction towards market economy it can never be branded a blind run to capitalism.

Privatization

- The policies through which the 'roll back' of the state was done included deregulation, **privatization** and introduction of market reforms in public services.
- Privatization was used as a process under which the state assets were transferred to the private sector.
- The root of the term privatization goes to this period which got more and more currency around the world once the East European nations and later the developing democratic nations went for it.
- But during the period several connotations and meanings of the term **'privatization'** have developed. Some of them are described below:
  - Privatization in its purest sense and lexically **means de-nationalization**, i.e., transfer of the state ownership of the assets to the private sector to the tune of 100 per cent. This route of privatization has been avoided by almost all democratic systems.

- The sense in which privatization has been used is the process of **disinvestment** all over the world. This process includes **selling of the shares of the state owned enterprises to the private sector.** Disinvestment is **de-nationalization of less than 100 per cent ownership transfer from the state to the private sector.** If an asset has been sold out by the government to the tune of **only 49 per cent the ownership remains with the state though it is considered privatization.** If the sale of shares of the state-owned assets has been to the tune of **51 per cent, the ownership is really transferred to the private sector even then it is termed as privatization.**
- The third and the last sense in which the term privatization has been used around the world, is very wide. Basically, all the **economic policies which directly or indirectly seem to promote the expansion of the private sector or the market (economy)** have been termed by experts and the governments as the process of privatization.

Globalization

- The process of Globalization has always been used in economic terms though it has always taken the political and cultural dimensions.
- Globalization is generally termed as **'an increase in economic integration among nations'**.
- The concept was popularised by the **Organisation of Economic Cooperation and Development (OECD) in the mid-1980s.**
- In its earlier deliberatization, the organisation had defined globalisation in a very narrow and business-like sense**—**'**any crossborder investment by an OECD company outside its country of origin for its benefit is globalisation'.**
- The official meaning of globalisation for the **WTO** is movement of the economies of the world towards **"unrestricted cross border movements of goods and services, capital and the labour force".**
- It simply means that the economies who are signatories to the process of globalization (i.e., signatories to the WTO) for them there will be nothing like foreign or indigenous goods and services, capital and labour. The world becoming a flat and level-playing field emerging in the due process of time
- For many political scientists, globalization is the emergence of a situation when our lives are increasingly shaped by the events that occur at a great distance from us about which the decisions are not taken by our conscious self.
- India became one of the founding members of the WTO and was obliged to promote the process of globalization, though its economic reforms started with no such obligations.
- It is a different thing that India started the process of globalization right after the reforms 1991.
- It should be noted here that the Indian idea of globalization is deeply and frequently inclined towards the **concept of welfare state,** which keeps coming in the day to day public policy as an emphatic reference.

Generations of Economic Reforms

Though there were no such announcements or proposals while India launched its reforms in 1991, in the coming times, many 'generations' of reforms were announced by the governments.31A total of three generations of reforms have been announced till date, while experts have gone to suggest the fourth generation, too.

First Generation reforms (1991–2000)

The reforms initiated during 1991 to 2000 were termed as First Generation Reforms. The broad coordinates of the First Generation of reforms may be seen as under:

- **Promotion to Private Sector**
  - This included various important and liberalising policy decisions, i.e., 'de-reservation' and 'delicencing' of the industries, abolition of the MRTP limit, abolition of the compulsion of the

phased-production and conversion of loans into shares, simplifying environmental laws for the establishment of industries, etc.

- **Public Sector Reforms**
  - The steps taken to make the public sector undertakings profitable and efficient, their disinvestment (token), their corporatization, etc., were the major parts of it.
- **External Sector Reforms**
  - They consisted of policies like, abolishing quantitative restrictions on import, switching to the floating exchange rate, full current account convertibility, reforms in the capital account, permission to foreign investment (direct as well as indirect), promulgation of a liberal Foreign Exchange Management Act (the FEMA replacing the FERA), etc.
- **Financial Sector Reforms**
  - Several reform initiatives were taken up in areas such as banking, capital market, insurance, mutual funds, etc.
- **Tax Reforms**
  - This consisted of all the policy initiatives directed towards **simplifying, broadbasing, modernising, checking evasion,** etc.
  - A major re-direction was ensued by this generation of reforms in the economy—the 'command' type of the **economy moved strongly towards a market-driven economy, private sector (domestic as well as foreign) to have greater participation in the future.**

Second Generation reforms (2000–01 onwards)

The government launched the second generation of reforms in 2000-01. Basically, the reforms India launched in the early 1990s were not taking place as desired and a need for another set of reforms was felt by the governments, which were initiated with the title of the Second Generation of economic reforms. These reforms were not only deeper and delicate, but required a higher political will power from the governments. The major components of the reform are as given below:

- **Factor Market Reforms**
  - Considered as the 'backbone' for the success of the reform process in India, it consists of dismantling of the Administered Price Mechanism (APM).
  - There were many products in the economy whose prices were fixed /regulated by the government, viz., petroleum, sugar, fertilizers, drugs, etc.
  - Though a major section of the products under the APM were produced by the private sector, they were not sold on market principles which hindered the profitability of the manufacturers as well as the sellers and ultimately the expansion of the concerned industries leading to a demand supply gap.
  - Under market reforms these products were to be brought into the market fold.
  - But we cannot say that the Factor Market Reforms (FMRs) are complete in India. It is still going on.
  - Cutting down subsidies on essential goods is a socio-political question in India.
  - Till market-based purchasing power is not delivered to all the consumers, it would not be possible to complete the FMRs.
- **Public Sector Reforms**
  - The second generation of reforms in the public sector especially emphasizes on areas like greater functional autonomy, freer leverage to the capital market, international tie-ups and Greenfield ventures, disinvestment.
- **Reforms in Government and Public Institutions**
  - This **involves all those moves which really go to convert the role of the government from the 'controller' to the 'facilitator'** or the administrative reform, as it may be called.
- **Legal Sector Reforms**

- Though reforms in the legal sector were started in the first generation itself, now it was to be deepened and newer areas were to be included, such as, abolishing outdated and contradictory laws, reforms in the Indian Penal Code (IPC) and Code of Criminal Procedure (CrPC), Labour Laws, Company Laws and enacting suitable legal provisions for new areas like Cyber Law, etc.

- **Reforms in Critical Areas**
  - The second generation reforms also commit to suitable reforms in the infrastructure sector (i.e., power, roads, especially as the telecom sector has been encouraging), agriculture, agricultural extension, education and healthcare, etc. These areas have been called by the government as **'critical areas'.**

Third Generation reforms

- Announcement of the third generation of reforms were made on the margins of the launching of the Tenth Plan (2002–07).
- This generation of reforms commits to the cause of a fully functional Panchayati Raj Institution (PRIs), so that the benefits of economic reforms, in general, can reach to the grassroots.
- Though the constitutional arrangements for a decentralized developmental process were already effected in the early 1990s, it was in the early 2000s that the government gets convinced of the need of **'inclusive growth and development'.**
- Till the masses are not involved in the process of development, the development will lack the **'inclusion' factor**; it was concluded by the government of the time.

Fourth Generation reforms

- This is not an official 'generation' of reform in India. Basically, in early 2002, some experts coined this generation of reforms which entail a **fully 'information technology-enabled'** India.
- They hypothesized **a 'two-way' connection between the economic reforms and the information technology (IT), with each one reinforcing the other.**

India's reform process which commenced in 1991 has been termed by experts as **gradualist** in nature with traits of occasional reversals, and without any big ideological U-turns. It reflects the compulsions of India's highly pluralist and participative democratic policy-making process. **Though such an approach helped the country to avoid sociopolitical upheavals/instability, it did not allow the desired economic outcome could have accrue from the reforms.** The first generation of economic reforms could not bring the expected results due to lack of some other set of reforms for which India goes after almost over a decade—the second generation of economic reforms. Similarly, the economic benefits (whatever accrued) remained non-inclusive, in absence of an active public policy aimed at inclusion (commencing via the third generation of economic reforms). This created a kind of disillusionment about the prospects of reforms and failed the governments to muster enough public support in favour of reforms.

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AGRICULTURE

- Agriculture remains the most important sector of the Indian economy, whether it be the pre independence or the post-independence periods.
- This fact is emphatically proved by the large number of people who depend on it for their livelihood.

Some of the special features of Indian Agriculture are mentioned below:

- From the monetary point of view the share of the agriculture sector in the economy remains at **17.4 per cent** of the GDP.
- From the livelihood point of view still **49 per cent** of the people of India depend on the agriculture sector.
- Agriculture is not only the biggest sector of the economy, but also the biggest private sector too. It is the **only profession which still carries no burden of individual income tax.**
- This is the **biggest unorganized sector** of the economy accounting for more than 90 per cent share in the total unorganized labor-force.
- India has emerged as a significant agri-exporter in few crops, namely—cotton, rice, meat, oil meals, spice, guar gum meal and sugar.
- According to the export figures, agriculture is deeply related to industrial growth and the national income in India—1 per cent increase in the agricultural growth leads to 0.5 per cent increase in industrial output (growth) and 0.7 per cent increase in the national income of India.
- **Productivity** of major crops are lower in case of India in comparison to the world's best practice.

Land-tenure systems

Three types of land-tenure systems existed in pre-independent India:

The Zamindari system

- Zamindari System (also known as Permanent Settlement System) was introduced by Cornwallis in 1793 through Permanent Settlement Act.
- It was introduced in provinces of Bengal, Bihar, Orissa and Varanasi. Zamindars were recognized as owner of the lands.
- Zamindars were given the rights to collect the rent from the peasants.
- The realized amount would be divided into 11 parts. 1/11th of the share belonged to Zamindars and 10/11th of the share belonged to East India Company

The Mahalwari system

- Mahalwari system was introduced in 1833 during the period of William Bentick.
- It was introduced in Central Province, North-West Frontier, Agra, Punjab, Gangetic Valley, etc. of British India.

- The Mahalwari system included many provisions of both the Zamindari System and Ryotwari System.
- In this system, the land was divided into Mahals. Each Mahal comprises one or more villages.
- Ownership rights were vested with the peasants.
- The villages committee was held responsible for collection of the taxes.

The Ryotwari system

- Here, individual cultivator was supposed to pay the rent directly to the government without any intermediary. It was prevalent in parts of Madras, Bombay province and Assam.
- In practice, however, all three types of system had taken the features of each other. The picture that emerged at independence was that of exploitation of agricultural labourers at the hands of landlords, exorbitant rents, lack of incentive for technological progress and rigid system of land transfer across the country.

Land reforms

- Land reform involves the changing of laws, regulations or customs regarding land ownership. Land reform may consist of government-initiated or government-backed property redistribution, generally of agricultural land.
- Land reform can, therefore, refer to transfer of ownership from the more powerful to the less powerful, such as from a relatively small number of wealthy (or noble) owners with extensive land holdings (e.g., plantations, large ranches, or agribusiness plots) to individual ownership by those who work the land. Such transfers of ownership may be with or without compensation; compensation may vary from token amounts to the full value of the land.
- The common characteristic of all land reforms, however, is modification or replacement of existing institutional arrangements governing possession and use of land.
- Land distribution has been part of India's state policy from the very beginning. Independent India's most revolutionary land policy was perhaps the abolition of the Zamindari system (feudal land holding practices). Land-reform policy in India had two specific objectives:
    - To remove such impediments to increase in agricultural production as arise from the agrarian structure inherited from the past.
    - To eliminate all elements of exploitation and social injustice within the agrarian system, to provide security for the tiller of soil and assure equality of status and opportunity to all sections of the rural population.

Three major types of land-reforms were undertaken after independence:

- **Abolition of Intermediaries** like Zamindars or jagirdars so that ownership of land could be clearly identified with management and control. Many states promulgated laws to put an end to absentee landlordism and as a result about 30 lakh tenants acquired land ownership over an area of 62 lakh acres throughout the country.
- **Tenancy reforms** to confirm the rights of occupancy of tenants and to regulate rent of leased land. These reforms could not be implemented due to two main reasons. Many small tenants were forced to surrender their land under the so called "voluntary surrender" rule in the legislation. Secondly, the unavailability of accurate and up-to-date land record also constrained its implementation.
- **Reorganization of land holdings** to offset extremely uneven distribution of agricultural land. Under this, ceiling laws were imposed which laid down the maximum land that can be owned by a land holder (which was subsequently amended to holding by a family with effect from 1972). The excess land was to be surrendered to the government. But its performance remained dismal as it leads to redistribution of less than 2% of operated area by 1992. Thus, with the exception of abolition of intermediaries, other reforms could not be implemented mainly due to lack of political will.

- **Consolidation of holding** was introduced as a measure of improving farming efficiency. It made considerable progress in Punjab, Haryana and western U.P. but did not took off in southern and eastern states.
- **Cooperative joint farming,** recommended by the Congress Agrarian Reforms Committee under Mr. J. C. Kumarappa was also encouraged in the five year plans initially. Under this, farmers pool their land and reap the economies of scale, although the ownership continues to remain with the individual farmer. But this could not be implemented mainly because of farmers' reluctance to alienate their land. Many landlords also tried to misuse this concept to circumvent land ceiling.
- **The National Land Records Modernization Programme (NLRMP)** was launched by the Government of India in August 2008, aimed to modernize management of land records, minimize scope of land/ property disputes, enhance transparency in the land records maintenance system, and facilitate moving eventually towards guaranteed conclusive titles to immovable properties in the country.

Reasons for Failure of Land Reforms:

Out of the many reasons forwarded by the experts responsible for the failure of the land reforms in India, the following three could be considered the most important ones:

- Land in India is considered a symbol of social prestige, status and identity unlike the other economies which succeeded in their land reform programmes, where it is seen as just an economic asset for income earning.
- Lack of political wills which was required to affect land reforms and make it a successful programme.
- Rampant corruption in public life, political hypocricy and leadership failure in the Indian democratic system.

Green Revolution

- It is the introduction of new techniques of agriculture, which became popular by the name of Green Revolution (GR) in early 1960s—at first for **wheat and by the next decade for rice**, too. It revolutionized **the very traditional idea of food production** by giving a boost by more than 250 per cent to the productivity level. The Green Revolution was centred around the use of the **High Yielding Variety** (HYV) of seeds developed by the **US agro-scientist Norman Borlaug doing research on a British Rockfellor Foundation Scholarship in Mexico by the early 1960s**.

Components of the Green Revolution

- The Green Revolution was based on the timely and adequate supply of many inputs/components.

The HYV Seeds

- These seeds were popularly called the **'dwarf'** variety of seeds.
- This made the plant dwarf and the grain heavier— resulting in high yield.
- These seeds were **non-photosynthetic**, hence **non-dependent** on sun rays for targeted yields.

The Chemical Fertilizers

- The seeds were to increase productivity provided they got sufficient level of nutrients from the land.
- The level of nutrients they required could not be supplied with the traditional composts because they have **low concentration of nutrients content** and required bigger area while sowing—it meant it will be shared by more than one seed.
- That is why a high concentration fertilisers, were required, which could be given to the targeted seed only— the only option was the chemical fertilisers—**urea (N), phosphate (P) and potash (K).**

The Irrigation

- For controlled growth of crops and adequate dilution of fertilizers, a controlled means of water supply was required.

- It made two important compulsions—firstly, the area of such crops should be at least free of flooding and secondly, artificial water supply should be developed.

Chemical Pesticides and Germicides

- As the new seeds were new and non-acclimatised to local pests, germs and diseases than the established indigenous varieties, use of pesticides and germicides became compulsory for result oriented and secured yields.

Chemical Herbicides and Weedicides

- To prevent costlier inputs of fertilisers not being consumed by the herbs and the weeds in the farmlands, herbicides and weedicides were used while sowing the HYV seeds.

Credit, Storage, Marketing/Distribution

- For farmers to be capable of using the new and the costlier inputs of the Green Revolution, availability of easy and cheaper credit was a must.
- As the farmlands suitable for this new kind of farming was region-specific (as it was only Haryana, Punjab and western Uttar Pradesh in India) storage of the harvested crops was to be done in the region itself till they were distributed throughout the country.

Recent Development

- Green Revolution made the country self-reliant in foodgrain production.
- Post Green Revolution, there is increase in the use of chemical fertilizers and irrigation water to meet the nutrients and water demand respectively, of high yielding varieties (HYVs) of crops.
- However, due to imbalanced use of fertilizers coupled with decrease in use of organic manure and over exploitation of ground water, there is deterioration of natural resources.
- In order to meet the foodgrains requirement of the growing population of the country, the Government of India is laying emphasis on development of resource rich eastern region of the country for enhancing agricultural production.
- This would also help in reducing the over exploitation of natural resources in north western region, the traditional food bowl of the country.
- Considering potentiality of increasing production and productivity of foodgrains in eastern states**, "Bringing Green Revolution to Eastern India (BGREI)"-** a sub scheme of **Rashtriya Krishi Vikas Yojana (RKVY) is being implemented since 2010-11 in seven (7) eastern states of the country namely Assam, Bihar, Chhatisgarh, Jharkhand, Odisha, Eastern Uttar Pradesh and West Bengal.**
- After implementation of the programme, the production of rice has increased in seven eastern states from 45.65 million tonnes during 2009-10 to 57.18 million tonnes during 2017-18.
- Besides, the Schemes/Missions namely, National Food Security Mission (NFSM), Mission for Integrated Development of Horticulture (MIDH), National Mission for Sustainable Agriculture (NMSA), Sub-Mission on Seeds and Planting Material (SMSP), Sub-Mission on Agricultural Mechanisation (SMAM) etc. under the Umbrella scheme, "Green Revolution– Krishonnati Yojana" are also continued beyond 12th Five Year Plan for the periods from 2017-18 to 2019-20.
- These schemes are for the development of the agriculture and allied sector in a holistic and scientific manner to increase the income of farmers by enhancing production, productivity and better returns on produce.

Food Management

- Managing enough food in the domestic market has been the prime focus of the government since Independence. Meeting the physical target of food together with the challenge of enabling Indians to procure food for their consumption was also there. Once, the country joined the WTO, a new need was felt for producing surplus and competing with the world, so that the benefits of globalization could also be reaped by the agriculture sector.

Minimum Support Price

- Minimum Support Price (MSP) is a form of market intervention by the Government of India to insure agricultural producers against any sharp fall in farm prices —a guarantee price to save farmers from distress sale.
- The MSPs are announced at the beginning of the sowing season for certain crops on the basis of the recommendations of the Commission for Agricultural Costs and Prices (CACP, 1985).
- The major objectives are to support the farmers from distress sales and to procure food grains for public distribution.
- In case the market price for the commodity falls below the announced minimum price due to bumper production and glut in the market, government agencies purchase the entire quantity offered by the farmers at the announced minimum price.
- Commencing with 'wheat' for the 1966–67, currently the MSPs are announced for 24 commodities including seven cereals (paddy, wheat, barley, jowar, bajra, maize and ragi); five pulses (gram, arhar/tur, moong, urad and lentil); eight oilseeds (groundnut, rapeseed/mustard, toria, soyabean, sunflower seed, sesamum, safflower seed and nigerseed); copra, raw cotton, raw jute and virginia flu cured (VFC) tobacco.

Market Intervention Scheme

- The Market Intervention Scheme (MIS) is similar to MSP, which is implemented on the request of state governments for procurement of perishable and horticultural commodities in the event of fall in market prices.
- The scheme is implemented when there is at least **10 per cent increase in production or 10 per cent decrease** in the ruling rates over the previous normal year.
- Proposal of MIS is approved on the specific request of the state/UT governments, if the **states/UTs are ready to bear 50 per cent loss (25 per cent in case of North Eastern states) incurred on its implementation.**

Procurement Prices

- In 1966–67, the Government of India announced a 'procurement price' for wheat, a bit higher than its MSP (the purpose being security of food procurement for requirement of the PDS).
- The MSP was announced before sowing, while the **procurement price was announced before harvesting**—the purpose was to encourage farmers to sell a bit more and get encouraged to produce more.
- But this increased price hardly served the purpose as a suitable incentive to farmers.
- It would have been better had it been announced before sowing and not after harvesting.
- **That is why since the fiscal 1968–69 the government announced only the MSP, which is also considered the effective procurement price.**

Buffer Stock

- India has a policy of maintaining a minimum reserve of foodgrains (only for wheat and rice) so that food is available throughout the country at affordable prices round the year.
- The main supply from here goes to the PDS and at times goes for Open Market Sale to check the rising prices, if needed.
- The Buffer stocking norms (of 2005) was revised by the government (by mid-2014) in the backdrop of increased requirement of foodgrains.

Open Market Sale Scheme

- The FCI has been undertaking sale of wheat at pre-determined prices (reserve prices) in the open market from time to time, known as the Open Market Sale Scheme (OMSS).

- **This is aimed at serving the following objectives:**
  - To enhance market supply of foodgrains;
  - To exercise a moderating influence on open market prices; and
  - To offload surplus stocks.
- Under the Open Market Sale Scheme (Domestic), the government now adopts a policy of differential prices to encourage sale of older stock first.

Price Stabilization Fund

- The Government of India, by late March 2015, launched the Price Stabilisation Fund (PSF) as a Central Sector Scheme to support market interventions for price control of perishable agri horticultural commodities.
- The cost to be borne between the **centre and the states in equal ratio (in case of the North Eastern-states, the respective share will be 75:25).**
- The scheme will commence with only two crops, viz., **onion and potato**.

Farm Subsidies

- Farm subsidies form an integral part of the government's budget.
- In the case of developed countries, the agricultural or farm subsidies compose nearly 40 per cent of the total budgetary outlay, while in India's case it is much lower (around 7.8 per cent of GDP) and of different nature.
- **Direct farm subsidies:** These are the kinds of subsidies in which direct cash incentives are paid to the farmers in order to make their products more competitive in the global markets
- **Indirect farm subsidies:** These are the farm subsidies which are provided in the form of cheaper credit facilities, farm loan waivers, reduction in irrigation and electricity bills, fertilizers, seeds and pesticides subsidy as well as the investments in agricultural research, environmental assistance, farmer training, etc. These subsidies are also provided to make farm products more competitive in the global market.

Food Security

- Food security means making food available at affordable prices at all times, to all, without interruptions.
- India attained self-sufficiency in food by late 1980s, though food security still evades the country.
- Lack of food security hampers the nutritional profile of the vulnerable section of the population.
- As per the State of Food Insecurity in the World, 2015 (FAO), India has the second highest number of undernourished people at 194.6 million which is around 15.2 per cent of the world's total undernourished population.
- Two important things need attention regarding India's food security –
- Around 27 per cent of India's population is BPL and a greater portion (one conservative estimate puts it at 75 per cent) of their household income is spent on food.
- There is a strong correlation between stability in agricultural production and food security. Volatility in agricultural production impacts food supplies and can result in spikes in food prices, which adversely affect the lowest income groups of the population.
- Therefore, **along with provision of food subsidy, stability in agricultural commodity prices is essential for making the poorer sections food secure.**
- Due to high level of undernourishment and volatility in agricultural prices, India has one of the largest number of food schemes in the World to ensure food security –
  - There is entitlement feeding programmes like the Integrated Child Development Scheme (ICDS – covers all Children under six, pregnant and lactating mothers)
  - Mid-Day Meal Schemes (MDMS),

- Food subsidy programmes like the Targeted Public Distribution System (through which the National Food Security Act is being implemented)
- Annapurna (10 kgs of free food grain for destitute poor) and the
- Employment Programmes like Mahatma Gandhi National Rural Employment Guarantee Scheme (100 days of employment at minimum wages) to ensure food security.

PDS & Food subsidy

- The Public Distribution System (PDS was changed to Targeted PDS in 1997) strives to ensure food security through timely and affordable distribution of food grains to the BPL population as this section cannot afford to pay market prices for their food.
- This involves procurement of food grain at MSP by the Government, building up and maintenance of food stocks, their storage, and timely distribution, making food grains accessible at reasonable prices to the vulnerable sections of the population.

Institutions/Schemes related to Agricultural Marketing

Agricultural Produce Market Committee (APMC)

- Agricultural Produce Market Committee (APMC) is a statutory market committee constituted by a State Government under the Agricultural Produce Market Committee Act in respect of trade in certain notified agricultural or horticultural or livestock products.
- APMCs are intended to be responsible for: Ensuring transparency in pricing system and transactions taking place in market area;
  - Providing market-led extension services to farmers;
  - Ensuring payment for agricultural produce sold by farmers on the same day;
  - Promoting agricultural processing including activities for value addition in agricultural produce;
  - Publicizing data on arrivals and rates of agricultural produce brought into the market area for sale; and Setup and promote public private partnership in the management of agricultural markets
  - There are about 2477 principal regulated markets based on geography (the APMCs) and 4843 sub-market yards regulated by the respective APMCs in India.

Model APMC Act 2003

- The monopoly of Government regulated wholesale markets has prevented development of a competitive marketing system in the country. An efficient agricultural marketing is essential for the development of the agriculture sector as it provides outlets and incentives for increased production, the marketing system contribute greatly to the commercialization of subsistence farmers. Worldwide Governments have recognized the importance of liberalized agriculture markets. In accordance with above objectives, Model APMC act was drafted by ministry of agriculture in 2003.

Major Features:

- It provides for direct sale of farm produce to contract farming sponsors.
- It provides a provision for setting up “Special markets” for “specified agricultural commodities”
- It permits private persons, farmers and consumers to establish new markets for agricultural produce in any area.
- Every market shall levy market fee on sale or purchase of agriculture commodities which brought from within or outside state.
- Replaces licensing with registrations of market functionaries and trade at any market area within state.
- Market Committees permitted to use its funds to create facilities like grading, standardization and quality certification; to create infrastructure for post-harvest handling of agricultural produce and development of modern marketing system.

- State Governments conferred power to exempt any agricultural produce brought for sale in market area, from payment of market fee.
- State Agricultural Marketing Board made responsible for grading and standardization.

National Agriculture Market (eNAM)

- eNAM is an online trading platform for agricultural commodities in India.
- It seeks to network the existing Agricultural Produce Market Committees (APMCs) and other market yards to create a unified national market for agricultural commodities.
- NAM is a "virtual" market but it has a physical market (mandi) at the back end.
- Following are the benefits of eNAM:
  - The market facilitates farmers, traders and buyers with online trading in commodities.
  - The market is helping in better price discovery and provides facilities for smooth marketing of their produce.
  - Over 90 commodities including staple food grains, vegetables and fruits are currently listed in its list of commodities available for trade.
  - The eNAM markets are proving popular as the crops are weighed immediately and the stock is lifted on the same day and the payments are cleared online.

Tribal Cooperative Marketing Development Federation of India (TRIFED)

- The Tribal Cooperative Marketing Development Federation of India (TRIFED) came into existence in 1987.
- It is a national-level apex organization functioning under the administrative control of Ministry of Tribal Affairs, Government of India. TRIFED organizes National Tribal Craft Expo called "**AADISHILP**", painting exhibition called "Aadi Chitra", "OCTAVE" for North Eastern Artisans and Tribal Artisan Melas to facilitate the sale of their products.
- Promote sustainable livelihood systems for tribal people by marketing development and ensuring remunerative price for their products, provide minimum support price and value addition of Non-Timber Forest Produce (Minor Forest Produce), empower them through meticulous capacity building, augment their resources substantially, Develop marketing partnership with Central/State Government agencies and other development partners through establishing convergence and coherence in activities.

National Agricultural Cooperative Marketing Federation of India Ltd (NAFED)

- NAFED is an apex organization of marketing cooperatives for agricultural produce in India, under Ministry of Agriculture, Government of India.
- It was founded in October 1958 to promote the trade of agricultural produce and forest resources across the nation.
- NAFED is now one of the largest procurement as well as marketing agencies for agricultural products in India.
- With its headquarters in New Delhi, NAFED has four regional offices at Delhi, Mumbai, Chennai and Kolkata, apart from 28 zonal offices in capitals of states and important cities.
- In 2008, it established, National Spot Exchange, a Commodities exchange as a joint venture of Financial Technologies (India) Ltd. (FTIL).

Promotion of National Market through Agri Tech Infrastructure Fund (ATIF)

- The Scheme envisages initiation of e-marketing platform at the national level and will support creation of infrastructure to enable e-marketing in 642 regulated markets across the country.
- For creation of a National Market, a common platform across all States is necessary.

- It is, therefore, proposed that a Service Provider be engaged centrally who would build, operate and maintain the e-platform on BOOT Project model (Build, Own, Operate, Transfer - BOOT) it is a PPP project model.
- This platform would be customized/ configured to address the variations in different states.
- As an initiative of deregulation, states have been advised by the Government of India to bring fruits and vegetables out of the ambit of APMC Act. In pursuance of this advisory, 12 States have, so far, either de-regulated the marketing of fruits and vegetables or have exempted from levying of market fee.

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SERVICE SECTOR

- India's services sector has not only outperformed other sectors of the Indian economy, but has also played an important role in India's integration with world trade and capital markets.
- There is, however, a concern about the sustainability of a services-led growth process which largely stems from exports of skill-based services.
- The prevailing view is that for services growth to **be sustained**, the sector cannot remain dependent on external demand. **It must also be driven by internal demand**.
- More broad-based growth within the services is also required to ensure balanced, equitable and employment oriented growth, with backward and forward linkages to the rest of the economy.
- In this regard further infrastructural and regulatory reforms and FDI liberalization in services can help diversify the sources of growth within India's services sector and provide the required momentum.
- In recent years, there has been a debate in the country regarding the selection of the sector which can lead the growth process in the country. This debate originated from the fact that the services sector contributed over 62 per cent in the GDP during the decade 2001–12.

India and Global Services

Services sector have been hit hard after the Great Recession among the western developed economies. Rather during 2017 there was a strong signal of recovery reported from this part of the world which had a positive impact on the services-oriented countries. Latest features about the services sector at global and India levels are as given below:

- As per the latest data4, India's ranking improved from 14th position in 2006 to 7th position in 2016, among the world's 15 largest economies in terms of overall GDP.
- In 2016, services GVA growth rate (at constant prices), was highest in India at 7.8 per cent followed by China at 7.4 per cent. As per the ILO's estimates, among the top 15 economies, the services sector accounted for more than two thirds of total employment in 2016 in most of them except India and China, with India's share of 30.6 per cent being the lowest.
- Services export growth, both for World and India, which had dipped to negative territory in 2015 after an interregnum of six years from 2009, returned to positive territory in 2016.
- As per the latest WTO data for 2017 (first half) world's services export growth was 4.3 per cent while it was 9.9 per cent for India (0.2 per cent for China and the highest 18.4 per cent for Russia).

Services Performance of India

Major feature of India's services performance are as given below:

- Out of the 32 States and UTs, it is the dominant sector, contributing over 50 per cent of the gross state value added (GSVA) in 15 states and UTs. The major services in most of the states are trade, hotels and restaurants, followed by real estate, ownership of dwellings and business services.
- The GVSAs show wide variation in terms of share and growth of services—Delhi and Chandigarh are at the top with over 80 per cent share, while Sikkim is at the bottom with 31.7 per cent share.

- In terms of services GSVA growth, Bihar is at the top and Uttar Pradesh at the bottom with 14.5 per cent and 7.0 per cent growth respectively in 2016-17.

FDI Inflows into Services Sector

- FDI data from the Department for Promotion of Industry and Internal Trade shows that gross FDI equity inflows (excluding re-invested earnings) into the services sector witnessed a strong recovery during April-September 2019 following a decline in 2018-19.
- Gross FDI equity inflows jumped by 33 per cent YoY during April-September 2019 to reach US$ 17.58 billion, accounting for about two-thirds of the total gross FDI equity inflows into India during this period.
- The jump in FDI equity inflows was driven by strong inflows into subsectors such as **'Information & Broadcasting', 'Air Transport', 'Telecommunications', 'Consultancy Services' and 'Hotel & Tourism'.**

Trade in Services Sector

- RBI's Balance of Payments data suggests that services exports during April-September 2019 maintained their momentum from 2018-19, with a growth (YoY) of 6.4 per cent.
- The jump in export growth of **travel, software, business and financial services offset the contraction in export growth of insurance and other services (including construction, etc.)**
- The robust growth in business services exports was driven by **higher receipts for R&D services, professional and management consultancy services, and technical and trade related services.**
- Trends in the composition of services exports over the past decade show that the shares of traditional services, such as **transport, and value-added services, such as software, financial services and communications, have witnessed a decline**.
- Meanwhile, the share of **travel services has increased over the past decade and that of business services has risen slightly.**
- The share of **software services has declined by 4 percentage points** over the past decade to reach 40 per cent of total services exports in 2018-19.
- Yet, **India's services exports remain concentrated in software services, accounting for twice the share of the second-largest component, business services.**
- This has made the software sector, and therefore overall services exports, susceptible to changes in exchange rate, global IT spending, stringent USA visa norms, and rising cost pressures due to increased local hiring in export destinations.
- Even though global IT spending, as projected by Gartner in October 2019, is expected to accelerate in 2020, rising production costs and uncertainty related to Brexit and USA's visa norms pose downward risks to India's software exports.
- Services import growth (YoY) during April-September 2019 was 7.9 per cent.
- **An increase in import growth for transport, software, communication and business services offset the contraction in imports of financial and insurance services and the slowdown in imports of travel services.**
- Increased business services payments were primarily driven by professional, management and consultancy services and technical and trade related services.
- Besides software services, India runs a small trade surplus in travel, insurance and financial services.
- However, within travel services, India persistently runs a trade deficit in education services with education imports, i.e., expenditure incurred by Indian students traveling abroad for education purposes on tuition, room and boarding, reaching about US$ 3 billion in 2018-19.
- Adding to this other payments for education purposes such as fees paid for correspondence courses abroad, which constitute as payments for receiving education services abroad, there has been a marked increase in India's education services imports in the recent years amounting to US$ 5.0

billion in 2018-19.

- From a long-run perspective, India's focus on boosting services exports during bilateral trade negotiations augurs well for mitigating bilateral trade deficits with trading partners.
- Looking ahead, world trade volume for goods and services are projected to recover in 2020 following a deceleration in 2019.
- Global uncertainty, protectionism and stricter migration rules would be key factors in shaping India's services trade ahead.

Manufacturing vs. Services

- All the focus being on the manufacturing exports in India has distracted attention from what might be a no less noteworthy development.
- In past few years, it is India's exports of services that has changed in the most significant, and perhaps alarming, way.
- What makes this development puzzling is that in recent years the composition of Indian exports of services is more favourable than that of Indian exports of manufactured goods. More of the former goes to the United States, and more of the latter to Asia.
- Realising India's medium-term growth potential of 8-10 per cent will require rapid growth of exports.
- How rapid this should be is suggested by comparing India's export performance in services with China's performance in manufacturing at a comparable stage of the growth surge.
- India's competitiveness will have to improve so that its services exports, currently about 3 per cent of world exports, capture nearly 15 per cent of world market share. That is a sizeable challenge, and recent trends suggest that a major effort at improving competitiveness will be necessary to meet it.

Global negotiations

India aims to position itself as a key player in world services trade. To promote services exports, the government has taken a number of policy initiatives – SEIS (Service Exports from India Scheme) for increasing exports of notified services from India; organising GES (Global Exhibitions on Services); and SCs (Services Conclaves). Besides, some initiatives in sectors like tourism and shipping have also been taken in this regard. Given the potential of India's services exports, services-sector negotiations both at multilateral and bilateral and regional levels are of vital importance to India. Some of the recent negotiations are as given below.

WTO negotiations

Though, the 11th Ministerial Conference (MC) of the WTO ended without a Ministerial Declaration or any substantive outcome, India saw certain favourable outcome from the 10th MC of the multi-lateral trade body

- Implementation of preferential treatment in favour of services and service suppliers of least developed countries (LDC) and increasing LDC participation in services trade;
- To maintain the current practice of not imposing customs duties on electronic transmissions (e-Commerce) until the next Ministerial Conference to be held in 2017.
- India, together with 20 other members have notified preferential treatment to LDCs in services trade. India has offered this in respect of:
    - Market access
    - Technical assistance and capacity building; and
    - Waiver of visa fees for LDC applicants for business and employment.

Bilateral Agreements

The bilateral agreements signed by India in recent times are:

- Comprehensive bilateral trade agreements signed, including trade in services, with the governments of Singapore, South Korea, Japan and Malaysia. An FTA in services and investment was signed with the Association of South East Asian Nations (ASEAN) effective since mid2015.
- India has joined the RCEP (Regional Comprehensive Economic Partnership) pluri- lateral negotiations. The proposed FTA includes the 10 ASEAN countries and its six FTA partners, viz. Australia, China, India, Japan, South Korea and New Zealand. The RCEP is the only mega-regional FTA of which India is a part.
- India is also engaged in bilateral FTA negotiations including trade in services with Canada, Israel, Thailand, the EU, the EFTA (European Free Trade Association), Australia and New Zealand. Dialogue is under way with the US under the India-US Trade Policy Forum (TPF), with Australia under the India-Australia JMC (Joint Ministerial Commission), with China under the India-China Working-Group on Services, and with Brazil under the India-Brazil Trade Monitoring Mechanism (TMM).

Restrictions and Regulations

- One major issue in services is the domestic barriers and regulations.
- Domestic regulations, in strict WTO terms, include licensing requirements, licensing procedures, qualification requirements, qualification procedures, and technical standards but here other restrictions and barriers are also considered.
- While there are many domestic regulations in our major markets, which deny market access to us and therefore need to be negotiated at multilateral and bilateral levels, there are also many domestic regulations in India which hinder the growth of this sector.
- Since domestic regulations perform the role of tariffs in regulating services, there is need to list the domestic regulations in India which need to be curbed to help growth of the sector and its exports, while retaining those which are necessary for regulating the sector at this stage.
- An indicative list of some important domestic regulations in India which need to be examined for suitable policy reforms9 in the services sector is as follows:
  - trade and transport services
  - construction development
  - **Accountancy services**
  - **legal services**
  - **education services**

The need for reforms

- Indian services sector have the potential to garner higher economic benefits to the country.
- But there are many issue both general and sector specific including domestic regulations hinder the growth prospects of the services sector.
- If these issues are addressed deftly the sector could lead to exponential gains for the economy.
- The need of policy reforms in this regards are outlined in the following way:

General Issues

There are some general issues related to the policy framework which hamper the healthy growth and expansion of the services sector in the country. They are broadly related to the following areas:

Nodal agency and marketing:

Despite having strong growth potential in various services sub-sectors, there is no single nodal department or agency for services. An inter-ministerial committee for services has been set up to look into this. But services activities cover issues beyond trade and a more proactive approach and proper institutional mechanism is needed to weed out unwanted regulations and tap the opportunities in the services sector in a coordinated way.

Disinvestment:

There is plenty of scope for disinvestment in services PSUs under both central and state governments. Speeding up disinvestment in some services-sector PSUs could not only provide revenue for the government but also speed up the growth of these services.

Credit related:

The issues here include 'collateral **free' soft loans to support the sector's** cash needs and possibility of considering even export or business orders as collateral for credit-worthy service firms.

Tax and Trade Policy related:

These include use of 'net' instead of 'gross' foreign exchange criteria for export benefit schemes, the issue of retrospective amendments of tax laws like,

- Amendment to the definition of royalty to include payment of any rights via any medium for use of computer software,
- Tax administrative measures to tackle delay in refunds,
- Introducing VAT (value added tax) refund for foreign tourists, and
- Addressing the issue of bank guarantees based on past performance to avail of export promotion benefits in services.

Outlining future

With plenty of opportunities, the services sector is like an uncharted sea. As yet, its potential has not been tapped fully by India. A targeted policy of removing bottlenecks in major and potential services can result in large dividends in the form of higher services growth and services exports, which in turn can help in pulling up the economy to higher growth levels. The future actions in the sector can be outlined as given below:

- India's services sector, which showed resilient growth after the recovery of the global economy following the global financial crisis, has been showing subdued performance in recent times. Despite the slowdown, the prospects continue to be bright for many segments of the sector. (ii)
- In future, government's focus on the following are expected to provide impetus to logistics services—
  - infrastructure development,
  - favourable regulatory policies like liberalisation of FDI norms,
  - increasing number of multimodal logistics service providers,
  - growing trend of outsourcing logistics to third party service providers, and
  - entry of global players.
- Though shipping services are at a low key at present, with increased imports of POL (petroleum, oil and lubricants) for stocks build up to take advantage of low crude oil prices, containerisation of export and import cargo and modernisation of ports with private sector participation, recovery of the shipping and port services sector can be expected.
- The prospects for Indian aviation services have improved following—
  - the fall in prices of aviation fuel, which accounts for nearly 40 per cent of the operating expenses of airlines in India;
  - liberalisation of FDI policies in civil aviation; and
  - strong growth in passenger traffic – expected to continue in the near future.
- The outlook for the retail industry remains positive as India continues to remain an attractive long-term retail destination despite the various challenges faced by the sector. Following initiatives are expected to give a fillip to the sector—
  - allocation of Rs. 1000 crore to technology and start-up sectors,

- promotion of cashless transactions via RUPay debit cards, and
- growth of e-commerce.

- Government's focus on the tourism sector including easing visas by eTV and building tourism infrastructure could help in the recovery of the tourism sector.
- Despite challenges in the global market, the Indian IT industry is expected to maintain double or near-double- digit growth as India offers depth and breadth across different segments of this industry, such as, IT services, BPM, ER&D, internet and mobility and software products.
- In the telecom sector, the introduction of 4G which could be a game changer and inclusion of fibre optic connectivity which will tremendously increase the reach and bandwidth along with greater use of mobiles in government's social sector programmes could give a further boost to this fast growing sector.

Several relevant and contemporary suggestions have been articulated by a Working Paper of the Ministry of Finance by late February 2016. Dealing with the sectors like tourism, shipping and port, IT and software the advices are deeper and effective

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FINANCIAL SECTOR

- The market of an economy where funds are transacted between the fund-surplus and fund scarce individuals and groups is known as the financial market.
- The basis of transaction is either interest or dividend. This market might have its organised (institutionalised) as well as non-organised (unregulated/non-institutionalised) segments in an economy.
- Financial markets in every economy are having two separate segments today, one catering to the requirements of short-term funds and the other to the requirements of long-term funds.
- The short term financial market is known as the **money market**, while the long-term financial market is known as the **capital market**.

Indian Money Market

- Money market is the short-term financial market of an economy.
- In this market, money is traded between individuals or groups (i.e., financial institutions, banks, government, companies, etc.), who are either cash-surplus or cash-scarce.
- Trading is done on a rate known as discount rate which is determined by the market and guided by the availability of and demand for the cash in the day-to-day trading.
- The **'repo rate'** of the time (announced by the RBI) works as the guiding rate for the current **'discount rate'.**
- In the money market the financial assets, which have quick conversion quality into money and carry minimal transaction cost, are also traded.

Need for Money Market:

- In the modern industrial economies creation of productive assets is not an easy task, as it requires investible capital of longterm nature.
- Long-term capital can be raised either through bank loans, corporate bonds, debentures or shares (i.e., from the capital market).
- But once a productive asset has been created and production starts there comes the need of another kind of capital, to meet the day-to-day shortfalls of working capital.
- It means that only setting-up of firms does not guarantee production as these firms keep facing fund mismatches in the day-to-day production process.
- Such funds are required only for a short period (days, fortnights or few months) and are needed to meet shortfalls in working capital requirements.
- This requires creation of a different segment of the financial market which can cater to the short-term requirements of such funds for the eneterprises—known as the money market or the working capital market.
- The short-term period is defined as upto 364 days.

Money Market in India:

- The organized form of money market in India is just close to three decades old. However, its presence has been there, but restricted to the government only.
- It was the **Chakravarthy Committee (1985)** which, for the first time, underlined the need of an organized money market in the country and the **Vahul Committee (1987)** laid the blue print for its development.
- Today, money market in India is not an integrated unit and has two segments— **Unorganized Money Market and Organized Money Market.**

Unorganized Money Market

Before the government started the organized development of the money market in India, its unorganized form had its presence since the ancient times—its remnant is still present in the country. Their activities are not regulated like the organized money market, but they are recognized by the government. In recent years, some of them have been included under the regulated organized market (for example, the NBFCs were put under the regulatory control of the RBI in 1997). The unorganized money market in India may be divided into three differing categories:

- **Unregulated Non-Bank Financial Intermediaries:** Unregulated Non-Banking Financial Intermediaries are functioning in the form of chit funds, nidhis (operate in South India, which lend to only their members) and loan companies. They charge very high interest rates (i.e., 36 to 48 per cent per annum), thus, are exploitative in nature and have selective reach in the economy.
- **Indigenous Bankers:** Indigenous bankers receive deposits and lend money in the capacity of an individual or private firm. There are, basically, four such bankers in the country functioning as non-homogenous groups:
  - *Gujarati Shroffs:* They operate in Mumbai, Kolkata as well as in industrial, trading and port cities in the region.
  - *Multani or Shikarpuri Shroffs:* They operate in Mumbai, Kolkata, Assam tea gardens and North Eastern India.
  - *Marwari Kayas:* They operate mainly in Gujarat with a little bit of presence in Mumbai and Kolkata.
  - *Chettiars:* They are active in Chennai and at the ports of southern India.
- **Money Lenders:** They constitute the most localized form of money market in India and operate in the most exploitative way. They have their two forms:
  - The professional money lenders who lend their own money as a profession to earn income through interest.
  - The non-professional money lenders who might be businessmen and lend their money to earn interest income as a subsidiary business.

Organized money market

Since the government started developing the organized money market in India (mid-1980s), we have seen the arrival of a total of eight instruments designed to be used by different categories of business and industrial firms. A brief description of these instruments follows:

- **Treasury Bills (TBs):** This instrument of the money market though present since Independence got organized only in 1986. They are used by the Central Government to fulfill its short-term liquidity requirement upto the period of 364 days.
- **Certificate of Deposit (CD):** Organized in 1989, the CD is used by banks and issued to the depositors for a specified period ranging less than one year—they are negotiable and tradable in the money market. Since 1993 the RBI allowed the financial institutions to operate in it— IFCI, IDBI, IRBI (IIBI since 1997) and the Exim Bank—they can issue CDs for the maturity periods above one year and upto three years.
- **Commercial Paper (CP):** Organized in 1990 it is used by the corporate houses in India (which should be a listed company with a working capital of not less than Rs. 5 crore). The CP issuing companies

need to obtain a specified credit rating from an agency approved by the RBI (such as CRISIL, ICRA, etc).

- **Commercial Bill (CB):** Organised in 1990, a CB is issued by the All India Financial Institutions (AIFIs), NonBanking Finance Companies (NBFCs), Scheduled Commercial Banks, Merchant Banks, Co-operative Banks and the Mutual Funds. It replaced the old Bill Market available since 1952 in the country.
- **Call Money Market (CMM):** This is basically an inter-bank money market where funds are borrowed and lent, generally, for one day—that is why this is also known as over-night borrowing market (also called money at call). Fund can be borrowed/raised for a maximum period upto 14 days (called short notice).
- **Money Market Mutual Fund (MF):** Popular as Mutual Funds (MFs) this money market instrument was introduced/organised in 1992 to provide short-term investment opportunity to individuals.
- **Repos and Reverse Repos:** In the era of economic reforms there developed two new instruments of money market— **repo and reverse repo. Repo** allows the banks and other financial institutions to borrow money from the RBI for short-term (by selling government securities to the RBI). **In reverse repo**, the banks and financial institutions purchase government securities from the RBI (basically here the RBI is borrowing from the banks and the financial institutions).
- **Cash Management Bill (CMB):** The Government of India, in consultation with the RBI, decided to issue a new short-term instrument, known as Cash Management Bills, since August 2009 to meet the temporary cash flow mismatches of the government. The Cash Management Bills are non-standard and discounted instruments issued for maturities less than 91 days.

Mutual Funds

- Of all investment options, mutual funds are touted to be the best tool for wealth creation over the long term. They are of several types, and the risk varies with the kind of asset classes these funds invest in.
- As the name suggests, a mutual fund is a fund that is created when a large number of investors put in their money, and is managed by professionally qualified persons with experience in investing in different asset classes—shares, bonds, money market instruments like call money, and other assets such as gold and property.
- Mutual funds, first of all came in the money market (regulated by the RBI), but they have the freedom to operate in the capital market, too. This is why they have provision of dual regulator—the RBI and SEBI.
- Mutual funds are compulsorily registered with the Securities and Exchange Board of India (SEBI), which also acts as the first wall of defence for all investors in these funds.
- Each mutual fund is run by a group of qualified people who form a company, called an asset management company (AMC) and the operations of the AMC are under the guidance of another group of people, called trustees.
- There are three types of schemes offered by MFs:
  - **Open-ended Schemes:** An open-ended fund is one which is usually available from an MF on an ongoing basis, that is, an investor can buy or sell as and when they intend to at a NAV-based price. As investors buy and sell units of a particular open-ended scheme, the number of units issued also changes every day and so changes the value of the scheme's portfolio. So, the NAV also changes on a daily basis. In India, fund houses can sell any number of units of a particular scheme, but at times fund houses restrict selling additional units of a scheme for some time.
  - **Closed-ended Schemes**: A close-ended fund usually issue units to investors only once, when they launch an offer, called new fund offer (NFO) in India. Thereafter, these units are listed on the stock exchanges where they are traded on a daily basis. As these units are listed, any investor can buy and sell these units through the exchange.
  - **Exchange-Traded Funds (ETFs):** ETFs are a mix of open-ended and close-ended schemes. ETFs, like close-ended schemes, are listed and traded on a stock exchange on a daily basis, but the price is usually very close to its NAV, or the underlying assets, like gold ETFs.

Indian Capital Market

- The long-term financial market of an economy is known as the 'capital market'. This market makes it possible to raise long-term money for a period of minimum 365 days and above.
- Across the world, banks emerged as the first and the foremost segment of the capital market.
- In coming times many other segments got added to it, viz., insurance industry, mutual funds, and finally the most attractive and vibrant, the security/stock market.
- Organised development of capital market together with putting in place the right regulatory framework for it, has always been a tough task for the economies.
- It is believed today that for strong growth prospects in an economy presence of a strong and vibrant capital market is essential.
- Over the time, Indian capital market started to have the following segments:

Financial institutions

- The requirement of project financing made India to go for a number of FIs from time to time, which are generally classified into four categories:
  - **All India Financial Institutions (AIFIs)**
    - The all India FIs are IFCI (1948); ICICI (1955); IDBI (1964); SIDBI (1990) & IIBI (1997).
    - All of them were public sector FIs except ICICI, which was a joint sector venture with initial capital coming from the RBI, some foreign banks and FIs.
    - The public sector FIs were funded by the Government of India.
    - The AIFIs witnessed a sharp decline in recent years. At this juncture the government decided to convert them into Development Banks (suggested by the Narasimhan Committee-I) to be known as the All India Development Banks (AIDBs).
    - In 2000, the government allowed ICICI to go for a reverse merger (when an elder enterprise is merged with a younger one) with the ICICI Bank—the first AIDB emerged with no obligation of project financing—such entities in coming times will be known as the **universal banks.**
    - In 2002, the government, proposed to merge IFCI and IIBI with the nationalized bank PNB to create big Universal Bank.
    - Meanwhile, at present, there are **only four financial institutions** operating in the country as AIFIs regulated by the RBI, viz., the NABARD, SIDBI, Exim Bank and the NHB.
  - **Specialized Financial Institutions (SFIs)**
    - Two new FIs were set up by the Central Government in the late 1980s to finance risk and innovation in the area of industrial expansion; this was India's trial in the area of venture capital funding.
    - **IFCI Venture Capital Funds Ltd (IFCI Venture), 2000: It was promoted as a Risk Capital** Foundation (RCF) in 1975 by IFCI Ltd., a society to provide financial assistance to first generation professionals and technocrat entrepreneurs for setting up own ventures through soft loans, under the Risk Capital Scheme.
    - **Tourism Finance Corporation of India Ltd (TFCI), 1989:** The Government of India had, on the recommendations of the National Committee on Tourism (Yunus Committee) set up under the aegis of the Planning Commission, decided in 1988, to promote a separate All India Financial Institution for providing financial assistance to tourism-related activities/projects. In accordance with the above decision, the IFCI Ltd. along with other all-India financial/investment institutions and some nationalized banks promoted a Public Limited Company under the name of "Tourism Finance Corporation of India Ltd. (TFCI)" to function as a Specialized All-India Development Financial Institution to cater to the financial needs of the tourism industry.
  - **Investment Instituions (IIs)**
    - Three investment institutions also came up in the public sector, which are yet another kind of FIs, i.e., the LIC (1956), the UTI (1964) and the GIC (1971).

- In the present time they are no more known as DIIs (Domestic Investment Institutions) or DFIs (Domestic Financial Institutions).
- LIC is now the public sector insurance company in the life segment, GIC was been converted into a public sector re-insurance company in 2000, while UTI was converted into a mutual fund company in 2002.
- LIC is now called an ‘insurance company’, part of the Indian Insurance Industry and is the lone public sector playing in the life insurance segment competing with the private life insurance companies.
- Similarly, the UTI is now part of the Indian Mutual Fund industry and the lone such firm in the public sector competing with other private sector mutual funds.
- Similarly, the erstwhile four public sector general insurance companies are part of India’s general insurance industry and competing with private companies in the area.

- **State Level Finance Institutions (SLFIs)**
  - In the wake of states involvement in the industrial development, the central government allowed the states to set up their own financial institutions (after the states demanded so). In this process two kinds of FIs came up:
  - **State Finance Corporations (SFCs):** First came up in Punjab (1955) with other states following its example. There are 18 SFCs working presently.
  - **State Industrial Development Corporations (SIDCs):** A fully dedicated state public sector FI to the cause of industrial development in the concerned states. First such FIs were set up (1960) in Andhra Pradesh and Bihar.

- **Banking Industry**
  - With the passage of time, the industry saw its nationalisation (1969 and 1980) and again opening up for private sector entry (1993–94) to emerge as the most dependable segement of Indian financial system—in a way its mainstay.
  - Presently, the industry consists of commercial banks both in public and private sectors, Regional Rural Banks (RRBs) and co-operative banks—a total of 171 Scheduled Commercial Banks (SCBs) out of which 113 are in the public sector (19 nationalised banks, 7 banks in SBI group, one IDBI Bank Ltd. and 86 RRBs); with the rest of the 58 banks owned by the private sector (domestic and foreign—FDI in banks is allowed upto 26 per cent).
- **Insurance Industry**
  - After Independence, for the purpose of expanding the industry, one after another the life and nonlife insurance businesses were nationalised by the government (in 1956 and 1970, respectively), and the public sector insurance companies did serve the better purpose in the areas of providing safety net and nation-building.
  - In the wake of the process of economic refroms a restructuring of the sector was started and the industry was opened for entry of private players in 1999 and an independent regulator was set up—the IRDA (domestic and foreign—with an FDI cap of 49 per cent).
  - Since then many private players have entered the industry.
  - Presently, Indian insurance industry consists of **one public sector life insurer** (LIC) **and four public sector general insurers; two specialised public sector insurers (AICIL and ECGC); one public sector re-insurer (GIC) and 37 private insurance companies (in collaboration with established foreign insurers from across the world).**
- **Security market**
  - After the government’s attempts to formally organise the security and stock market of India, the segment has seen accelerated expansion.
  - Today, it is counted among the most vibrant share markets of the world and has challenged the monopoly of banks in the capital market of the country.
  - The security market of India is regulated by SEBI. India has developed a regulated ‘forward market’ also where hunderds of commodities and derivatives are traded on spot and non-spot basis—regulated by FMC which merged into SEBI by late 2015.

Financial Regulation

- India has a multiple regulatory architecture in the financial sector. The design has developed complexities over the time due to: the number of regulatory, quasi-regulatory, non-regulatory but-still-regulating bodies; overlapping ambiguous operational design and their influence. A brief overview of the financial regulatory framework is being given here.

Regulatory Agencies

- India has product-wise regulators—Reserve Bank of India (RBI) regulates credit products, savings and remittances; the Securities and Exchange Board of India (SEBI) regulates investment products; the Insurance Regulatory and Development Authority (IRDA) regulates insurance products; and the Pension Fund Regulatory and Development Authority (PFRDA) regulates pension products. The Forward Markets Commission (FMC) regulates commodity-based exchange-traded futures (which was merged with the SEBI by late 2015).

Quasi-regulatory Agencies

- Several other government bodies perform quasi-regulatory functions—National Bank for Agriculture and Rural Development (NABARD), Small Industries Development Bank of India (SIDBI), and National Housing Bank (NHB). NABARD supervises regional rural banks as well as state and district cooperative banks. NHB regulates housing finance companies, and SIDBI regulates the state finance corporations (SFCs).

Establishment of FSDC

- Few years back, an important addition was made to the regulatory architecture—the Financial Sector Development Council (FSDC) was set up which replaced the High Level Committee on Capital Markets. The council is convened by Ministry of Finance and does not have statutory authority—it is structured as a council of regulators—Finance Minister as chairman. It has a permanent secretariat.
- The council resolves inter-agency disputes; look after the regulation of financial conglomerates that fall under various regulators' purview; and performs wealth management functions dealing with multiple products.
- The FSLRC (Financial Sector Legislative Reforms Commission), set up (headed by Justice B. N. Srikrishna) to examine the regulatory structure and the laws governing the financial sector, submitted its report by early 2013.
- **Major highlights of the recommendations are as follows:**
  - Developing a 'horizontal structure' whereby, the basic regulatory/monitoring functions to be done by a UIA (Unified Financial Agency)—in place of each agency (like SEBI, IRDA, etc.) looking after one financial type and area. It will eliminate regulatory overlap (due to which the ULIP controversy happened between the SEBI and IRDA).
  - Setting up a FRA (Financial Redressal Agency) to handle consumer complaints, regardless of area. It means, regulator not to oversee the consumer complaints.
  - FSAT (Financial Sector Appellate Tribunal) to be set up to hear the appeals of entire financial sector.
  - Advice to set up three other agencies which will oversee banking, besides the RBI.

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EXTERNAL SECTOR

All economic activities of an economy which take place in foreign currency fall in the external sector such as export, import, foreign investment, external debt, current account, capital account, balance of payment, etc.

Forex reserves

- The total foreign currencies (of different countries) an economy possesses at a point of time is its 'foreign currency assets/reserves'.
- The Forex Reserves (short for 'foreign exchange reserves') of an economy is its 'foreign currency assets' added with its gold reserves, SDRs (Special Drawing Rights) and Reserve Tranche in the IMF.
- In a sense, the Forex reserves is the upper limit upto which an economy can manage foreign currency in normal times if need be.

Exchange Rate

- As India started managing its balance of payment in a more prudent way after the reform period, its external debt position has also improved in a big way. Exchange rate is the value for domestic currency with respect to foreign currency and vice-versa. In India, exchange rates are managed and any capital inflows would be mopped up by RBI to prevent rupee from appreciating thus resulting in build of reserves. They can be either fixed exchange rate or market determined exchange rates.

Fixed currency regime

- A method of regulating exchange rates of world currencies brought by the IMF.
- In this system exchange rate of a particular currency was fixed by the IMF keeping the currency in front of a basket of important world currencies (they were UK£, US $, Japanese ¥, German Mark DM and the French Franc FFr).
- Different economies were supposed to maintain that particular exchange rate in future.
- Exchange rates of currencies were modified by the IMF from time to time.

Floating currency regime

- A method of regulating exchange rates of world currencies based on the market mechanism (i.e., demand and supply).
- In the floating exchange rate system, a domestic currency is left free to float against a number of foreign currencies in its foreign exchange market and determine its own value.
- Such exchange rates, are also called as market driven or based exchange rates, which are regulated by factors such as the demand and supply of the domestic and the foreign currencies in the concerned economy.

Managed exchange rates

- A managed-exchange-rate system is a hybrid or mixture of the fixed and flexible exchange rate systems in which the government of the economy attempts to affect the exchange rate directly by buying or selling foreign currencies or indirectly, through monetary policy.
- Almost all countries tend to intervene when the markets become disorderly or the fundamentals of economics are challenged by the exchange rate of the time.

Foreign exchange market

- The market where different currencies can be bought and sold is called the foreign exchange market.
- Out of the trades in different currencies, the exchange rate of the currency is determined by the economy.
- This is an institutional framework for the exchange of one national currency for another.
- This is particularly correct either in the case of a free float exchange (i.e., floating currency) regime or is a managed or hybrid exchange rate system.
- It is altogether not allowed either in a fixed currency system or a hard fix (in a hard fix this happens once the currency to which the hard fix has been done itself starts fluctuating).

Exchange rate in India

- Indian currency, the 'rupee', was historically linked with the British Pound Sterling till 1948 which was fixed as far back as 1928.
- Once the IMF came up, India shifted to the fixed currency system committed to maintain rupee's external value (i.e., exchange rate) in terms of gold or the US ($ Dollar).
- In 1948, Rs. 3.30 was fixed equivalent to US $ 1. In September 1975, India delinked rupee from the British Pound and the RBI started determining rupee's exchange rate with respect to the exchange rate movements of the basket of world currencies (£, $, ¥, DM, Fr.).
- This was an arrangement between the fixed and the floating currency regimes.
- In 1992–93 financial year, India moved to the floating currency regime with its own method which is known as the **'dual exchange rate'**.
- There are two exchange rates for rupee, one is the '**official rate'** and the other is the '**market rate'.**
- None of the economies have till date followed an ideal free-floating exchange rate. They require some mechanism to intervene in the foreign exchange market because this is a highly speculative market.

Trade balance

- The monetary difference of the total export and import of an economy in one financial year is called trade balance. It might be positive or negative, known to be either favorable or unfavorable, respectively to the economy.

Trade Policy

- Broadly speaking, the economic policy which regulates the export-import activities of any economy is known as the trade policy.
- It is also called the foreign trade policy or the Exim Policy.
- This policy needs regular modifications depending upon the economic policies of the economies of the world or the trading partners.

Depreciation

- This term is used to mean two different things. In foreign exchange market, it is a situation when domestic currency loses its value in front of a foreign currency if it is market-driven. It means depreciation in a currency can only take place if the economy follows the floating exchange rate system. In domestic economy, depreciation means an asset losing its value due to its use, wear and tear or due to other economic reasons. Depreciation here means wear and tear. This is also known as capital consumption. Every economy has an official annual rates for different assets at which fixed assets are considered depreciating.

Devaluation

- In the foreign exchange market when exchange rate of a domestic currency is cut down by its government against any foreign currency, it is called devaluation. It means official depreciation is devaluation.

Revaluation

- A term used in foreign exchange market which means a government increasing the exchange rate of its currency against any foreign currency. It is official appreciation.

Appreciation

- In foreign exchange market, if a free floating domestic currency increases its value against the value of a foreign currency, it is appreciation.
- In domestic economy, if a fixed asset has seen increase in its value it is also known as appreciation.
- Appreciation rates for different assets are not fixed by any government as they depend upon many factors which are unseen.

Current Account

It has two meanings—one is related to the banking sector and the other to the external sector:

- In the banking industry, a business firms bank account is known as current account. The account is in the name of a firm run by authorised person or persons in which no interest is paid by the bank on the deposits. Every withdrawal from the account takes place by cheques with limitations on the number of deposits and withdrawals in a single day. The overdraft facility or the cash-cum-credit (c/c Account) facility to business firms is offered by the banks on this account only.
- In the external sector, it refers to the account maintained by every government of the world in which every kind of current transactions is shown—basically this account is maintained by the central banking body of the economy on behalf of the government. Current transactions of an economy in foreign currency all over the world are—export, import, interest payments, private remittances and transfers.

All transactions are shown as either inflow or outflow (credit or debit). At the end of the year, the current account might be positive or negative. The positive one is known as a surplus current account, and the negative one is known as a deficit current account.

Capital Account

- Every government of the world maintains a capital account, which shows the capital kind of transactions of the economy with outside economies.
- Every transaction in foreign currency (inflow or outflow) considered as capital is shown in this account—external lending and borrowing, foreign currency deposits of banks, external bonds issued by the Government of India, FDI, PIS and security market investment of the QFIs (Rupee is fully convertible in this case).
- There is no deficit or surplus in this account like the current account.

Balance of Payment (BoP)

- The outcome of the total transactions of an economy with the outside world in one year is known as the balance of payment (BoP) of the economy.
- Basically, it is the net outcome of the current and capital accounts of an economy.
- It might be favourable or unfavourable for the economy.
- However, negativity of the BoP does not mean it is unfavourable.
- A negative BoP is unfavourable for an economy if only the economy lacks the means to fill the gap of negativity.
- The BoP of an economy is calculated on the principles of accountancy (double-entry bookkeeping) and looks like the balance sheet of a company—every entry shown either as credit (inflow) or debit (outflow).
- If there is a positive outcome at the end of the year, the money is automatically transferred to the foreign exchange reserves of the economy.
- And if there is any negative outcome, the same foreign exchange is drawn from the country's forex reserves.
- If the forex reserves are not capable of fulfilling the negativity created by the BoP, it is known as a BoP crisis and the economy tries different means to solve the crisis in which going for forex help from the IMF is the last resort.

Convertibility in India

- India's foreign exchange earning capacity was always poor and hence it had all possible provisions to check the foreign exchange outflow, be it for current purposes or capital purposes (remember the draconian FERA). But the process of economic reforms has changed the situation to unidentifiable levels.

Current Account

- Current account is today **fully convertible** (operationalized on 19 August, 1994).
- It means that the full amount of the foreign exchange required by someone for current purposes will be made available to him at official exchange rate and there could be an unprohibited outflow of foreign exchange (earlier it was partially convertible).
- India was obliged to do so as per Article VIII of the IMF which prohibits any exchange restrictions on current international transactions (keep in mind that India was under pre-conditions of the IMF since 1991).

Capital Account

- After the recomendations of the **S.S. Tarapore Committee** (1997) on Capital Account Convertibility, India has been moving in the direction of allowing full convertibility in this account, but with required precautions. India is still a country of partial convertibility (40:60) in the capital account, but inside this overall policy, enough reforms have been made and to certain levels of foreign exchange requirements, it is an economy allowing full capital account convertibility—
  - Indian corporate are allowed full convertibility in the automatic route upto $500 million overseas ventures (investment by Ltd. companies in foreign countries allowed) per annum.
  - Indian corporate are allowed to prepay their external commercial borrowings (ECBs) via automatic route if the loan is above $ 500 million per annum.
  - Individuals are allowed to invest in foreign assets, shares, etc., upto the level of $ 2,50,000 per annum.
  - Unlimited amount of gold is allowed to be imported (this is equal to allowing full convertibility in capital account via current account route, but not feasible for everybody) which is not allowed now.

- The Second Committee on the Capital Account Convertibility (CAC)—again chaired by S.S. Tarapore—handed over its report in September 2006 on which the RBI/the government is having consultations.

Nominal Effective Exchange Rate (NEER) and Real Effective Exchange Rate (REER)

- The indices of Nominal Effective Exchange Rate (NEER) and Real Effective Exchange Rate (REER) are used as indicators of external competitiveness. NEER is the weighted average of bilateral nominal exchange rates of the home currency in terms of foreign currencies. Conceptually, the REER, defined as a weighted average of nominal exchange rates adjusted for relative price differential between the domestic and foreign countries, relates to the purchasing power parity (PPP) hypothesis.
- These are prepared jointly in the Division of International Finance, Department of Economic Analysis and Policy and the Department of External Investments and Operations, Reserve Bank of India.

Coverage

- The new six-currency indices represent the US, the Eurozone (comprising of 12 countries), UK, Japan, China and Hong Kong SAR. Two currencies in the existing five-country series, viz., French franc and Deutsche mark have been replaced by the Euro in the new indices. Two new currencies have been included in the new indices, both being Asian - the Chinese Yuan and the Hong Kong Dollar.
- The coverage has also been revised for the 36-country REER/NEER indices. The old indices comprised 36 countries including five members of the Euro Area. With an objective to broad base the REER/NEER and also to highlight India's changing trade pattern, countries have been chosen in the new series based on three broad criteria: (i) the share in India's exports and trade, (ii) regional representation and (iii) the regular availability of data on exchange rates and prices on a monthly basis.
- The new countries included in the revised series are Hong Kong SAR, Denmark, Iran, Kuwait, Qatar, Russia, South Africa, Sweden and United Arab Emirates (Annex). Besides, with the inclusion of the Euro zone, the new 36-currency indices include all the twelve countries that have Euro as common currency. Thus, the revised 36-currency REER indices effectively represent 47 countries.

Significance of REER

- REER is used to measure the value of a specific currency in relation to an average group of major currencies. A country's REER is an important measure when assessing its trade capabilities.
- The REER can be used to measure the equilibrium value of a country's currency, identify the underlying factors of a country's trade flow, and analyze the impact of other factors such as competition, and technological changes have on a country and ultimately the trade-weighted index.
- For example, if the U.S. dollar exchange rate weakened against the euro, U.S. exports to Europe become cheaper. European businesses or consumers buying U.S. goods need to convert their euros to dollars to buy our exports.
- If the dollar is weaker than the euro, it means Europeans can get more dollars for each euro. As a result, U.S. goods are cheaper due solely to the exchange rate between the euro and U.S. dollar.
- The real effective exchange rate is important because if the U.S. has a large trading relationship with Europe, the euro to U.S. dollar exchange would have a larger weighting in the index. As a result, a large move in the euro exchange rate would impact the REER more so than if another currency with a smaller weighting strengthened against the dollar.

Foreign Investment

- Foreign Direct Investment (FDI) FDI is a foreign investment which aims to maximize profit and provide unique mixture of resources, technology, knowledge, professionalism and management techniques.
- India's economy has been opening for more FDI. 100% FDI is permitted in sectors like petroleum sector, road building, power, drugs and pharmaceuticals hotels and tourism.
- No FDI is allowed in gambling, betting, lottery, atomic energy etc.

- FDI in India is allowed under Automatic Route i.e. without prior approval of government/RBI whereas other is government route which requires approval of FIPB.

Foreign Institutional Investment (FII)

- FII is done in the stock market with the purpose of only trading in shares of companies, in corporate debt and in government securities. Such investments are volatile in nature.
- There is no restriction on FII in the stock market except for the maximum percent shares of a company including in corporate debt instruments and government securities.
- FII also comes in the form of participatory notes (PN) (unregistered FII) and round tipping. Through round tipping, capital goes out of the country only to return from a different route to avoid incidence of tax on profit earned.
- Much of FII invested in India comes from Mauritius taking advantage of Double Taxation Avoidance Treaty.

Some key points from Mayaram Committee Report:

- Foreign investment of 10% or more in a listed company will now be treated as FDI.
- An investor may be allowed to invest below 10% and this can be treated as FDI subject to the condition that the FDI stake is raised to 10% or beyond within one year from the date of the first purchase.
- If the stake is not raised to 10% or above, then the investment can be treated as portfolio investment.
- Foreign Portfolio Investors include Foreign Institutional Investors (FIIs) and Qualified Foreign Investors (QFIs).
- Foreign investment in an unlisted company, irrespective of the threshold limit, may be treated as FDI

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FISCAL POLICY

- Fiscal policy is the means by which a government adjusts its spending levels and tax rates to monitor and influence a nation's economy.
- It is a complimentary strategy to monetary policy (through which a central bank influences a nation's money supply).
- These two policies are used in various combinations to direct a country's economic goals.
- Fiscal policy deals with the taxation borrowing and expenditure decisions of the government.
- Fiscal policy is an important constituent of the overall economic framework of a country and is therefore intimately linked with its general economic policy strategy.

Objectives of Fiscal Policy

- In a system of indicative planning, reliance on fiscal policy as an instrument of development is considerable.
- The Planning Commission had stated in the Seventh Five Year Plan that "Though with it the government creates and sustains the public economy consisting of the provision of public services and public investment; at the same time it is an instrument for reallocation of resources according to national priorities, redistribution, promotion of private savings and investments, and the maintenance of stability".
- Thus, fiscal policy primarily aims at economic growth with price stability. Among other goals of fiscal policies are: capital formation, resource allocation and redistribution for mitigating inequality. It is notable that fiscal policy in a developed country is preoccupied with the problems of business cycle-boom and depression.
- But in a developing economy, tackling business cycle becomes secondary because the prime objective of such economies is capital formation through increased savings and investments in order to achieve high level of economic growth. Further, given scarcity of capital and other resources in a developing economy, it is imperative to allocate resources to various sectors of the economy and heads of development judiciously and in line with development priorities. Fiscal policy helps to achieve these goals.

Types of Fiscal Policy

Expansionary fiscal policy

- It is defined as an increase in government expenditures and/or a decrease in taxes that causes the government's budget deficit to increase or its budget surplus to decrease. A government can adopt Expansionary fiscal policy on the following basis:
  - Government needs to borrow from domestic or foreign sources.
  - Print an equivalent amount of money.
  - Draws upon its foreign exchange reserves

Drawbacks of this policy

- The flipside of printing is it leads to inflation.
- If the government borrows too much from abroad it leads to a debt crisis.
- If it draws down on its foreign exchange reserves, a balance of payments crisis may arise.

Contractionary fiscal policy

- It is defined as a decrease in government expenditures and/or an increase in taxes that causes the government's budget deficit to decrease or its budget surplus to increase.

Neutral Fiscal Policy

- It is usually undertaken when an economy is in equilibrium. Government spending is fully funded by tax revenue and overall the budget outcome has a neutral effect on the level of economic activity.

Instruments of Fiscal Policy

- Fiscal policy is carried out by the legislative and/or the executive branches of government. The two main instruments of fiscal policy are:
  - **Government expenditure**
  - **Taxes**
- The effect of government expenditures, taxation, and debt on the aggregate economy is of immense importance. The government collects taxes in order to finance expenditures on a number of public goods and services.

Government Expenditure

- **Public Expenditure**
  - It is also known as Government expenditure which can be classified under the following heads:

Capital Expenditure

- These are those government expenditures which result in the creation of physical or financial assets or reduction in financial liabilities. These include:
  - expenditure on the acquisition of land, building, machinery, equipment, investment in shares, and
  - Loans and advances by the central government to State and Union Territory governments, PSUs and other parties.

Revenue Expenditure

- These are that expenditure incurred for purposes of day to day expenses rather than the creation of physical or financial assets of the central government. It relates to:
  - Expenses incurred for the normal functioning of the government departments and various services;
  - Interest payments on debt incurred by the government; and
  - Grants given to state governments and other parties.
- Both Capital and Revenue expenditure are also categorized as plan **and non-plan** in the budget documents.
- **Plan expenditure**-relates to Expenditure on Central Plans (the Five-Year Plans) and Central Assistance for State and Union Territory plans.
- **Non-plan expenditure**-covers a vast range of general, economic and social services of the government. The main items of non-plan expenditure are:

- Interest payments
- Defence services
- Subsidies
- Salaries
- Pensions

- Interest payments on market loans, external loans and from various reserve funds constitute the single largest component of non-plan revenue expenditure. Defence expenditure, is committed expenditure in the sense that given the national security concerns, there exists little scope for drastic reduction. Subsidies are an important policy instrument which aim at increasing welfare.

Government Revenue

Government revenue is classified into:

Revenue Receipts

- These are those receipts of the government which are non-redeemable, that is, they cannot be reclaimed from the government.
- They are further divided into **tax and non-tax revenues**

Tax Revenue

- Tax Revenues consist of the proceeds of taxes and other duties levied by the central government. Tax revenues are an important component of revenue receipts and comprise of following taxes:
  - **Income tax:** Taxes on individual salaries and income.
  - **Corporate tax:** Taxes on firms and corporations.
  - **Excise duties:** Duties levied on goods produced within the country.
  - **Customs duties:** Duties imposed on goods imported into and exported out of India.
  - **Service tax:** Tax levied by the government on service providers on certain service transactions.
  - **Wealth tax:** Charged on the net wealth of the assesse. It is a tax on the benefits derived from ownership of property.
  - **Gift tax:** Tax on the transfer of property by one individual to another while receiving nothing, or less than full value, in return.
- The tax applies whether the donor intends the transfer to be a gift or not. Taxes like wealth tax, gift tax and estate duty (now abolished) have never been of much significance in terms of revenue yield and have thus been referred to as paper taxes.
- The advantage of the tax is that it raises money for governments.
- Critics argue that the tax will result in fewer financial transactions being made, resulting in job losses in financial centres. Others warn that the tax will mean pension funds and savers get less returns, as banks will simply pass the cost of the tax onto their customers.

Non Tax Revenue

- Non-tax revenue mainly consists of:
  - Interest receipts on account of loans by the central government;
  - Dividends and profits on investments made by the government;
  - Fees and other receipts for services rendered by the government; and
  - Cash grants-in-aid from foreign countries and international organisations

Capital Receipts

- All those receipts of the government which create liability or reduce financial assets are termed as capital receipts.

- The main items of capital receipts are:
  - Loans raised by the government from the public which are called market borrowings,
  - Borrowings by the government from the Reserve Bank of India (RBI) and Commercial Banks and other Financial Institutions through the sale of treasury bills,
  - Loans received from foreign governments and international organisations,
  - Recoveries of loans granted by the central government,
  - Small savings (Post-Office Savings Accounts,
  - National Savings Certificates, etc),
  - Provident funds, and
  - Net receipts obtained from the sale of shares in Public Sector Undertakings

The functions that operate through the revenue expenditure measures of the government are: **Allocation Function - Expenditure on "Public Goods":**

- Certain goods, referred to as public goods (such as national defence, roads, government administration), as distinct from private goods (like clothes, cars, food items), cannot be provided through the market mechanism, i.e. by transactions between individual consumers and producers and must be provided by the government. This is the allocation function. Note: Public goods are financed through the budget.

Distribution Function:

- Government, through its tax and expenditure policy, attempts to bring about a distribution of income that is considered 'fair' by society.
- The government affects the personal disposable income of households by making transfer payments and collecting taxes and, therefore, can alter the income distribution. This is the distribution function.

Stabilization function:

- The economy tends to be subject to substantial fluctuations and may suffer from prolonged periods of unemployment or inflation. There may be times when extra government expenditure is needed to raise aggregate demand.
- There may be times when expenditures exceed the available output under conditions of high employment and thus may cause inflation.
- In such situations, restrictive conditions are needed to reduce demand. These constitute the stabilization requirements of the domestic economy.

Government Budgeting

Budget

- Budget is an Annual Financial Statement of yearly estimated receipts and expenditures of the government in respect of every financial year.
- It acts as instruments of control and act as a benchmark to evaluate the progress of various departments.
- Budgeting is the process of estimating the availability of resources and then allocating them to various activities according to a pre-determined priority.

Types of Budgeting

Performance Budgeting

- A Performance Budget gives an indication of how the funds spent are expected to give outputs and ultimately the outcomes.

- A performance budget reflects the goal/objectives of the organization and spells out its performance targets.
- These targets are sought to be achieved through a strategy. Unit costs are associated with the strategy and allocations are accordingly made for achievement of the objectives.
- However, performance budgeting has a limitation – it is not easy to arrive at standard unit costs especially in social programmes, which require a multi-pronged approach.

Zero-Based Budgeting (ZBB)

- The concept of ZBB was introduced in the 1970s. As the name suggests, in the process every budgeting cycle starts from scratch.
- Unlike the earlier systems, where only incremental changes were made in the allocation, under zero-based budgeting every activity is evaluated each time a budget is made and only if it is established that the activity is necessary, funds are allocated to it.
- Under the ZBB, a close and critical examination is made of the existing government programmes, projects and other activities to ensure that funds are made available to high priority items by eliminating outdated programmes and reducing funds to the low priority items.
- The basic purpose of ZBB is phasing out of programmes/activities, which do not have relevance anymore. ZBB is done to overhaul the functioning of the government departments and PSUs so that productivity can be increased and wastage can be minimized. Scarce government resources can be deployed efficiently. Therefore, ZBB is followed for **rationalization of expenditure.**
- Governmental programmes and projects are appraised every year as if they are new and funding for the existing items is not continued merely because a part of the project cost has already been incurred.

Programme Budgeting

- It aimed at a system in which expenditure would be planned and controlled by the objective. The basic building block of this system is the classification of expenditure into programmes, which meant objective oriented classification so that programmes with common objectives are considered together.

Programme and Performance Budgeting System (PPBS)

- PPBS went much beyond the core elements of programme budgeting and was much more than the budgeting system. It aimed at an integrated expenditure management system, in which systematic policy and expenditure planning would be developed and closely integrated with the budget. Thus, it was too ambitious in scope.
- Many governments today use the "programme budgeting" label for their performance budgeting system. As pointed out by Marc Robertson, the contemporary influence of the basic programme budgeting idea is much wider than the continuing use of the label. It is defined in terms of its core elements as mentioned above. Programme budgeting is an element of many contemporary budgeting systems which aim at linking funding and results. Neither was adequate preparation time given nor was a stage-by-stage approach adopted. Therefore, the Introduction of PPBS in the federal government in USA was not successful, although the concept of performance budgeting and programme budgeting endured.

Outcome Budget

- Outcome Budget was first introduced in India in 2005-06 by stating "the people of the country are concerned with outcomes, not just outlays".
- In 2007-08 onwards the previous Performance Budget was merged with Outcome Budget.
- It is practiced by most of the ministeries while preparing their budget details and submitting it to the **Ministry of Finance** for the preparation of annual budget towards the end of February.

- It is a performance measurement tool that helps in better service delivery; decision-making; evaluating programme performance and results; communicating programme goals; and improving programme effectiveness.
- It measures the development outcomes of all government programmes.
- It, however, will not necessarily include information of targets already achieved.
- This method of monitoring flow of funds, implementation of schemes and the actual results of the usage of the money is followed by many countries.

Gender Budgeting

- Gender Buget was also introduced along with Outcome Budget in India in 2005-06.
- Gender budgeting is an exercise to translate the stated gender commitments of the government into budgetary commitments, involving special initiatives for empowering women and examination of the utilization of resources allocated for women and the impact of public expenditure and policies of the government on women.
- The 2019-20 Budget aims to design a roadmap for woman empowerment and their increased participation in the Indian economy through gender budgeting.

Balanced Budgeting

- It is that budget in which Government receipts are equal to Government expenditure.

Merits of the Balanced Budget

- The Government does not indulge in wasteful expenditure.
- Interference in economic functioning of the system is totally avoided by the government generally.
- Financial stability is ensured with balanced budget.
- However, balanced budget is not an achievement of the government when economy is in a state of depression for at that time, government is expected to increase its expenditure with a view to increasing aggregate demand.

Demerits of a Balanced Budget

- It does not offer any solution to the problem of unemployment during depression.
- It is not helpful to the growth and development programmes of the less developed countries.

Unbalanced Budgeting

- It is that budget in which receipts and expenditure of the government are not equal.
- It includes two cases: Surplus Budget and Deficit Budget arise.
- In **Surplus Budget**, Government receipts are greater than Government expenditures. While in the case of **Deficit Budget,** Government expenditures are greater than Government receipts.

Merits of a Deficit Budget

- It helps in addressing the problem of unemployment during depressions.
- It is conducive for growth and development in less developed countries.
- It works towards social welfare of the people.

Demerits of Deficit Budget

- It shows wasteful expenditure by the government.
- It shows less revenue realization in comparison with the expenditure.
- It increases debt burden of the government
  - Measures used to record government deficit and their implications for the economy are as follows:

Revenue Deficit

- Revenue deficit refers to the excess of government's revenue expenditure over revenue receipts Revenue deficit = Revenue expenditure - Revenue receipts.
- The revenue deficit includes only such transactions that affect the current income and expenditure of the government. When the government incurs a revenue deficit, it implies that the government is dissaving and is using up the savings of the other sectors of the economy to finance a part of its consumption expenditure.
- This situation means that the government will have to borrow not only to finance its investment but also its consumption requirements. This will lead to a build-up of stock of debt and interest liabilities and force the government, eventually, to cut expenditure. Since a major part of revenue expenditure is committed expenditure, it cannot be reduced.
- Often the government reduces productive capital expenditure or welfare expenditure. This would mean lower growth and adverse welfare implications.
- **Effective revenue deficit**: Revenue deficit - those grants given to states which are used for creation of capital assets.

Fiscal Deficit

- Fiscal deficit is the difference between the government's total expenditure and its total receipts excluding borrowing.
- **Gross fiscal deficit** = Total expenditure - (Revenue receipts + Non-debt creating capital receipts)
- The fiscal deficit will have to be financed through borrowing. Thus, it indicates the total borrowing requirements of the government from all sources.
- From the financing side: Gross fiscal deficit = Net borrowing at home + Borrowing from RBI + Borrowing from abroad
- Net borrowing at home includes that directly borrowed from the public through debt instruments (for example, the various small savings schemes) and indirectly from commercial banks through Statutory Liquidity Ratio (SLR).
- The gross fiscal deficit is a key variable in judging the financial health of the public sector and the stability of the economy. From the way gross fiscal deficit is measured it can be seen that revenue deficit is a part of fiscal deficit.
- Fiscal Deficit = Revenue Deficit + Capital Expenditure - non-debt creating capital receipts
- A large share of revenue deficit in fiscal deficit indicated that a large part of borrowing is being used to meet its consumption expenditure needs rather than investment.

Primary Deficit

- Borrowing requirements of the government includes interest obligations on accumulated debt. The goal of measuring primary deficit is to focus on present fiscal imbalances.
- Primary deficit is used to obtain an estimate of borrowing on account of current expenditures exceeding revenues. It is simply the fiscal deficit minus the interest payments.
- Gross primary deficit = Gross fiscal deficit - Net interest liabilities
- Net interest liabilities consist of interest payments minus interest receipts by the government on net domestic lending.

Public Debt

- Budgetary deficits must be financed by either taxation or borrowing or printing money. Governments have mostly relied on borrowing, giving rise to what is called government debt. The concepts of deficits and debt are closely related. Deficits can be thought of as a flow which adds to the stock of debt. If the government continues to borrow year after year, it leads to the accumulation of debt and the government has to pay more and more by way of interest. These interest payments themselves contribute to the debt.

- By borrowing, the government transfers the burden of reduced consumption on future generations. This is because it borrows by issuing bonds to the people living at present but may decide to pay off the bonds some twenty years later by raising taxes. These may be levied on the young populations that have just entered the work force, whose disposable income will go down and hence consumption. Thus, national savings, it was argued, would fall. Also, government borrowing from the people reduces the savings available to the private sector. To the extent that this reduces capital formation and growth, debt acts as a 'burden' on future generations.

Fiscal Responsibility and Budget Management (FRBM) Act

- Enacted in 2003, the FRBM Act requires the elimination of revenue deficit by 2008-09. This means that from 2008-09, the government will have to meet all its revenue expenditure from its revenue receipts. Any borrowing would then only be to meet capital expenditure - repayment of loans, lending and fresh investment.
- The Act also mandates a 3% limit on the fiscal deficit after 2008-09. This is a reasonable limit that allows significant-cant leverage to the government to build capacities in the economy without compromising fiscal stability.
- It is important to note that since the entire Budget is at current market prices the deficits are also calculated with reference to GDP at current market prices. The main features of the bill are as follows:
    - The Fiscal Responsibility and Budget Management (FRBM) Bill was introduced in December 2000 and enacted in August 2003. The rules are effective from July 5, 2004 and the government is now committed to implement the FRBM act. Following are the main features of the FRBM Act:
    - The Act stipulates the elimination of revenue deficit by March 31, 2008.
    - According to the Act, the revenue deficit is to be reduced by a minimum of 0.5% of GDP per annum and the fiscal deficit by 0.3%. The rolling targets of FRBM provide for a reduction in the revenue deficit to 1.5% in 2005-06 and to 1.1% in 2006-07 and eventually to zero in 2008.
    - The FRBM Act also caps the level of guarantees and prohibits government to borrow from the RBI after April 1, 2006.
    - The Act requires that on a quarterly basis, the Government would have to place before both the Houses of Parliament an assessment of trends of receipts and expenditure. The Government also has to annually present the macro-economic framework statement, medium term fiscal policy statement and fiscal policy strategy statement. The three statements would provide the macroeconomic background and assessment relating to the achievement of FRBM goals.
    - The medium term fiscal policy statement will contain a three-year rolling target for key fiscal parameters that underpin the Government's fiscal correction trajectory.
    - Through the FRBM discipline, the Government is also committed to undertake an intra-year assessment of the achievement of its budgetary targets. During the Economy Crisis of 2008, the FBRM guidelines were not followed rigorously but now government is committed for reducing the deficits.

Deficit Financing

- Excessive domestic borrowing by the government may lead to higher real interest rates and the domestic private sector being unable to access funds resulting in the crowding out of private investment. Sometimes a combination of these can occur.
- In any case, the impact of a large deficit on long run growth and economic well-being is negative. Therefore, it is not prudent for a government to run an unduly large deficit.
- However, in case of developing countries, where the need for infrastructure and social investments may be substantial, running surpluses at the cost of long-term growth might also not be wise.
- The challenge then for most developing country governments is to meet infrastructure and social needs while managing the government's finances in a way that the deficit or the accumulating debt burden is not too great.
- Deficit Financing is a practice in which a government spends more money than it receives as revenue, the difference being made up by borrowing or minting new funds.

- Although budget deficits may occur for numerous reasons, the term usually refers to a conscious attempt to stimulate the economy by lowering tax rates or increasing government expenditures.

What is Fiscal Stimulus?

- Fiscal or Economic Stimulus are attempts by government to financially stimulate an economy.
- An economic stimulus is the use of monetary or fiscal policy changes to kick start a lagging or struggling economy.
- Example: Governments can adopt practices such as lowering interest rates, increasing government spending and quantitative easing, to name a few, to accomplish this.

Effects of Fiscal Policy on Macro Economy

- Fiscal policy affects aggregate demand, the distribution of wealth, and the economy's capacity to produce goods and services. In the short run, changes in spending or taxation can alter both the magnitude and the pattern of demand for goods and services. With time, this aggregate demand affects the allocation of resources and the productive capacity of an economy through its influence on the returns to factors of production, the development of human capital, the allocation of capital spending, and investment in technological innovations.
- Tax rates, through their effects on the net returns to labour, saving, and investment, also influence both the magnitude and the allocation of productive capacity. Fiscal policy also feeds into economic trends and influences monetary policy.

Effects of Fiscal Policy on Consumer Spending

- Lower taxes, everything else being constant, increase households' disposable income, allowing consumers to increase their spending. The consequences of the cut - how much is spent or saved, and the response of economic activity - depend on the way households make their decisions and on prevailing macroeconomic conditions.
- Whether the tax cut is perceived to be temporary or permanent will influence how much consumers save. A temporary cut will alter households' disposable income relatively little, and so might have little effect on consumption. If the cut is, instead, perceived to be permanent, then households will perceive a larger increase in their disposable income and so will likely increase their desired consumption by much more than they would if they thought the cut were temporary.
- There is a potential conflict between the use of fiscal policy to stimulate aggregate demand when the economy is operating below potential in the short run and the use of policy to promote longer-run goals for national saving and capital formation to improve future living standards. When there are underutilized economic resources, fiscal stimulus can increase investment. But when the economy is operating near potential, an increase in the public debt might eventually depress private investment, unless the fiscal stimulus is reversed as the economy approaches full employment and utilisation.
- This fiscal drag has the effect of reducing Aggregate Demand and becomes an example of deflationary fiscal policy. It could also be viewed as an automatic fiscal stabiliser because higher earnings growth will lead to higher tax and therefore moderate inflationary pressure in the economy.

Limitations of Fiscal Policy

- There are significant time lags
  - **Recognition lag:** time it takes government to recognize there is a problem
  - **Decision lag:** time required for government to determine most appropriate policy **Implementation lag**: time it takes to figure out how to implement new directives
  - **Impact lag:** time it takes to be felt through multiplier effect
- There are difficulties in changing spending and taxation policies
  - It is far easier to increase spending and decrease taxes then to increase taxes and decrease spending

- There is a conflict between levels of government over appropriate policies
  - Federal, provincial and city governments may differ on what needs to be done.
  - Regional variations
- There is crowding out of private investment
  - Increases interest rates
  - Reduces amount of funding for private investment
- Deficits impose burden on future generations and Foreign-owned debt removes capital from economy

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BUDGET HIGHLIGHTS (2020): SECTOR-WISE ANALYSIS

Growth Forecasts and fiscal projections to be achieved by Budget 2020

- Fiscal deficit of 3.5% of GDP has been set for current financial year.
- Nominal GDP growth rate has been targeted at 12%of GDP.
- Overall GDP growth rate has been forecasted for 2020-21 growth at 6%-6.5% by Economic survey.
- To sustain fast GDP growth rate and achieve 5 trillion economy target, India needs to invest 1.4 trillion dollars in infrastructure.

- This budget is woven around three prominent themes:
  - **Aspirational India** in which all sections of the society seek better standards of living, with access to health, education and better jobs.
  - **Economic development for all**, indicated in the Prime Minister's exhortation of "Sabka Saath , Sabka Vikas , Sabka Vishwas". This would entail reforms across swathes of the economy. Simultaneously, it would mean yielding more space for the private sector. Together, they would ensure higher productivity and greater efficiency.
  - **Caring Society**: Ours shall be a Caring Society that is both humane and compassionate. Antyodaya is an article of faith.

Aspirational India:

Agriculture, Irrigation and Rural Development: Sixteen Point Agenda for doubling the farmer's income by 2022

- **Adoption of Model Laws such as:** These laws have already been enforced to be adopted by state government:
  - Model Agricultural Land Leasing Act, 2016
  - Model Agricultural Produce and Livestock Marketing (Promotion and Facilitation) Act, 2017;, and
  - Model Agricultural Produce and Livestock Contract Farming and Services (Promotion and Facilitation) Act, 2018.
- **Water Security:** It aims to address the water stress issue in **hundred water stressed districts.**
- **Solar Pumps under KUSUM Scheme:** It aims to **20 lakh farmers for setting up stand-alone solar pumps** and further to help another **15 lakh farmers solarise their grid-connected pump sets** under KUSUM Scheme.
- **Sustainable use of fertilizers:** The budget has sought to use **all kinds of fertilizers including the traditional organic and other innovative fertilizers in a sustainable manner with a 'balanced approach'.**
- **Development of forward-linkages:**
  - Proposal of **geo-tagging of all warehouses** which are present in the country.

- Proposal of **setting up of warehouses** in accordance with norms set by Warehouse Development and Regulatory Authority (WDRA) at block/taluk level with **Viability Gap Funding by the central government**.

- **Village Storage scheme** to be run by Self help Groups (SHGs) in order to store the agricultural produce and provide farmers a good holding capacity and reduce their logistics cost.
- **National Cold Supply Chain** and **"Kisan Rail"** to be setup to provide better **storage and transportation facilities for perishable agricultural goods.**
  - Proposal of refrigerated coaches in **Express and Freight trains to transport perishable agricultural products.**
- **Krishi Udaan Scheme:** This will be launched by **Ministry of Civil Aviation** on international and national routes to **transport agricultural products specially fish, meat and dairy produ**cts across globe.
- **"One product one district"** Scheme in horticulture sector to be supported by central government by providing incentives to **those states which supports cluster-wise production of horticulture products.**
- **Promotion of 'Integrated Farming System'** in rainfed areas to counter the vagaries of monsoon or unseasonal rain.
  - This will include Multi-tier cropping, **bee-keeping, solar pumps, solar energy production in non-cropping season. Zero-Budget Natural Farming** will be promoted in this area to reduce the on-farm expenditure by farmers.
- Budget proposes to **strengthen Negotiable Warehousing Receipts (e-NWR)** which will be integrated with e-NAM.
- **Agricultural Credit:**
  - The budget proposes to strengthen agricultural credit by expanding refinance by NABARD and has set target of Rs. 15 lakh crore for agricultural credit.
  - It has further intended to cover all eligible beneficiaries of PM-KISAN under the KCC scheme.
- **Livestock and Animal Husbandary:** Budget proposes **to eliminate Foot and Mouth disease and brucellosis in cattle and also peste des petits ruminants (PPR) in sheep and goat by 2025.**
  - It also proposes to **increase coverage of artificial insemination** from existing 30% to 70%, **development of fodder farms** to produce quality fodder and **doubling milk processing facility** by 2025.
- **Blue Economy:** It proposes to put in place a framework for development, management and conservation of marine fishery resources.
- It aims to **raise the production of fish** and promotion of **growing of algae, sea-weed and cage Culture.** It will further employ **'Sagar Mitras'** to involve youths in **marine processing industries** and form **500 Fish Farmer Producer Organisations.**
- It aims to further help SHGs under Deen Dayal Antyodaya Yojana for alleviation of poerty.

Wellness, Water and Sanitation

- It proposes to setup more **hospitals tier-2 and tier-3 cities under PPP model** and will provide assistance in form of viability gap funding.
- They will be setup in first phase with **priority in those 'Aspirational District', which do not have empanelled hospitals under 'Ayushman Bharat' scheme.**
- It reiterates to **eliminate TB from India by 2025 and** setting up of **Jan Ausadhi Kendras** offering 2000 medicines and 300 surgicals **to all districts by 2024.**

Education and Skills

- Budget proposes to announce **'The New Education Policy'** which proposes to start a programme whereby urban local bodies across the country would provide internship opportunities to fresh engineers for a period up to one year.

- **'National Police University'** and **'National Forensic Science University'** have been proposed. It has also proposed to provide **degree level full-fledged online education programme.**
- It is proposed to attach **a medical college to an existing district hospital in PPP modl** with availability of Viability Gap Funding from the government.

Economic Development

Industry, Commerce and Investment

- The budget proposed **Investment Clearance Cell** that will provide "end to end" facilitation and support, including pre-investment advisory, information related to land banks and facilitate clearances at Centre and State level.
- It also proposed to develop **five new smart cities** in collaboration with States in PPP mode and sites will be chosen on the basis of location (near economic corridors and industries to be developed) and other factors.
- **National Technical Textiles Mission** has been proposed to create export oriented industry of technical textile.
- **NIRVIK (Niryat Rin Vikas Yojana)** has been proposed by the budget to achieve higher export credit disbursement to small exporters. This includes higher insurance coverage, reduction in premium for small exporters and simplified procedure for claim settlements.

Infrastructure

- **National Infrastructure Pipeline** to be strengthened which has already been launched with 103 lakh crore investment having 6500 projects across sector.
- Budget proposed for a **National Logistics Policy** to strengthen logistic sector.
- The budget proposed to **replace conventional energy meters by prepaid smart meters** in the next 3 years.
- It proposed to expand **the national gas grid** from the present 16200 km to 27000 km.
- **"Arth Ganga" Plans** to energise economic activity along river banks will be realised. It also proposed to complete NW-2 (Dhubri to Sadiya) by 2022.
- It has proposed to build infrastructure to **harness solar power along the Railway track. It also proposed to run 150 more trains and on PPP model.**

New Economy: Assimilating new technologies and governance ideas

- Budget proposed a policy to enable private sector to build **Data Centre parks** throughout the country.
- **Fibre to the Home (FTTH) connections** through Bharatnet will link 100,000 gram panchayats this year.
- The budget Proposed **National Mission on Quantum Technologies and Applications to** be setup with a corpus of 8000 crore rupees.
- The budget proposed **'Fibre to the Home (FTTH) connections'** through Bharatnet to link 100,000 gram panchayats this year.
- It proposed to create **two new national level Science Schemes to create a comprehensive database of genetic landscape of India.**

Caring Society

Women & Child, Social Welfare

- Budget proposed to do away with **manual scavenging by introducing automated cleaning of sewer lines with new technologies.**

- It has also allocated a significant amount to **nutrition-related programmes**, programmes related to women and child development and welfare of' schedule caste and schedule caste.

Culture & Tourism

- The budget proposed to develop **five archaeological sites as iconic sites with onsite Museums. They are: Rakhigarhi (Haryana), Hastinapur (Uttar Pradesh) Shivsagar (Assam), Dholavira (Gujarat) and Adichanallur (Tamil Nadu).**
- **A museum on Numismatics and Trade** will be opened at Old Mint building Kolkata and **'Tribal Museum'** in Ranchi will be supported by the government.
- It also proposed to setup a **maritime museum at Lothal**, the Harrapan age maritime site near Ahmedabad, by Ministry of Shipping.

Environment & Climate Change

- Budget proposed to achieve targets set up by Paris Climate Deal by cutting emission and closing down those thermal plants whose emission is higher than pre-set limit.
- It also proposed to help state government to cut air pollution in cities.

Governance

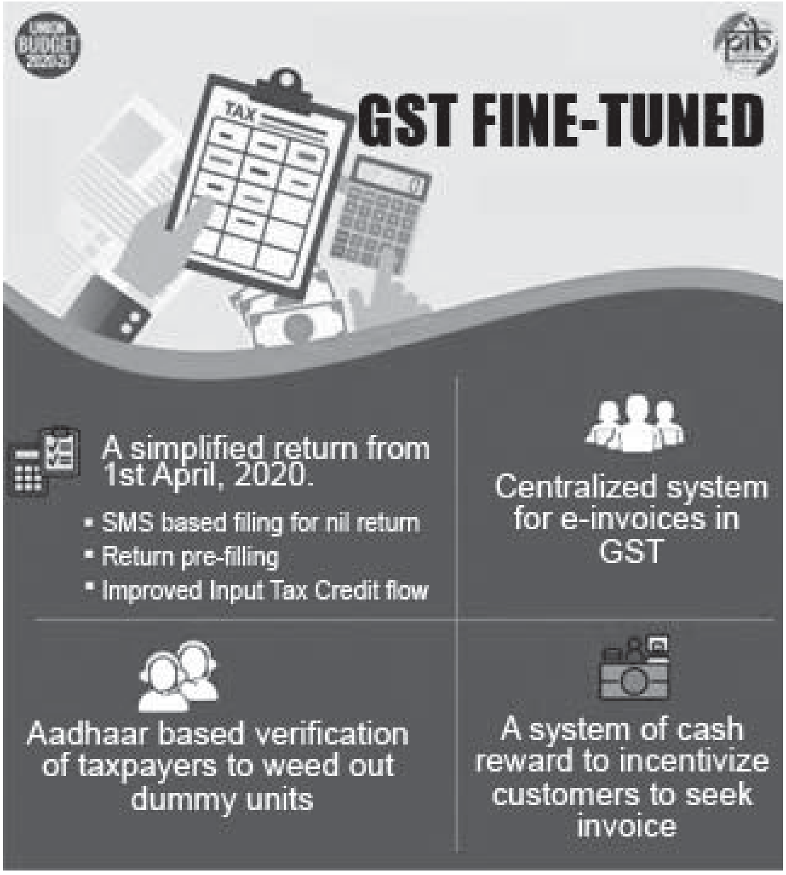
- India will host G-20 presidency in the year 2022 - the year of **75th anniversary of Independence of Indian Nation**. Budget has allocated a sum of Rs. 100 crore to begin the preparations for the event.
- It has also proposed a special package for newly created union territories of Jammu and Kashmir and Ladakh.

Financial Sector

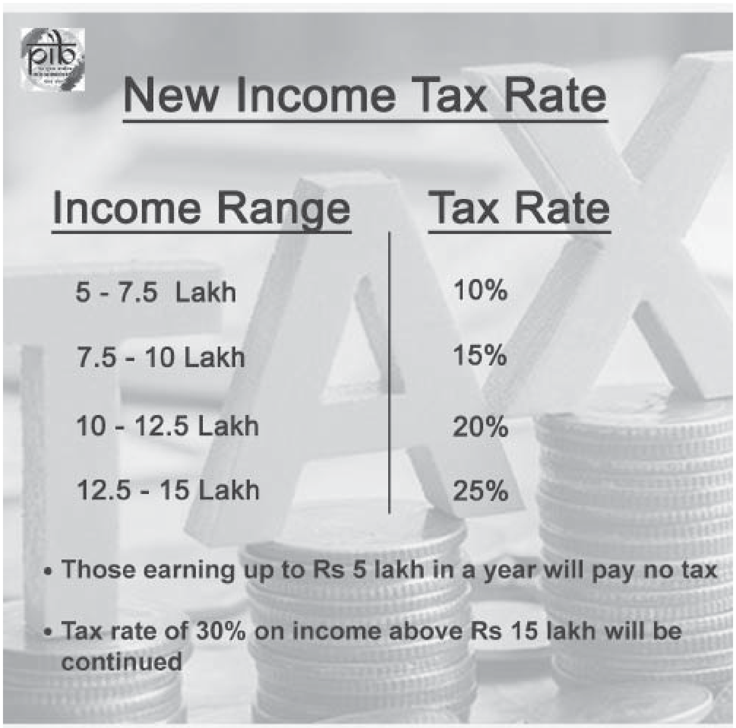
- It has proposed to increase Deposit Insurance Coverage for a depositor under **Deposit Insurance and Credit Guarantee Corporation (DICGC)** from **Rs. one lakh to Rs. five lakh per depositor.**
- It has proposed to strengthen **the Cooperative Banks by amendments to the Banking Regulation Act.**
- It has proposed to **sell the balance holding of Government of India IDBI Bank** to private, retail and institutional investors through the stock exchange.
- **Credit Guarantee Trust for Medium and Small Entrepreneurs (CGTMSE)** has been proposed by the budget **to provide subordinate debt for entrepreneurs of MSMEs.**

Taxation System

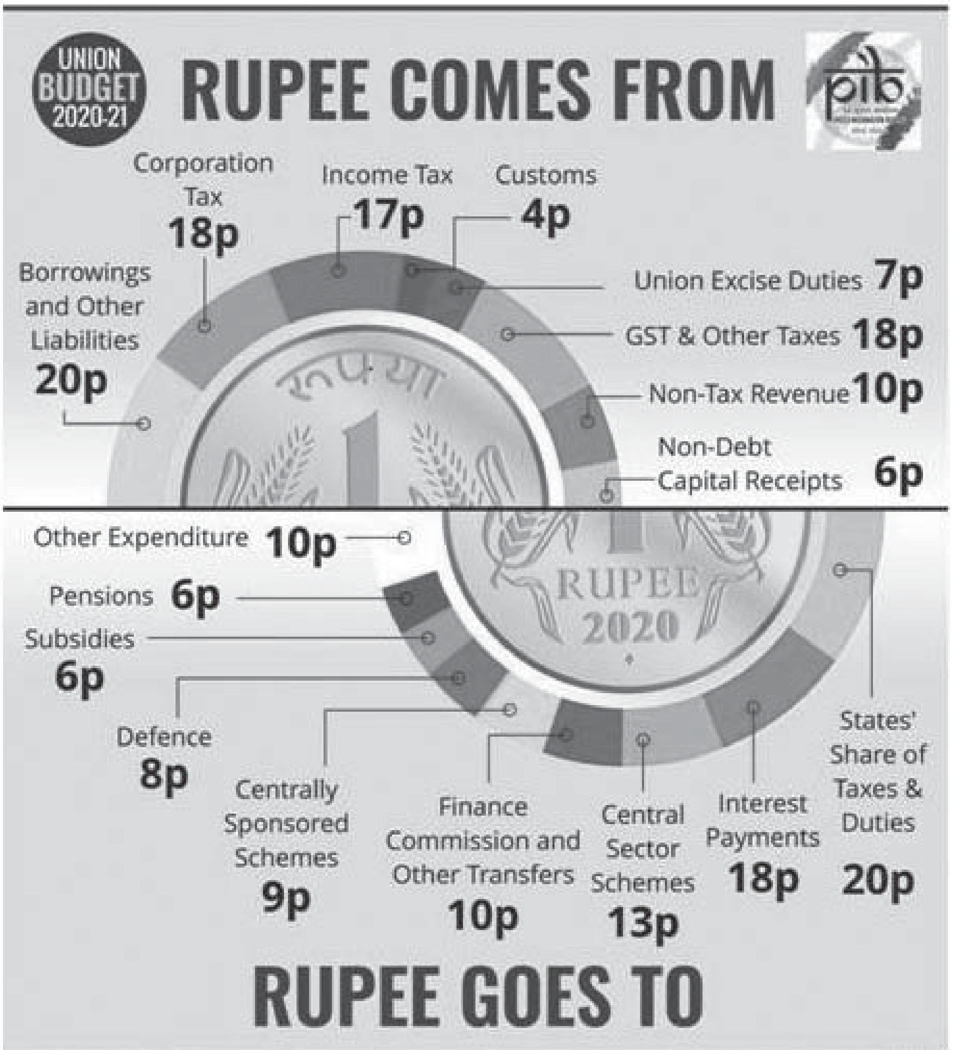
- **PAN to be allotted online on the basis of Aadhaar details** without any requirement of detailed application.
- There have a lot of modifications for simplification of paying GST.



- **Budget has proposed new taxation slabs for paying income tax**



- Budget has proposed **to abolish Dividend Distribution Tax (DDT)** and instead proposed and adopt the classical system of dividend taxation under which the companies would not be required to pay DDT.
- The dividend shall be taxed only in the hands of the recipients at their applicable rate.
- It has proposed **concessional corporate tax rate of 15% to new domestic companies engaged in the generation of electricity.**
- It has proposed **to grant 100% tax exemption to interest, dividend and capital gains income in respect of investment made in infrastructure and other notified sectors by the Sovereign Wealth Fund of foreign governments.**
- Budget has proposed **'Vivad Se Vishwas' scheme** under which will **cover disputes related to Direct Taxes.**
- Under this scheme, a taxpayer would be required **to pay only the amount of the disputed taxes** and will get complete waiver of interest and penalty provided he pays by 31st March, 2020.
- Option to be provided to **cooperative societies to be taxed at 22% plus 10% surcharge and 4% cess, with no exemptions or deductions.**



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ECONOMIC SURVEY

Economic Survey Vol. 1

Chapter-1 Wealth Creation: The Invisible Hand Supported by the Hand of Trust

- For more than three-fourths of known economic history, India has been the dominant economic power globally. Such dominance manifested by design. During much of India's economic dominance, the economy relied on the invisible hand of the market for wealth creation with the support of the hand of trust. Specifically, the invisible hand of markets, as reflected in openness in economic transactions, was combined with the hand of trust by appealing to ethical and philosophical dimensions. As far as half-a-century back, Spengler (1971) reflected this fact by asserting that Kautilya's Arthashastra postulates the role of prices in an economy.
- The Survey shows that contemporary evidence following the liberalization of the Indian economy support the economic model advocated in our traditional thinking. The exponential rise in India's GDP and GDP per capita post liberalisation coincides with wealth generation in the stock market. Similarly, the evidence across various sectors of the economy illustrates the enormous benefits that accrue from enabling the invisible hand of the market. Indeed, the Survey shows clearly that sectors that were liberalized grew significantly faster than those that remain closed. The events in the financial sector during 2011-13 and the consequences that followed from the same illustrate the second pillar - the need for the hand of trust to support the invisible hand. In fact, following the Global Financial Crisis, an emerging branch of the economics literature now recognises the need for the hand of trust to complement the invisible hand.
- The Survey posits that India's aspiration to become a $5 trillion economy depends critically on strengthening the invisible hand of markets together with the hand of trust that can support markets. The invisible hand needs to be strengthened by promoting pro-business policies to (i) provide equal opportunities for new entrants, enable fair competition and ease doing business, (ii) eliminate policies that undermine markets through government intervention even where it is not necessary, (iii) enable trade for job creation, and (iv) efficiently scale up the banking sector to be proportionate to the size of the Indian economy. Introducing the idea of "trust as a public good that gets enhanced with greater use", the Survey suggests that policies must empower transparency and effective enforcement using data and technology to enhance this public good.

Chapter-2 Entrepreneurship and Wealth Creation at the Grassroots

- **The "Startup India" campaign of the Government of India recognizes entrepreneurship as an increasingly important strategy to fuel productivity growth and wealth creation in India**. Given this initiative, this chapter examines the content and drivers of entrepreneurial activity at the bottom of the administrative pyramid – over 500 districts in India.
- The analysis employs comprehensive data on new firm creation in the formal sector across all these districts from the Ministry of Corporate Affairs (MCA)-21 databases.

- **First**, using the World Bank's Data on Entrepreneurship, this chapter confirms that India ranks third in number of new firms created. The same data shows that new firm creation has gone up dramatically in India since 2014. While the number of new firms in the formal sector grew at a compounded annual growth rate of 3.8 per cent from 2006-2014, the growth rate from 2014 to 2018 has been 12.2 per cent. As a result, from about 70,000 new firms created in 2014, the number has grown by about 80 per cent to about 1, 24,000 new firms in 2018.
- **Second**, reflecting India's new economic structure, i.e. comparative advantage in the Services sector, new firm creation in services is significantly higher than that in manufacturing, infrastructure or agriculture.
- **Third**, grassroots entrepreneurship is not just driven by necessity as a 10 percent increase in registration of new firms in a district yields a 1.8 percent increase in GDDP. Thus, entrepreneurship at the bottom of the administrative pyramid – a district – has a significant impact on wealth creation at the grassroot level. This impact of entrepreneurial activity on GDDP is maximal for the manufacturing and services sectors.
- **Fourth**, birth of new firms is very heterogeneous across Indian districts and across sectors. Moreover, it is dispersed across India and is not restricted to just a few cities.
- **Fifth**, literacy and education in the district foster local entrepreneurship significantly. For instance, the eastern part of India has the lowest literacy rate of about 59.6 per cent according to the census of 2011. This is also the region in which new firm formation is the lowest. In fact, the impact of literacy on entrepreneurship is most pronounced when it is above 70 per cent.
- **Sixth**, the level of local education and the quality of physical infrastructure in the district.

- Finally, **policies that enable ease of doing business and flexible labour regulation enable new firm creation, especially in the manufacturing sector**. As the manufacturing sector has the greatest potential to create jobs for our youth, enhancing ease of doing business and implementing flexible labour laws can create the maximum jobs in districts and thereby in the states.
- **Literacy, education and physical infrastructure are the other policy levers that district and state administrations must focus on foster entrepreneurship**.

Chapter- 3 Pro-Business versus Pro-Crony

- **India's aspiration to become a $5 trillion economy depends critically on promoting "probusiness" policy that unleashes the power of competitive markets to generate wealth**, on the one hand, and weaning away from "pro-crony" policy that may favour specific private interests, especially powerful incumbents, on the other hand. Economic events since 1991 provide powerful evidence supporting this crucial distinction.
- Viewed from the lens of the Stock market, which captures the pulse of any economy, creative destruction has increased significantly after reform. Before liberalization, a Sensex firm expected to stay in it for 60 years, which decreased to only 12 years after liberalization. Every five years, one-third of Sensex firms are churned out, reflecting the continuous influx of new firms, products and technologies into the economy.
- Despite impressive progress in enabling competitive markets, pro-crony policies have destroyed value in the economy. For example, an equity index of connected firms significantly outperformed the market by 7 per cent a year from 2007 to 2010, reflecting abnormal profits extracted at common citizens' expense. In contrast, the index underperforms the market by 7.5 per cent from 2011, reflecting the inefficiency and value destruction inherent in such firms.
- Pro-crony policies as reflected in discretionary allocation of natural resources till 2011 led to rent-seeking by beneficiaries while competitive allocation of the same resources post 2014 have put an end to such rent extraction. Similarly crony lending that led to willful default, wherein promoters have collectively siphoned off wealth from banks, led to losses that dwarf subsidies directed towards rural development.

Chapter-4 Undermining Markets: When Government Intervention Hurts More Than It Helps

- Government intervention, sometimes though well intended, often ends up undermining the ability of the markets to support wealth creation and leads to outcomes opposite to those intended. This chapter analyses four examples of anachronistic government interventions, though many more abound.
  - First, frequent and unpredictable imposition of blanket stock limits on commodities under **Essential Commodities Act (ECA)** neither brings down prices nor reduces price volatility. However, such intervention does enable opportunities for rent-seeking and harassment. For instance, imposition of stock limits on dal in 2006-Q3, sugar in 2009- Q1 and onions in September 2019 spiked up the volatility of the wholesale and retail prices instead of smoothening them – in contrast to its objective of easing pressure on prices. Around 76000 raids under ECA were conducted during 2019. Assuming a minimum of 5 persons involved in a raid, considerable administrative effort goes into enforcement of ECA. As the conviction rate, however, is abysmally low and raids have no impact on prices, the ECA only seems to enable rent-seeking and harassment. The Act is anachronistic as it was passed in 1955 in an India worried about famines and shortages; it is irrelevant in today's India and must be jettisoned.
  - Second, the regulation of prices of drugs through the DPCO 2013, has led to increase in the price of a regulated pharmaceutical drug vis-à-vis that of a similar drug whose price is not regulated. Our analysis shows that the increase in prices was witnessed for more expensive formulations than for cheaper ones and those sold in hospitals rather than retail shops, reinforcing that the outcome is opposite to what DPCO aims to do - making drugs affordable. The evidence across different commodities (pulses, sugar, onions and drugs) - not just onions or sugar where cartelisation is often suspected - and episodes spanning different time periods (2006-19) suggests that the ineffectiveness of ECA stems from unnecessary government intervention that undermines markets.
  - Third, government policies in the foodgrain markets has led to the emergence of Government as the largest procurer and hoarder of foodgrains – adversely affecting competition in these markets. This has led to overflowing of buffer stocks with FCI, burgeoning food subsidy burden, divergence between demand and supply of cereals and acted as a disincentive towards crop diversification.
  - Fourth, analysis of debt waivers given by States/Centre shows that full waiver beneficiaries consume less, save less, invest less and are less productive after the waiver when compared to the partial beneficiaries. The share of formal credit decreases for full beneficiaries when compared to partial beneficiaries, thereby defeating the very purpose of the debt waiver provided to farmers.
- The **Ministry of Consumer Affairs and its related arms must examine whether the anachronistic ECA, which was passed in 1955 in an India worried about famines and shortages, is relevant in today's India**. Around 76000 raids under ECA were conducted during 2019. Assuming a minimum of 5 persons involved in a raid, considerable administrative effort goes into enforcement of ECA. As the conviction rate, however, is abysmally low and raids have no impact on prices, the ECA only seems to enable rent-seeking and harassment. The Survey provides clear evidence that the case for jettisoning this anachronistic legislation is strong.
- The regulation of prices of drugs, through the DPCO 2013, has led to increase in the price of the regulated pharmaceutical drug vis-à-vis that of a similar drug whose price is not regulated. The increase in prices is greater for more expensive formulations than for cheaper ones and for those sold in hospitals rather than retail shops. These findings reinforce that the outcome is opposite to what DPCO aims to do - making drugs affordable.
- **As the Government is a huge buyer of drugs through its various arms such as CGHS, Defense, Railways etc., the Government can intervene more effectively to provide affordable drugs by combining all its purchases and thereby exercise its bargaining power**. The Ministry of Health and Family Welfare as well as its related arms must imbibe the evidence to evolve non-distortionary mechanisms that utilise Government's bargaining power in a transparent manner.

- Government policies in the foodgrain markets has led to the emergence of Government as the largest procurer and hoarder of rice and wheat crowding out. This has led to burgeoning food subsidy burden and inefficiencies in the markets, which is affecting the long run growth of agricultural sector. The foodgrains policy needs to be dynamic and allow switching from physical handling and distribution of foodgrains to cash transfers/ food coupons/smart cards.
- Analysis of debt waivers given by States/Centre shows that full waiver beneficiaries consume less, save less, invest less and are less productive after the waiver when compared to the partial beneficiaries. Debt waivers disrupt the credit culture and end up reducing the formal credit flow to the very same farmers, thereby defeating the very purpose of the debt waiver provided to farmers.
- This chapter makes the case that each department and ministry in the Government must systematically examine areas where the Government needlessly intervenes and undermines markets. Note that the chapter does not argue that there should be no Government intervention. Instead, interventions that were apt in a different economic setting may have lost their relevance in a transformed economy. Eliminating such instances will enable competitive markets and thereby spur investments and economic growth.

Chapter- 5 Creating Jobs and Growth by Specializing to Exports in Network Products

- The current environment for international trade presents India an unprecedented opportunity to chart a China-like, labor-intensive, export trajectory and thereby create unparalleled job opportunities for our burgeoning youth.
- By integrating "Assemble in India for the world" into Make in India, India can create 4 crore well-paid jobs by 2025 and 8 crore by 2030. Exports of network products, which is expected to equal $7 trillion worldwide in 2025, can contribute a quarter of the increase in value-added for the $5 trillion economy by 2025. This chapter, therefore, articulates a clear-headed strategy to grab this opportunity. China's remarkable export performance vis-à-vis India is driven primarily by deliberate specialization at large scale in labour-intensive activities, especially "network products", where production occurs across **Global Value Chains (GVCs) operated by multi-national corporations**. Laser-like focus must be placed on enabling assembling operations at mammoth scale in network products. As an India that harbours misplaced insecurity on the trade front is unlikely to grab this opportunity, our trade policy must be an enabler. In fact, contrary to recent fears, careful analysis that controls for all confounding factors shows that India has gained from trade agreements: a 0.7 per cent increase per year in trade surplus with partner countries for manufactured products and 2.3 per cent per year for total merchandise.
- **The current environment for international trade presents India an unprecedented opportunity to chart a China-like, labour-intensive, export trajectory and thereby create unparalleled job opportunities for our burgeoning youth**.
- **By integrating "Assemble in India for the world" into Make in India, India can raise its export market share to about 3.5 per cent by 2025 and 6 per cent by 2030**. This will create 4 crore well-paid jobs by 2025 and 8 crore by 2030.
- One-quarter of the increase in value added required for making India a $5 trillion economy by 2025 can come from exports of network products.
- This chapter, therefore, articulates a clear-headed strategy to grab this opportunity.
- China's remarkable export performance vis-à-vis India is driven primarily by deliberate specialization at large scale in labour-intensive sectors, especially "network products", where production occurs across Global Value Chains (GVCs) operated by multi-national corporations. China used this specialised strategy to export primarily to markets in rich countries. Similarly, India must place laser-like focus on enabling assembling operations at mammoth scale in network products.
- As an India that harbours misplaced insecurity on the trade front is unlikely to grab this opportunity, our trade policy must be an enabler. When the impact of India's trade agreements on overall trade balance is made by accounting for all confounding factors, India's exports have increased by 13.4 per cent for manufactured products and 10.9 per cent for total merchandise while imports increased by 12.7 per cent for manufactured products and 8.6 per cent for total merchandise. Thus, India has

clearly gained 0.7 per cent increase in trade surplus per year for manufactured products and 2.3 per cent per year for total merchandise.

Chapter- 6 Targeting Ease of Doing Business in India

- **Ease of doing business is key to entrepreneurship, innovation and wealth creation. India has risen significantly in the World Bank's Doing Business rankings in recent years, but there are categories where it lags behind – Starting a Business, Registering Property, Paying Taxes and Enforcing Contracts**.
- This chapter focuses on these parameters and compares India's performance with both its peers and with the best-in-class. For example, registering property in Delhi and Mumbai takes 49 and 68 days respectively, while it takes 9 days in China and 3.5 days in New Zealand.
- These performance matrices provide a measure of the scope for improvement. The chapter then explores the density of laws, rules and other statutory compliance requirements faced by a manufacturing or services business (specifically the restaurants segment).
- **Export competitiveness depends not only on the cost of production but also on the efficiency of logistics**.
- A series of case studies are used to analyse the time taken at each stage for specific merchandise items to travel from factory gate to the warehouse of the foreign customer. For instance, a study found that an apparels consignment going from Delhi to Maine (U.S.) takes roughly 41 days, but 19 of these are spent within India due to delays in transportation, customs clearance, ground handling and loading at sea-ports.
- A study of carpets exports from Uttar Pradesh to the United States also showed similar results. The process flow for imports, ironically, is more efficient than that for exports! In contrast, however, the imports and exports of electronics through Bengaluru airport was found to be world class. The processes of Indian airports should be adapted and replicated in sea-ports.
- India has jumped up 79 positions in World Bank's Doing Business rankings, improving from 142 in 2014 to 63 in 2019. However, it continues to trail in parameters such as Ease of Starting Business (rank 136), Registering Property (rank 154), Paying Taxes (rank 115), and Enforcing Contracts (rank 163).
- Enforcing a contract in India takes on average 1,445 days in India compared to just 216 days in New Zealand, and 496 days in China. Paying taxes takes up more than 250 hours in India compared to 140 hours in New Zealand, 138 in China and 191 in Indonesia. These parameters provide a measure of the scope for improvement.
- Setting up and operating a services or manufacturing business in India faces a maze of laws, rules and regulations. Many of these are local requirements, such as burdensome documentation for police clearance to open a restaurant. This must be cleaned up and rationalized one segment at a time.
- Case studies of merchandise exports found that logistics is inordinately inefficient in Indian sea-ports. The process flow for imports, ironically, is more efficient than that for exports. Although one needs to be careful to directly generalize from specific case studies, it is clear that customs clearance, ground handling and loading in sea ports take days for what can be done in hours. A case study of electronics exports and imports through Bengaluru airport illustrates how Indian logistical processes can be world class.
- It must be noted that the turnaround time of ships in India has been on a continuous decline, almost halving from 4.67 days in 2010-11 to 2.48 days in 2018-19. This shows that achieving significant efficiency gains in the case of sea ports is possible. Although, a full case study of Chennai port was not done, partial data suggests that its processes are smoother than those of the ports discussed above.
- The streamlining of the logistics process at sea-ports requires close coordination between the Logistics division of the Ministry of Commerce and Industry, the Central Board of Indirect Taxes and Customs, Ministry of Shipping and the different port authorities. The simplification of the Ease of Doing Business landscape of individual sectors such as tourism or manufacturing, however, requires a more targeted approach that maps out the regulatory and process bottlenecks for each

segment. Once the process map has been done, the correction can be done at the appropriate level of government - central, state or municipal.

Chapter-7 Golden Jubilee of Bank Nationalization: Taking Stock

- **In 2019, India completed the 50th anniversary of bank nationalization**. It is, therefore, apt to celebrate the accomplishments of the 3, 89,956 officers, 2, 95,380 clerks, and 1, 21,647 sub-staff who work in Public Sector Banks (PSBs). At the same time, an objective assessment of PSBs is apposite.
- **Since 1969, India has grown significantly to become the 5th largest economy in the world**. Yet, India's banking sector is disproportionately under-developed given the size of its economy. For instance, India has only one bank in the global top 100 – same as countries that are a fraction of its size: Finland (about 1/11th), Denmark (1/8th), Norway (1/7th), Austria (about 1/7th), and Belgium (about 1/6th). Countries like Sweden (1/6th) and Singapore (1/8th) have thrice the number of global banks.
- A large economy needs an efficient banking sector to support its growth. Historically, in the last 50 years, the top-five economies have always been ably supported by their banks. Should India's banks play a role proportionate to its economic size, India should have six banks in the top 100. As PSBs account for 70 per cent of the market share in Indian banking, the onus of supporting the Indian economy and fostering its economic development falls on them. Yet, on every performance parameter, PSBs are inefficient compared to their peer groups. Previously, the **Narasimhan Committee (1991, 1997), Rajan Committee (2007) and P J Nayak Committee (2014) have provided several suggestions to enhance the efficiency of PSBs**. The survey suggests **use of FinTech (Financial Technology) across all banking functions and employee stock ownership across all levels to enhance efficiencies in PSBs**. These will make PSBs more efficient so that they are able to adeptly support the nation in its march towards being a $5 trillion economy. All these recommendations need to be seriously considered and a definite, timebound plan of action drawn up. With the cleaning up of the banking system and the necessary legal framework such as the Insolvency and Bankruptcy Code (IBC), the banking system must focus on scaling up efficiently to support the economy.
- In 2019, every rupee of taxpayer money invested in PSBs, on average, lost 23 paise. In contrast, every rupee of investor money invested NPBs on average gained 9.6 paise. Also, credit growth in PSBs has been much lower than NPBs for the last several years.
- To incentivize employees and align their interests with that of all shareholders of banks, bank employees should be given stakes through an employee stock ownership plan (ESOP) together with proportionate representation on boards proportionate to the blocks held by employees.
- **A GSTN type of entity should be setup to enable the use of big data, artificial intelligence and machine learning in credit decisions, especially those pertaining to large borrowers**. As Government is the owner of all the PSBs, Government has the right to use the data that PSBs generate during their business. Therefore, the Government as the promoter must set up this entity that will aggregate data from all PSBs to enable decision making using big data techniques.
- The patterns in default that such powerful techniques can unearth are far beyond the capacity of any unscrupulous promoter to escape. Therefore, such investments are critical to ensuring better screening and monitoring of borrowers, especially the large ones.

Chapter- 8 Financial Fragility in the NBFC Sector

- Following payment defaults by subsidiaries of Infrastructure Leasing and Financing Services and by Dewan Housing Finance Limited, investors in Liquid Debt Mutual Funds (LDMFs) ran collectively to redeem their investments. In fact, the defaults triggered panic across the entire gamut of NBFC-financiers, thereby causing a funding (liquidity) crisis in the NBFC sector.
- This chapter highlights that problems faced by the NBFCs stemmed from their over-dependence on short term wholesale funding from the Liquid Debt Mutual Funds. While such reliance works well in good times, it generates significant risk to NBFCs from the inability to roll over the short-term funding during times of stress.

- An asset-side shock not only exacerbates the Asset Liability Management (ALM) problem but also makes investors in LDMFs jittery and thereby leads to a redemption pressure that is akin to a "bank run." This run on LDMFs then precipitates the refinancing (rollover) risk for NBFCs and further exacerbates the initial problems caused on the asset side. A dynamic health index (Health Score) is constructed that captures these risks and can be used as an early warning system to anticipate liquidity crisis in an NBFC. Policy makers can use this tool to monitor, regulate and avert financial fragility in the NBFC sector.
- Motivated by the current liquidity crunch the NBFC sector, this chapter investigates the key drivers of Rollover Risk of the shadow banking system in India.
- The key drivers of Rollover Risk are: ALM Risk, Interconnectedness Risk and Financial and Operating Resilience of an NBFC.
- The over-dependence on short-term wholesale funding exacerbates Rollover Risk.
- **Using a novel scoring methodology, Rollover Risk is quantified for a sample of HFCs and Retail-NBFCs (which are representative of their respective sectors) and thereby compute a diagnostic (Health Score)**.
- The Health Score for the HFC sector exhibited a declining trend post 2014. By the end of FY2019, the health of the overall sector had worsened considerably.
- The Health Score of the Retail-NBFC sector was consistently below par for the period 2014 till 2019.
- Larger Retail-NBFCs had higher Health Scores but among medium and small Retail NBFCs, the medium size ones had a lower Health Score for the entire period from March 2014 till March 2019.
- The above findings suggest that the Health Score provides an early warning signal of impending liquidity problems.
- The analysis find significant evidence that equity markets react favourably to increase in Health Score of individual HFCs and Retail-NBFCs, thereby confirming the validity of Health Score as an early warning signal.

Chapter-9 Privatization and Wealth Creation

- The recent approval of strategic disinvestment in Bharat Petroleum Corporation Limited (BPCL) led to an increase in value of shareholders' equity of BPCL by Rs. 33,000 crore when compared to its peer Hindustan Petroleum Corporation Limited (HPCL)! This reflects an increase in the overall value from anticipated gains from consequent improvements in the efficiency of BPCL when compared to HPCL which will continue to be under Government control.
- This chapter, therefore, examines the realized efficiency gains from privatization in the Indian context. It analyses the before-after performance of 11 CPSEs that had undergone strategic disinvestment from 1999-2000 to 2003-04. To enable a careful comparison using a difference in-difference methodology, these CPSEs are compared with their peers in the same industry group.
- The analysis shows that these privatized CPSEs, on an average, perform better post privatization than their peers in terms of their net worth, net profit, return on assets (ROA), return on equity (RoE), gross revenue, net profit margin, sales growth and gross profit per employee. More importantly, the ROA and net profit margin turned around from negative to positive surpassing that of the peer firms, which indicates that privatized CPSEs have been able to generate more wealth from the same resources.
- This improved performance holds true for each CPSE taken individually too. The analysis clearly affirms that privatization unlocks the potential of CPSEs to create wealth. The chapter, therefore, bolsters the case for aggressive disinvestment of CPSEs.

Chapter- 10 Is India's GDP Growth Overstated? No!

- As investors deciding to invest in an economy care for the country's GDP growth, uncertainty about its magnitude can affect investment. Therefore, the recent debate about India's GDP growth rates following the revision in India's GDP estimation methodology in 2011 assumes significance, especially given the recent slowdown in the growth rate.

- Using careful statistical and econometric analysis that does justice to the importance of this issue, this chapter finds no evidence of mis-estimation of India's GDP growth. The chapter starts from the basic premise that countries differ among each other in various observed and unobserved ways. Therefore, cross-country comparisons are fraught with risks of incorrect inference due to various confounding factors that stem from such inherent differences. As a result, cross-country analysis has to be carefully undertaken so that correlation is distinguished from causality.
- The models that incorrectly over-estimate GDP growth by 2.77 per cent for India post-2011 also mis-estimate GDP growth over the same time period for 51 other countries out of 95 countries in the sample. The magnitude of mis-estimation in the incorrectly specified model is anywhere between +4 per cent to -4.6 per cent, including UK by +1.6 per cent, Germany by +1.0 per cent, Singapore by -2.3 per cent, South Africa by -1.2 per cent and Belgium by -1.3 per cent. Given the lower growth rates for UK and Germany compared to India, the mis-estimation in percentage terms in the incorrectly specified model is much larger for UK (76 per cent) and Germany (71 per cent) than for India (40 per cent).
- However, when the models are estimated correctly by accounting for all unobserved differences among countries as well as the differential trends in GDP growth across countries, GDP growth for most of these 52 countries (including India) is neither over- or underestimated. In sum, concerns of over-estimation of India's GDP are unfounded. The larger point made by this chapter needs to be understood by synergistically viewing its findings with the micro-level evidence in Chapter 2, which examines new firm creation in the formal sector across 504 districts in India. Two observations are critical.
  - The granular evidence shows that a 10 per cent increase in new firm creation increases district-level GDP growth by 1.8 per cent.
  - As the pace of new firm creation in the formal sector accelerated significantly more after 2014, the resultant impact on district-level growth.
- **GDP growth is a critical variable for decision-making by investors as well as policymakers.** Therefore, the recent debate about whether India's GDP is correctly estimated following the revision in estimation methodology in 2011 is extremely significant.
- As countries differ in several observed and unobserved ways, cross-country comparisons have to be undertaken with care to separate out the effect of other confounding factors and isolate the effect of the methodology revision alone on GDP growth estimates.
- The models that incorrectly over-estimate GDP growth by 2.7 per cent for India post-2011 also mis-estimate GDP growth over the same time period for 51 other countries out of 95 countries in the sample. Several advanced economies such as UK, Germany and Singapore turn out to have their GDPs misestimated when the econometric model is incompletely specified.
- Correctly specified models that account for all unobserved differences among countries as well as differential trends in GDP growth across countries fail to find any misestimation of growth in India or other countries.
- Concerns of a misestimated Indian GDP are unsubstantiated by the data and are thus unfounded.

Chapter- 11 Thalinomics: The Economics of a Plate of Food in India

- Though economics affects the common lives of people in tangible ways, this fact often remains unnoticed. What better way to make economics relate to the common person than something that s (he) encounters every day – a plate of food? Enter **"Thalinomics: The economics of a plate of food in India"** – an attempt to quantify what a common person pays for a Thali across India.
- Has a Thali become more or less affordable? Has inflation in the price of a Thali increased or decreased? Is the inflation the same for a vegetarian Thali as for a non-vegetarian one? Is the inflation in the price of a Thali different across different states and regions in India? Which components account for the changes in the price of a Thali – the cereals, vegetables, pulses or the cost of fuel required for its preparation? Questions that can engage a dinner-table conversation in Lutyens Delhi or in a road-side Dhaba in the hinterland can now be answered and positions taken on either side of a "healthy" debate.

- Using the dietary guidelines for Indians (NIN, 2011), the price of Thalis are constructed. Price data from the Consumer Price Index for Industrial Workers for around 80 centres in 25 States/UTs from April 2006 to October 2019 is used.
- Both across India and the four regions – North, South, East and West – it is found that the absolute prices of a vegetarian Thali have decreased significantly since 2015-16 though the price has increased in 2019. As a result, an average household of five individuals that eats two vegetarian Thalis a day gained around Rs. 10887 on average per year while a non-vegetarian household gained Rs. 11787, on average, per year. Using the annual earnings of an average industrial worker, it is found that affordability of vegetarian Thalis improved 29 per cent from 2006-07 to 2019-20 while that for non-vegetarian Thalis improved by 18 per cent.
- 2015-16 can be considered as a year when there was a shift in the dynamics of Thali prices. Many reform measures were introduced since 2014-15 to enhance the productivity of the agricultural sector as well as efficiency and effectiveness of agricultural markets for better and more transparent price discovery.

Economic Survey Vol.2

Chapter-1 State of the Economy

- The year 2019 was a difficult year for the global economy with world **output growth estimated to grow at its slowest pace of 2.9 per cent since the global financial crisis of 2009**, declining from a subdued 3.6 per cent in 2018 and 3.8 per cent in 2017. Uncertainties, although declining, are still elevated due to protectionist tendencies of China and USA and rising USA-Iran geo-political tensions.
- Amidst a weak environment for **global manufacturing, trade and demand, the Indian economy slowed down with GDP growth moderating to 4.8 per cent in H1 of 2019-20, lower than 6.2 per cent in H2 of 2018-19**. A sharp decline in real fixed investment induced by a sluggish growth of real consumption has weighed down GDP growth from H2 of 2018-19 to H1 of 2019-20.
- Real consumption growth, however, has recovered in Q2 of 2019-20, cushioned by a significant growth in government final consumption. At the same time, India's external sector gained further stability in H1 of 2019-20, with a narrowing of Current Account Deficit (CAD) as percentage of GDP from 2.1 in 2018-19 to 1.5 in H1 of 2019-20, impressive Foreign Direct Investment (FDI), rebounding of portfolio flows and accretion of foreign exchange reserves. Imports have contracted more sharply than exports in H1 of 2019-20, with easing of crude prices, which has mainly driven the narrowing of CAD.
- On the supply side, agricultural growth, though weak, is moderately higher in H1 of 2019-20 than in H2 of 2018-19. Headline inflation rose from 3.3 per cent in H1 of 2019-20 to 7.4 per cent in December 2019 on the back of temporary increase in food inflation, which is expected to decline by year end. Rise in CPI-core and WPI inflation in December 2019 suggests building of demand pressure.
- The **deceleration in GDP growth can be understood within the framework of a slowing cycle of growth with the financial sector acting as a drag on the real sector**. In an attempt to boost demand, 2019-20 has witnessed significant easing of monetary policy with the repo rate having been cut by RBI by 110 basis points.
- Having duly recognized the financial stresses built up in the economy, the government has taken significant steps this year towards speeding up the insolvency resolution process under **Insolvency and Bankruptcy Code (IBC) and easing of credit**, particularly for the stressed real estate and Non-Banking Financial Companies (NBFCs) sectors. At the same time, impact of critical measures taken to boost investment, particularly under the National Infrastructure Pipeline, present green shoots for growth in H2 of 2019-20 and 2020-21.
- Based on first Advance Estimates of India's GDP growth for 2019-20 recorded at 5 per cent, an uptick in GDP growth is expected in H2 of 2019-20. The government must use its strong mandate to deliver expeditiously on reforms, which will enable the economy to strongly rebound in 2020-21.

Chapter-2 Fiscal Developments

- The year 2019-20 has been challenging for the Indian economy owing to the decelerating growth rate experienced in the first half of the year. Amongst the various reforms introduced during the year to promote growth and investment, reduction in corporate income tax rate was a major structural reform.
- The **fiscal policy 2019-20 was characterized by sluggish growth in Tax revenue relative to the budget estimates**. The Non-Tax revenue registered a considerably higher growth in the first eight months of this financial year compared to the same period last year.
- On the expenditure side, Total Expenditure has increased at a considerable pace during April to November 2019-20 with Capital Expenditure growing at roughly three times the growth registered during the same period last year.
- The fiscal deficit as a per cent of Budget Estimate during the first eight months of this financial year was at a similar level as that in the corresponding period last year.
- During the first eight months of 2019-20, the Revenue Receipts registered a higher growth compared to the same period last year, which was led by considerable growth in Non-Tax revenue.
- During 2019-20 (upto December 2019), the gross GST monthly collections has crossed the mark of Rs. one lakh crore for a total of five times.
- Structural reforms undertaken in taxation during the current financial year include change in corporate tax rate and measures to ease the implementation of GST.
- The States have continued on the path of fiscal consolidation and contained the fiscal deficit within the targets set out by the FRBM Act.
- The General Government (Centre plus States) has been on path of fiscal consolidation.
- Going forward, considering the urgent priority of the Government to revive growth in the economy, the fiscal deficit target may have to be relaxed for the current year.

Chapter- 3 External Sector

- India's external sector gained further stability in the first half of 2019-20, witnessing improvement in Balance of Payments (BoP) position. India's foreign reserves are comfortably placed at US$ 461.2 billion as on 10th January, 2020.
- The improvement in BoP was anchored by narrowing of current account deficit (CAD) from 2.1 per cent in 2018-19 to 1.5 per cent of GDP in H1 of 2019-20. The contraction of CAD has emanated from easing of crude prices.
- Export growth remains subdued with external demand weakened by slowdown in global investment, output and heightened trade tensions, notwithstanding resilient service exports. Increase in service imports is inevitable with increasing **foreign direct investment (FDI) and 'Make in India'**.
- Petroleum products, precious stones, drug formulations & biologicals, gold and other precious metals continue to be top exported commodities, with fastest growth seen in drug formulations & biologicals in 2019-20 (April to November). Crude petroleum, gold, petroleum products, coal, coke & briquittes constitute top import items, with fastest growth seen in electronics in 2019-20 (April to November).
- **India's top five trading partners continue to be USA, China, UAE, Saudi Arabia and Hong Kong**. Further improvement in BoP was contributed by easing of external financial conditions, impressive FDI, rebounding of portfolio flows and receipt of robust remittances. Net FDI inflows have continued to be buoyant in 2019-20 attracting US$ 24.4 billion in the first eight months, higher than the corresponding period of 2018-19. Net FPI in the first eight months of 2019-20 stood at US$ 12.6 billion.
- This reflects a global sentiment that increasingly believes in India's growth story and reform measures being undertaken by the government. External debt as at end September, 2019 remains low at 20.1 per cent of GDP.
- India's **Net International Investment Position (NIIP) to GDP ratio has also improved compared to 2018-19**. After witnessing significant decline since 2014-15, India's external liabilities (debt and

equity) to GDP has increased at the end of June, 2019 primarily driven by increase in FDI, portfolio flows and external commercial borrowings (ECBs).

- In sync with an estimated 2.9 per cent growth in global output in 2019, global trade is estimated to grow at 1.0 per cent after having peaked in 2017 at 5.7 per cent. However, it is projected to recover to 2.9 per cent in 2020 with recovery in global economic activity.
- India's merchandise trade balance has improved from 2009-14 to 2014-19 although most of the improvement in the latter period was on account of more than fifty per cent decline in crude prices in 2016-17.
- India's net services surplus has been steadily declining in relation to GDP. It financed two-thirds of merchandise deficit in 2016-17 before declining to less than half in the last couple of years.
- Under trade facilitation, India has improved its ranking from 143 in 2016 to 68 in 2019 under the indicator, "Trading across Borders", monitored by World Bank in determining the overall ranking of around 190 countries in its Ease of Doing Business Report.
- The logistics industry of India is currently estimated to be around US$ 160 billion and is expected to touch US$ 215 billion by 2020.
- Net remittances from Indians employed overseas has been constantly increasing year after year and has continued doing so with the amount received in H1 of 2019-20 being more than fifty per cent of the previous year level.

Chapter-4 Monetary Management and Financial Intermediation

- Monetary policy remained accommodative in 2019-20. The repo rate was cut by 110 basis points in four consecutive Monetary Policy Committee meetings in the financial year due to slower growth and lower inflation. However, it was kept unchanged in the fifth meeting held in December 2019.
- Liquidity conditions were tight for initial two months of 2019-20; but subsequently it has remained comfortable. The financial flows to the economy however, remained constrained as credit growth declined for both banks and Non-Banking Financial Corporations.
- The growth (YoY) of loans from NBFCs declined from 27.6 per cent in September 2018 and 21.6 per cent in December 2018 to 9.9 per cent at end September 2019.
- The Gross Non Performing Advances ratio of Scheduled Commercial Banks has remained unchanged at 9.3 per cent between March and September 2019 and increased slightly for the Non-Banking Financial Corporations from 6.1 per cent to 6.3 per cent.
- Capital to Risk-weighted Asset ratio of Scheduled Commercial Banks increased from 14.3 per cent to 15.1 per cent between March 2019 and September 2019.
- Systemic liquidity has been largely in surplus in 2019-20. Weighted Average Call Money Rate remeined mostly close to repo rate within the Liquidity Adjustment Facility (LAF) corridor.
- Nifty 50 and S&P BSE Sensex indices, reached record high closing of 12,355 and 41,952 respectively during 2019-20 (upto January 16, 2020). The resolution under IBC has been much higher as compared to previous resolution channels. Amount recovered as percentage of amount involved was 49.6 per cent in 2017-18 and 42.5 per cent in 2018-19. The proceedings under IBC take on average about 340 days, including time spent on litigation, in contrast with the previous regime where processes took about 4.3 years.
- The total money raised by public issue and rights increased to Rs. 73,896 crore in 2019-20 (up to December 31, 2019) from Rs. 44,355 crore in the corresponding period last year. Rs. 6.29 lakh crore was raised through private placements in 2019-20 (up to December 31, 2019) as compared to Rs. 5.3 lakh crore in the corresponding period of previous year.
- As on end December 2019, Rs. 1.58 lakh crore were realizable in cases resolved under Corporate Insolvency Resolution Processes.

Chapter-5 Prices and Inflation

- Inflation has been witnessing moderation since 2014 backed by low food inflation. During the current financial year, however, food and beverages inflation has been trending differently. Food inflation has been on an upward trend mainly backed by rising vegetables, fruits and pulses prices.

- However, the volatility in prices of most of the essential agricultural commodities with some exceptions like pulses has been on a downward trend. **Since July 2018, CPI-Urban inflation has been consistently higher than CPI-Rural inflation**, which is in contrast to earlier trend where rural inflation was higher than urban inflation.
- Inflation has been declining in most of the States, however, the variability of inflation has been increasing. Since 2012, there has been a change in inflation dynamics. There is evidence for a strong reversion of headline inflation to core inflation.
- **Transmission of inflation from non-core components to core components is minimal**.
- Headline Consumer Price Index (CPI) inflation was 3.7 per cent in 2018-19 (April to December, 2018), compared to 4.1 per cent in 2019-20 (April to December, 2019).
- During 2019-20, WPI based inflation has been on a continuous fall declining from 3.2 per cent in April 2019, only marginally rising in November and December to end at 2.6 per cent in December 2019.
- Food index which declined on an annual basis between 2017-18 and 2018-19, saw an uptick during the current financial year (April-December, 2019).
- During 2019-20 (April- December), food and beverages emerged as the main contributor to CPI-C inflation, with 54 per cent of the inflation during this period attributable to this group.
- In the four metropolitan cities of the country, retail prices of various essential commodities have diverged from wholesale prices over the years.
- Inflation in fifteen States/Union Territories (UTs) was below 4 percent in FY 2019-20 (April-December). Comparing FY 2018-19 (April- December) with FY 2019-20 (April- December), inflation has actually decreased in eight states.
- Inflation expectations have declined thereby indicating that the inflation targeting framework has started influencing expectations of inflation in the economy.

Chapter-6 Sustainable Development and Climate Change

- The Sustainable Development Goals (SDGs) constitute a befitting framework to answer the developmental challenges to achieve a sustainable future, free from social, economic, and environmental inequalities and thereby ensuring a greener and healthy Planet for future generations.
- **India's achievement in the composite SDG index is commendable as the score has improved from 57 in 2018 to 60 in 2019**. Along with following the holistic approach for achieving the SDGs by implementing a comprehensive array of schemes, India's progress in adopting, implementing, and monitoring SDGs stands noteworthy.
- The SDG indicator linked reporting and monitoring framework helped in exploring the nexus approach to attain development goals of India. As a responsible nation, with the introduction of various schemes, India has been continuously moving towards economic growth, keeping in mind the imperatives of sustainable development. **As per the SDG Index, Kerala, Himachal Pradesh, Tamil Nadu, Andhra Pradesh, Telangana, Karnataka, Goa, Sikkim, Chandigarh and Puducherry are the front runners**.
- India is among a few countries in the world where forest and tree cover have increased considerably. **The forest and tree cover have reached 80.73 million hectare which is 24.56 per cent of the geographical area of the country**. Increased focus on sustainability requires various actions towards building individual and institutional capacity, accelerating knowledge and enhancing technology transfer and deployment, enabling financial mechanisms, implementing early warning systems, undertaking risk management and addressing gaps in implementation and upscaling. These fair and justified demands have been discussed in various multilateral negotiations but remain largely unresolved.
- Burning of agricultural residues, leading to rise in pollutant levels and deterioration of air quality, is still a major concern though the total number of burning events recorded reduced due to various efforts taken.
- Global agenda of delivering sustainable development and addressing climate change can be delivered only if all nations act upon their fair share of responsibilities including the fulfillment on

means of implementation by the developed world to the developing countries. Therefore, enhanced ambition and enhanced support should be on equal footing.

- **India is the second largest Emerging Green Bond Market after China**.
- GCF's first replenishment (2020-2023) witnessed 28 countries pledging resources to replenish the Fund for an amount of US$ 9.7 billion, which is even quantitatively lower than the IRM period.
- At COP 25 of UNFCCC at Madrid, India reiterated its commitment to implement Paris Agreement in accordance with the principles of equity and common but differentiated responsibilities. COP 25 decision provides for balanced and integrated view of ambition that includes efforts for climate change mitigation, adaptation and means of implementation from developed country parties to developing country parties.
- ISA has taken up the role of an 'enabler' by institutionalizing 30 Fellowships from the Member countries; of a 'facilitator' by getting the lines of credit worth US$ 2 Billion from EXIM Bank of India and US$ 1.5 Billion from AfD, France; of an 'incubator' by nurturing initiatives like the Solar Risk Mitigation Initiative and of an 'accelerator' by developing tools to aggregate demand for 1000 MW solar and 270,000 solar water pumps.
- India launched the CDRI, focus on developing resilience in ecological, social and economic infrastructure.
- Government of India hosted COP 14 to UNCCD from 2-13 September, 2019. COP 14 adopted the **Delhi Declaration: Investing in Land and Unlocking Opportunities**.

Chapter-7 Agriculture and Food Management

- **Agriculture and its allied sectors still remain an important sector because of its continued role in employment, income and most importantly in national food security**. Proportion of Indian population depending directly or indirectly on agriculture for employment opportunities is more than that of any other sectors in India. Its contribution to national income has gradually declined from 18.2 per cent in 2014-15 to 16.5 in 2019-20, reflecting the development process and the structural transformation taking place in the economy.
- The **realisation of the objective of doubling farmer's income requires that the challenges of the sector such as access to credit, insurance coverage, irrigation facilities, etc. are addressed**. There is also a need to address the issue of lower farm mechanisation in India which is only about 40 per cent as compared to about 60 per cent in China and around 75 per cent in Brazil.
- Given the fact that the **livestock sector has grown at a compound annual growth rate of nearly 8 per cent over the last five years**, it assumes an important role in income, employment and nutritional security. Though, the food processing sector is growing at an average annual growth rate of more than 5 per cent over the last six years ending 2017-18, more focussed attention to the sector is required due to its significant role in reducing post-harvest losses and creation of additional market for farm outputs. With the implementation of the National Food Security Act from July 2013, the food subsidy bill has increased from Rs. 113171.2 crore in 2014-15 to Rs. 171127.5 crore in 2018-19.
- India's food management should focus on rationalisation of food subsidy while addressing the challenges of food security, especially of the most vulnerable sections.
- The **regional distribution of agricultural credit in India shows a highly skewed pattern. It is seen that credit is low in North Eastern, Hilly and Eastern States. The share of North Eastern States has been less than one percent in total agricultural credit disbursement**.

Chapter-8 Industry and Infrastructure

- The industrial sector based on Index of Industrial Production (IIP) registered a growth of 0.6 per cent for 2019-20 (April-November) as compared to 5.0 per cent during 2018-19 (April-November).
- Growth of manufacturing sector was 0.9 per cent during 2019-20 (April-November) as compared to 4.9 per cent during 2018-19 (April-November).
- Growth of refinery products sector stood at (-)1.1 per cent during 2019-20 (April-November) as compared to 5.3 per cent during 2018-19 (April-November). Steel sector achieved a growth of

5.2 per cent during 2019-20 (April-November) as compared to 3.6 per cent during 2018-19 (April-November).

- Government has initiated several policies in various infrastructure sectors to enhance their capacity and output.
- Report of the Task Force on National Infrastructure Pipeline released on 31.12.2019 has projected total infrastructure investment of ` 102 lakh crore during the period FY 2020 to 2025 in India.
- Fertilizer sector achieved a growth of 4.0 per cent during 2019-20 (April-November) as compared to (-)1.3 per cent during 2018-19 (April-November). ¬ India has considerably improved its ranking in Ease of Doing Business to 63rd position in 2019 compared to 77th position in 2018.
- Crude steel production witnessed growth of 1.5 per cent during 2019-20 (April-October).
- The installed capacity of power generation has increased to 3,64,960 MW as on 31 October 2019.
- Report of the Task Force on National Infrastructure Pipeline released on 31.12.2019 has projected total infrastructure investment of ` 102 lakh crore during the period FY 2020 to 2025 in India.

Chapter-9 Services Sector

- The **services sector's significance in the Indian economy has continued to increase, with the sector now accounting for around 55 per cent of total size of the economy and GVA growth, two-thirds of total FDI inflows into India and about 38 per cent of total exports**. The share of services sector now exceeds 50 per cent of Gross State Value Added in 15 out of the 33 states and UTs, with this share more than 80 per cent in Delhi and Chandigarh.
- However, data on GVA growth, high-frequency indicators and sectoral trends suggest a moderation in services sector activity during 2019-20. Bank credit to services sector, air passenger traffic and rail freight traffic have witnessed a deceleration, while foreign tourist arrivals and port traffic have continued to ease during 2019-20.
- On the bright side, the very latest readings on most of these indicators suggest a recovery. Moreover, gross FDI equity inflows into services sector have registered a strong recovery and services exports have maintained their momentum during April-September 2019.
- **Services exports have outperformed goods exports in the recent years**, due to which India's share in world's commercial services exports has risen steadily over the past decade to reach 3.5 per cent in 2018, twice the share in world's merchandise exports at 1.7 per cent.
- **India's education services imports have increased markedly in the recent years**, up from about US$ 2.3 billion in 2013-14 to US$ 5.0 billion in 2018-19. The shipping turnaround time at ports has almost halved from 4.67 days in 2010-11 to 2.48 days in 2018-19. India has launched around 5-7 satellites per year in the recent years with no failures, barring one in 2017.

Chapter- 10 Social Infrastructure, Employment and Human Development

- Considering India's demographic advantage of a large young population in the productive age group, improvements in the social sectors like education, health care, water supply and sanitation leaves a profound impact on the quality of life of the people as well as to the productivity of the economy.
- Interventions made to reach out to all sections of the society includes fundamental changes in design of the policies/schemes, expanding the reach through people's participation, awareness generation, technology use, and direct benefit transfer.
- Expenditure on social services, as a proportion of GDP, has increased by 1.5 percentage points during the period 2014-15 to 2019-20. **Access to education has improved the participation in education system at all levels both in rural and urban areas. Scaling up of the efforts to impart necessary skills through a wide network of ITIs focusing on women has pushed the skill development up**. Gross Enrolment Ratio at secondary, higher secondary and higher education level needs to be improved.

- **Gender disparity in India's labour market widened due to decline in female labour force participation especially in rural areas and around 60 per cent of productive age (15-59) group are engaged in full time domestic duties**.
- Total formal employment in the economy increased from 8 per cent in 2011-12 to 9.98 per cent in 2017-18. Access to health services, inter-alia, through **Ayushman Bharat and Mission Indradhanush across the country has improved.** Mission Indradhanush has vaccinated 3.39 crore children and 87.18 lakh pregnant women of 681 districts across the country.
- About 76.7 per cent of the households in the rural and about 96 per cent in the urban areas had houses of pucca structure. **Jal Shakti Abhiyan launched to accelerate progress on water conservation activities in water stressed districts of India**.

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DAY - 58

DEVELOPMENTAL ECONOMICS

Introduction:

- Development economics is a branch of economics that focuses on improving fiscal, economic, and social conditions in developing countries.
- Development economics considers factors such as health, education, working conditions, domestic and international policies, and market condition with a focus on improving conditions in the world's poorest countries.
- Development economics studies the transformation of emerging nations into more prosperous nations. Strategies for transforming a developing economy tend to be unique because the social and political backgrounds of countries can vary dramatically.
- Some aspects of development economics include determining to what extent rapid population growth helps or hinders development, the structural transformation of economies, and the role of education and health care in development.
- They also include international trade and globalization, sustainable development, the effect of epidemics such as HIV and AIDS, and the impact of catastrophes on economic and human development.

Main Indicators of the Developmental economics:

- Poverty
- Unemployment
- Social Infrastructure

Poverty:

Concept:

- Poverty is a social phenomenon wherein a section of society is unable to fulfill even its basic necessities of life. The UN Human Rights Council has defined poverty as "A human condition characterized by the sustained or chronic deprivation of the resources, capabilities, choices, security and power necessary for the enjoyment of an adequate standard of living and other civil, cultural, economic, political and social rights".
- The poor are those who live Below the Poverty Line (BPL). The poverty line is defined in terms of per capita household expenditure. Poverty manifests itself in the form of both absolute poverty as well as relative poverty.

Causes of Poverty:

The extent of poverty in an economy is due to a wide range of factors as follows:

- Underdeveloped nature of economy.
- Rapid growth of population in an overpopulated country; even if the national income increases, the per capita income remains the same due to increase in population.

- Large inequalities in the ownership of earning assets such as land, buildings, industry etc.
- Low level of productivity in agriculture and industry.
- Large scale unemployment and under-employment.
- Inequality of opportunity in acquiring education and skills.
- State Policies.
- Regional disparities.

Types of Poverty:

- **Absolute Poverty:**
  - This concept is based on absolute needs of the people and people are defined as poor when some absolute needs are not sufficiently satisfied. It is also defined in terms of insufficiency of basic needs. In India, these basic needs are measured in terms of calorie intake of 2400 in rural areas per person per day and 2100 in urban areas. The corresponding monetary yardstick for calorie intake is based on per capita monthly household expenditure.
- **Relative Poverty**
  - This concept is related to the general standard of living in a society. Thus, according to this concept, people are poor because they are deprived of the opportunities, comforts and self-respect regarded as normal in the community to which they belong. In relative poverty, poor are defined as, a person or family whose incomes are less than the average income of the community. Thus, Relative Poverty relates to inequalities in a society. India is characterised by both in extreme measures, i.e., absolute and relative poverty.
- **Situational Poverty**
  - It is a temporary type of poverty based on occurrence of an adverse event like environmental disaster, job loss and severe health problem. People can help themselves even with a small assistance, as the poverty comes because of unfortunate events.
- **Generational Poverty**
  - It is handed over to individual and families from one generation to the another. This is more complicated as there is no escape because the people are trapped in its cause and unable to access the tools required to get out of it.
- **Rural Poverty**
  - It occurs in rural areas with population below 50,000. It is the area where there are less job opportunities, less access to services, less support for disabilities and quality education opportunities. People are tending to live mostly on the farming and other menial work available to the surroundings.
- **Poverty line basket:**
  - Determining composition of the basket is among most debated part of the issue. To make a living people consume innumerable items. Apart from food; housing, fuel, health, education, communication, conveyance, entertainment/recreations are the things which are important. But whether they should be included or not, if so their weights in basket, whether health should get preference over housing, or whether reasonable expenditure on recreation be included in basket etc. are toughest questions to be answered. Problem is that these are qualitative aspects, which are needed to be quantified.

Poverty in India:

2000s onwards:

- The **Saxena Committee report**, using data from 1972 to 2000, separated calorific intake apart from nominal income in its economic analysis of poverty in India, and then stated that 50% of Indians lived below the poverty line. The Planning Commission of India, in contrast, determined that the poverty rate was 39%.

- The **Suresh Tendulkar Committee** set up to look into the people living under the poverty line in India submitted its report in November 2009. It provided a new method of calculating the poverty line based on per capita consumption expenditure per month or day. For rural areas, it was Rs 816 per month or Rs 27 per day. For urban areas, it was Rs 1000 per month or Rs 33 per day. Using this methodology, the population below the poverty line in 2009-2010 was 354 million (29.6% of the population) and that in 2011-2012 was 269 million (21.9% of the population).
- The **Rangarajan Committee** set up to look into the poverty line estimation in India submitted its report in June 2014. It amended the calculation of the poverty line based on per capita consumption expenditure per month or day given by the Tendulkar Committee. The new poverty threshold for rural areas was fixed at Rs 972 per month or Rs 32 per day. For urban areas, it was fixed at Rs 1407 per month or Rs 47 per day.
- Under this methodology, the population below the poverty line in 2009-2010 was 454 million (38.2% of the population) and that in 2011-2012 was 363 million (29.5% of the population).

Anti-Poverty Strategy:

- Inclusive growth
- Financial Inclusion

Major Reasons for Failure of Poverty Alleviation Programmes:

- Planning process is faulty
- Identifying the 'poor'
- Defining 'poor'
- Processing of the identification involves too many stages.
- Lack of technology up gradation.
- Ideally the programs should be broader based. (benefitting the large number of people).
- Disjointed programs- not integrated. (Beneficiaries overlap, the same rural areas benefited from served programs.)
- Implementation of programs:
- Corrupt officials/ staffs.
- Lack of involvement of people.
- Local politics. (selection of beneficiaries)
- Improper follow up of program/ review or revision is practically none existed.
- Lack of support from the credit and marketing system:
- Role of local money lenders and banks.
- Inability to sustain income generation from the asset credited.

Steps Needed:

- Adopt a comprehensive reform approach to further lower the incidence of poverty and reverse the pattern of growing inequality. This multi-dimensional approach must include education, health care and labour market reforms.
- Enhance the cost effectiveness properties of the MGNREGA, by ensuring that the wage is set at a level around the minimum wage.
- Re-target environmentally harmful subsidies, to more directly support poor households and increase equity.
- Tackle regulatory and infrastructure barriers still preventing small towns from realising their potential.

Unemployment:

Concept:

Unemployment is a situation when a capable and willing to do job workforce does not get work.

Phillips Curve

It is a graphic curve which advocates a relationship between inflation and unemployment in an economy. As per the curve there is a 'trade of' between inflation and unemployment, i.e., an inverse relationship between them. The curve suggests that lower the inflation, higher the unemployment and higher the inflation, lower the unemployment.

Business Cycle

The business cycle describes the rise and falling production output of goods and services in an economy.

Types of Unemployment:

- **Cyclical Unemployment:** It is caused due to business cycle. This kind of an unemployment occurs when all those who want to work cannot be employed because there is not enough demand in the market for their work. It is called as, cyclical unemployment because it varies with the trade cycle.
- **Frictional Unemployment:** This kind of unemployment occurs when a person leaves/loses a job and starts looking for another one. This search for a job may take a considerable amount of time resulting in frictional unemployment. Frictional unemployment tends to be on a high when an economy is not doing so well and low otherwise because during good times it will be easier for people to find jobs that match their skills and requirements easily.
- **Seasonal Unemployment:** This kind of unemployment is expected to occur at certain parts of the year. For example, the jobs at a hill station may experiences seasonal unemployment during the winter months because less people will visit these areas during this time.
- **Structural Unemployment:** This kind of unemployment happens when the structure of an industry changes. For example, as the country is tending to move from use of bicycles to motorbikes and cars, the demand for labor in the cycle industry has continuously fallen in the country.
- **Full Employment:** Employment would be full literally when every able-bodied adult works the number of hours considered normal for a fully employed person.
- **Under Employment:** This term can be used in multiple connotations but one of the primary usage is to showcase a situation where a person with high skills works in low wage and low skills job.
- **Disguised Unemployment:** Such type of unemployment is quite common in the agri-cultural sector in India. It occurs when people are employed in a job where their presence or absence does not make any difference to the output of the economy.

Nature of Unemployment in India:

- India being a developing country, the nature of unemployment therefore is in stark contrast to the one observed in the developed countries. In developed countries, unemployment is driven by a fall in demand because as the demand for goods and services, machines fall idle and the demand for labour goes down. But in India, the bigger problem is that of under-employment or disguised unemployment, which is not due to the lack of demand for goods but due to the shortage of capital equipment etc. in the economy. Because of lack of capital stock, India has not been able to commensurately meet the needs of the growing labour force in the country.

This manifests itself in two ways:

- The prevalence of large scale unemployment in the urban areas.
- In rural areas the growing numbers engaging themselves in the agricultural sector resulting in disguised unemployment.

- As per one of NSS data 8.5 million people in the rural areas and 1.2 million people in the urban areas work for less than 14 hours a week resulting in underemployment.

Solution:

- The basic solution to the entire problem is faster rate of capital formation so as to enlarge employment opportunities. For this the government needs to encourage savings and their productive utilization in increasing the rate of investment. The state itself can participate in the process of capital formation by undertaking such development activities as the private entrepreneurs do not find it profitable to undertake. There is also a need for the government to increase and attract more foreign investment in a country like India.

Social Infrastructure:

What is Social Infrastructure?

Infrastructure can broadly be defined as long-term physical assets that operate in markets with high barriers to entry and enable the provision of goods and services. Social services include, education, sports, art and culture; medical and public health, family welfare, water supply and sanitation, housing; urban development; welfare of Schedule Castes (SCs), Schedule Tribes (STs) and Other Backward Castes (OBCs), labour and labour welfare; social security and welfare, nutrition, relief on account of natural calamities etc. Expenditure on 'Education' pertains to expenditure on 'Education, Sports, Arts and Culture'.

Status of Social Sector in India:

The expenditure on social infrastructure like health and education is a critical indicator of the commitment of the government towards these sectors. Public investment in social infrastructure has a critical role in providing access to social services for the people, especially the marginal and vulnerable sections of the society. The expenditure on social services by the Centre and States as a proportion of Gross Domestic Product (GDP) has registered an increase of more than 1 percentage points during the period 2014-15 to 2018-19 (BE), from 6.2 per cent in 2014- 15 to 7.3 per cent in 2018-19 (BE). The increase was witnessed across all social sectors especially education where the public expenditure as a per cent of GDP increased from 2.8 per cent in 2014-15 to 3 per cent in 2018-19. The share of expenditure on social services out of total budgetary expenditure increased from 24.9 per cent in 2013-14 to 26 per cent in 2018-19.

- **Education in India:** As per Educational Statistics at a Glance (ESAG), 2018, the thrust on providing primary education has yielded results across social categories and gender in Gross Enrolment Rate (GER). Over the years, remarkable progress has been made in respect of female participation up-to secondary level and GER for girls has exceeded that of boys. But girls' enrolment rate is lower than that of boys at the higher education level. At this level, the gap is visible across the social categories too. The Pupil Teacher Ratio (PTR) at national level for primary schools is 23, 17 for upper primary, 27 for secondary and 37 for senior secondary schools.
- **Gender Parity Index (GPI) based on GER:** GPI based on GER indicates increasing trend of female participation at all levels. At the higher education level the GPI is low. Although, enrolment of girls is higher than that of boys in government schools, the pattern gets reversed in private schools. The gender gap in enrolment in private schools has consistently increased across age groups.
- **Status of Health:** Public health expenditure (centre, states and local bodies), as a percentage of Total Health Expenditure (THE) increased from 22.5 per cent in 2004-05 to 30.6 per cent in 2015-16. The National Health Mission (NHM), with its two sub-missions National Urban Health Mission (NUHM) and National Rural Health Mission (NRHM) envisages achievement of universal access to equitable, affordable and quality healthcare services that are accountable and responsive to peoples' needs. Under this Mission, support is provided to States/UTs to provide accessible, affordable, accountable and effective healthcare up to District Hospital level. Major programme components under NRHM are Reproductive-Maternal- Neonatal-Child and Adolescent Health and Communicable and Non-Communicable diseases.

- **Skill Development:** The schooling system improves the educational level of the population. It is skill training that equip the youth to enter the labour market and improves their employability. According to NSSO Report 2011-12, only 2.3 per cent of the total workforce in India had formal sector skill training. Keeping in view the predominance of young population, the government had formulated the National Policy on Skill Development & Entrepreneurship, 2015 under which the Skill India Mission by 2022 was formulated.

Government Initiatives:

The government has been committed to provision of social security which is evident in the initiation of major social sector schemes by the Government of India during the last five years given below:

- **Pradhan Mantri Suraksha Bima Yojana, 2015 -** It offers a one-year accidental death and disability cover with annual premium of Rs. 12. It is available to people in the age group 18 to 70 years.
- **Pradhan Mantri Jeevan Jyoti Bima Yojana, 2015 -** It is government-backed life insurance scheme with annual premium of Rs. 330. It is available to people between 18 and 50 years of age.
- **Pradhan Mantri Vaya Vandana Yojana,** 2018 - It is a pension scheme exclusively for the senior citizens aged 60 years and above.
- PM-KISAN, 2019 - It offers income support of Rs. 6000 per annum in three equal instalments to all eligible farmers irrespective of land holdings.
- **National Nutrition Mission (POSHAN Abhiyaan) -** It ensure attainment of malnutrition free India by 2022. Targeted intervention in areas with high malnutrition burden.
- **Skilling Ecosystem -** Skilling ecosystem in India is equipping the youth to meet the challenges of a dynamic labour market by providing various short term and long term skilling under programmes like **'Pradhan Mantri Kaushal Vikas Yojana' (PMKVY).** PMKVY has had positive impact on employment and incomes of the youth as per evaluation studies.
- **Rural Infrastructure -** Connectivity is critical for rural areas to improve quality of lives of the poor by enhancing access to various social services, education, health and access to markets. PMGSY has played a crucial role in connecting the unconnected in rural India and enhanced their livelihood opportunities. Government has accorded highest priority to rural housing, by providing dwelling with all basic facilities to the most needy under **Pradhan Mantri Awas Yojana (Gramin) (PMAY-G)**. Government has also prioritized employment programmes like MGNREGS which is reflected in the upward trend in budget allocation and release of funds to the States in the last four years.
- **Financial Inclusion -** Financial inclusion of women is considered as an essential tool for empowerment of women as it enhances their self confidence and enables financial decision-making to a certain extent. As far as financial inclusion in India is concerned, significant progress has been made during the last decade. At all India level, the proportion of women having a bank or saving account that they themselves use have increased from 15.5 per cent in 2005-06 to 53 per cent in 2015-16.

Way Forward:

- India's development trajectory is critically intertwined with the investments in social infrastructure. To reap the benefits of demographic dividend, the government is committed to improve the outcomes in education and skilling and to provide employment and affordable healthcare to all.
- Scaling up development programmes for improving connectivity, providing housing and bridging gender gaps in socio-economic indicators is of paramount importance for sustainable development. India's march towards achieving SDGs is firmly anchored in investing in human capital and inclusive growth.
- Inclusiveness has been the cornerstone of India's development agenda. As India is a developing economy with resource constraints, we have to prioritize and optimize the expenditure on social infrastructure to promote sustainable and inclusive growth.

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DAY - 59

INDUSTRY

Introduction

- The classification of industries can be done on the basis of
  - **size, capital investment, and labor force employed, industries are classified as large, medium, small scale, and cottage industries.**
  - **ownership, industries come under public sector, private sector, joint, and cooperative sector.**
  - **Industries are also classified on the basis of the use of their products such as basic goods industries, capital goods industries, intermediate goods industries, and consumer goods industries**.
  - On the basis of raw materials used by the industries – industries are categorized as agriculture-based industries, forest-based industries, mineral-based industries, and industrially processed raw material-based industries.
  - Location of industries is influenced by several factors like access to raw materials, power, market, capital, transport, and labor, etc.
- Industries of strategic and national importance are usually in the public sector.
- The establishment of iron and steel industry in Bhilai (Chhattisgarh) and Rourkela (Odisha) were based on decision to develop backward tribal areas of the country.

Iron and Steel Industry

- The **major raw materials for the iron and steel industries are iron ore, coking coal, limestone, dolomite, manganese, and fire clay**.
- Major iron and steel industries in India are –
  - The Tata Iron and Steel plant (TISCO);
  - The Indian Iron and Steel Company (IISCO);
  - Rourkela Steel Plant;
  - Bhilai Steel Plant;
  - Durgapur Steel Plant; and
  - Bokaro Steel Plant.
- Some other major iron and steel industries are –
  - Vizag Steel Plant, in Vishakhapatnam in Andhra Pradesh is the first port based plant which established in 1992.
  - The Vijaynagar Steel Plant in Karnataka was developed by using indigenous technology.
  - The Salem Steel Plant in Tamil Nadu was commissioned in 1982.
- The **Rourkela Steel plant** was set up in the year 1959 in the Sundargarh district of Odisha in collaboration with Germany.

- The **Bhilai Steel Plant** was established in 1959 with Russian collaboration in Durg District of Chhattisgarh.
- **Durgapur Steel Plant** was established in 1962 in West Bengal, in collaboration with the government of the United Kingdom
- **Bokaro steel plant** was set up in 1964 at Bokaro with Russian collaboration.
- **Pittsburg is an important steel city of the United States of America**. The steel industry at Pittsburgh enjoys locational advantages. Some of the raw material such as coal is available locally, while the iron ore comes from the iron mines at Minnesota, about 1500 km from Pittsburgh.

Cotton Industry

- India was famous worldwide for the production of *muslin*, a very fine variety of cotton cloth, calicos, chintz, and other different varieties of fine cotton cloth.
- In **1854**, the first modern cotton mill was established in Mumbai.
- At present, the major centers of the cotton textile industry are Ahmedabad, Bhiwandi, Solapur, Kolhapur, Nagpur, Indore, and Ujjain.
- **Tamil Nadu has the largest number of mills**; however, most of them produce yarn rather than cloth.
- Davangere, Hubballi, Ballari, Mysuru, and Bengaluru are important cotton growing regions in Karnataka.
- **Osaka is an important textile centre of Japan, also known as the 'Manchester of Japan'**. The textile industry at Osaka depends completely upon imported raw materials. Cotton is imported from Egypt, India, China and USA.

Sugar Industry

- With more than one-third of the total production, **Maharashtra has emerged as a leading sugar producer in the country**.
- **Uttar Pradesh is the second largest producer of sugar**.

Petrochemical Industry

- Many items are derived from crude petroleum, which provide raw materials for many new industries; hence, these are collectively known as petrochemical industries.
- Petrochemical industries are categorized as polymers, synthetic fibers, elastomers, and surfactant intermediate industries.
- Mumbai is the hub of petrochemical industries.
- Three organizations, which are working in the petrochemical sector under the administrative control of the **Department of Chemicals** and **Petrochemicals** are –
  - The Indian Petrochemical Corporation Limited (IPCL);
  - The Petrofils Cooperative Limited (PCL);
  - The Central Institute of Plastic Engineering and Technology (CIPET).
  - The **National Organic Chemicals Industries Limited** (NOCIL), established as private sector in 1961.

Information Technology

- The Information Technology (IT) revolution opened up new possibilities of economic and social transformation.

- The IT software and services industry account for almost 2% of India's GDP.
- India is also doing wonders in the field of supercomputers, its computes got success to feature in top 500 ranks, e.g; PARAM SHIVAY, PARAM Yuva etc.
- Silicon Valley is a part of Santa Clara Valley, located next to the Rocky Mountains of North America. The area has temperate climate with the temperatures rarely dropping below 0 degrees centigrade.
- Bangalore is located on the Deccan Plateau from where it gets the name 'Silicon Plateau'. The city is known for its mild climate throughout the year. There are other emerging information technology hubs in metropolitan centres of India such as Mumbai, New Delhi, Hyderabad and Chennai. Other cities such as Gurgaon, Pune, Thiruvanthapuram, Kochi and Chandigarh are also important centres of the IT industry. However, Bangalore has always had a unique advantage, as a city with highest availability of middle and top management talent.

Industrial Policy

The highlights of the Industrial Policy, 1991 are:

- Industrial licensing will be abolished for all projects except for a short list of industries (18 selected sectors mentioned in Annexure II). The exemption from licensing will apply to all substantial expansion of existing units. The existing and new industrial units will be provided with a broad banding facility to enable them to produce any article so long as no additional investment in plant and machinery is involved.
  - However, the small-scale industries taking up manufacture of those products reserved for small sector will not be subjected to compulsory licensing procedures. As a result, all existing registration schemes (like delicensed registration, exempted industries registration, DGTD registration) will be abolished. Now, entrepreneurs are required to fill an information memorandum of new projects and substantial expansion.
- The policy provides for automatic clearance for import of capital goods in cases where the foreign exchange availability is ensured through foreign equity.
- As for the MRTP Act, the policy states that the pre-entry scrutiny of investment decisions by the so-called MRTP companies will no longer be required.
- The policy intends to scrap the asset limit of the MRTP companies.
- The policy envisages disinvestment of government equity in public sector to mutual funds, financial institutions, general public and workers. For the first time, sick public units has come under the purview of the Board of Industrial and Financial Reconstruction (BIFR) for their revival. A social security mechanism to protect workers' interests in such affected public sectors has been proposed in this policy. Pre-eminent place of public sector in 5 core areas like arms and ammunition, atomic energy, mineral oils, rail transport and mining will, however, continue.
  - Reservation for the public sector, as on 2008, is very limited (just 2)—covering only manufacturing involving certain substances relevant for atomic energy (as well as production of atomic energy) and provision of railway transport.
- In order to invite foreign investment in high priority industries, requiring large investments and advanced technology, it has been decided to provide approval for direct foreign investment up to 51 p.c. foreign equity in such industries.
- In a departure from the present locational policy for industries, the policy provides that in locations other than cities of population of more than one million, there will be no requirement for obtaining industrial approvals except for industries subject to compulsory licensing.

Industrial Regions

- India has **eight** major industrial regions namely (as shown on the map given below) –
  - Mumbai-Pune Region,
  - Hugli Region,

- Bengaluru-Tamil Nadu Region,
- Gujarat Region,
- Chhotanagpur Region,
- Vishakhapatnam-Guntur Region,
- Gurgaon-Delhi-Meerut Region, and
- Kollam-Thiruvananthapuram Region.

Infrastructure

Introduction

- Infrastructure provides **supporting services in the main areas of industrial and agricultural production, domestic and foreign trade and commerce**.
- These **services include roads, railways, ports, airports, dams, power stations, oil and gas pipelines, telecommunication facilities, the country's educational system including schools and colleges, health system including hospitals, sanitary system including clean drinking water facilities and the monetary system including banks, insurance and other financial institutions**.
- Some of these facilities have a direct impact on production of goods and services while others give indirect support by building the social sector of the economy.
- **Infrastructure is the support system on which depends the efficient working of a modern industrial economy**. Modern agriculture also largely depends on it for speedy and large-scale transport of seeds, pesticides, fertilisers and the produce using modern roadways, railways and shipping facilities.
- In recent times, agriculture also depends on insurance and banking facilities because of its need to operate on a very large scale. Infrastructure contributes to economic development of a country both by increasing the productivity of the factors of production and improving the quality of life of its people. Inadequate infrastructure can have multiple adverse effects on health.
- **Improvements in water supply and sanitation have a large impact by reducing morbidity** (meaning proneness to fall ill) from major waterborne diseases and reducing the severity of disease when it occurs.
- In addition to the obvious linkage between water and sanitation and health, the quality of transport and communication infrastructure can affect access to health care. Air pollution and safety hazards connected to transportation also affect morbidity, particularly in densely populated areas.

Energy

- There are **commercial and non-commercial sources of energy**.
  - Commercial sources are coal, petroleum and electricity as they are bought and sold.
  - Non-commercial sources of energy are firewood, agricultural waste and dried dung. These are noncommercial as they are found in nature/forests.
- While commercial sources of energy are generally exhaustible (with the exception of hydropower), noncommercial sources are generally renewable. More than 60 per cent of Indian households depend on traditional sources of energy for meeting their regular cooking and heating needs.
- Both commercial and non-commercial sources of energy are known as conventional sources of energy. **There are three other sources of energy which are commonly termed as non-conventional sources — solar energy, wind energy and tidal power. Being a tropical country, India has almost unlimited potential for producing all three types of energy** if some appropriate cost effective technologies that are already available are used.
- **In India, commercial energy consumption makes up about 74 per cent of the total energy consumed in India**. This includes coal with the largest share of 54 per cent, followed by oil at 32 per cent, natural gas at 10 per cent and hydro energy at 2 per cent. Non-commercial energy sources

consisting of firewood, cow dung and agricultural wastes account for over 26 per cent of the total energy consumption.

- **In India, in 2018-19, thermal sources accounted for 70 per cent of the power generation capacity. Hydel and wind power accounted for 16 per cent while nuclear power accounted only for 2 per cent.** India's energy policy encourages two energy sources— hydel and wind —as they do not rely on fossil fuel and, hence, avoid carbon emissions.

Health

- Development of health infrastructure ensures a country of healthy manpower for production of goods and services. The government has the constitutional obligation to guide and regulate all health related issues such as medical education, adulteration of food, drugs and poisons, medical profession, vital statistics, mental deficiency and lunacy. **The Union Government evolves broad policies and plans through the Central Council of Health and Family Welfare**.
- In recent times, while the public health sector has not been so successful in delivering the goods about which we will study more in the next section, private sector has grown by leaps and bounds. More than 70 per cent of the hospitals in India are run by the private sector. They control nearly two-fifth of beds available in the hospitals. Nearly 60 per cent of dispensaries are run by the same private sector. They provide healthcare for 80 per cent of outpatients and 46 per cent of in-patients.
- In recent times, private sector has been playing a dominant role in medical education and training, medical technology and diagnostics, manufacture and sale of pharmaceuticals, hospital construction and the provision of medical services.
- India's health infrastructure and health care is **made up of a three-tier system —primary, secondary and tertiary.**
  - **Primary health care includes education concerning prevailing health problems and methods of identifying, preventing and controlling them; promotion of food supply and proper nutrition and adequate supply of water and basic sanitation; maternal and child health care; immunisation against major infectious diseases and injuries; promotion of mental health and provision of essential drugs**.
  - Auxiliary Nursing Midwife (ANM) is the first person who provides primary healthcare in rural areas. In order to provide primary health care, hospitals have been set up in villages and small towns which are generally manned by a single doctor, a nurse and a limited quantity of medicines. They are known as Primary Health Centres (PHC), Community Health Centres (CHC) and sub-centres.
  - When the condition of a patient is not managed by PHCs, they are referred to secondary or tertiary hospitals. Hospitals which have better facilities for surgery, X-ray, Electro Cardio Gram (ECG) are called secondary health care institutions. They function both as primary health care provider and also provide better healthcare facilities. They are mostly located in district headquarters and in big towns. All those hospitals which have advanced level equipment and medicines and undertake all the complicated health problems, which could not be managed by primary and secondary hospitals, come under the tertiary sector.
  - **The tertiary sector also includes many premier institutes which not only impart quality medical education and conduct research but also provide specialised health care**. Some of them are — All India Institute of Medical Science, New Delhi; Post Graduate Institute, Chandigarh etc.
- **Indian Systems of Medicine (ISM):** It includes six systems — Ayurveda, Yoga, Unani, Siddha, Naturopathy and Homeopathy (AYUSH). At present there are 3167 ISM hospitals, 26,000 dispensaries and as many as 7 lakh registered practitioners in India.

Road Transport

- **Road Transport India has one of the largest road networks in the world with a total length of 42.3 lakh km (2008-09)**. About 85 per cent of passenger and (1961) was introduced to improve the conditions of roads in India. However, roads continue to concentrate in and around urban centres. Rural and remote areas had the least connectivity by road. For the purpose of construction and maintenance, roads are classified as National Highways (NH), State Highways(SH), Major District Roads and Rural Roads.

- The **National Highways Authority of India (NHAI) was operationalised in 1995**. It is an autonomous body under the Ministry of Surface Transport. It is entrusted with the responsibility of development, maintenance and operation of National Highways. This is also the apex body to improve the quality of the roads designated as National Highways.

The major initiative undertaken by the government for the development of road sector are:

- **The National Highway Development Project (NHDP).**
- **Pradhan Mantri Bharat Jodo Pariyojana (PMBJP): linking of major cities to National Highways.**
- **Pradhan Mantri Gram Sadak Yojana (PMGSY): Construction of Rural roads.**

National Highway Development Project

- NHDP deal with the development of high quality highways. NHDP is the largest highway project undertaken in the country. It has been implemented by the National Highway Authority of India (NHAI).
- Initially, The National Highway Development Project (NHDP) consists of two major components:
- The “Golden Quadrilateral”: The Golden Quadrilateral” project will connect the four major metropolitan cities (Delhi. Mumbai, Chennai & Kolkata) with 4-6 lane highways, with a total length of about 5,850 km.
- The “North South – East West” projects: The “North South – East West” project will connect the Northern most point of the country to the Southernmost, and similarly from East to West, with a total length of about 7,300 km
- The NHDP was expected to cost Rs 540 billion, when started in 1998. The financing pattern of this project indicates that private sector participation in the form of investment amounts to only Rs 40 billion (7.4 per cent of the total).
- Over the course of the project, institutions like the World Bank, Asian Development Bank (ADB) and Japanese Bank for International Cooperation (JBIC) are expected to finance about Rs 200 billion; another Rs 200 billion of investment would be financed from the cess.

Rail Transport

- **Indian railways network is one of the longest in the world**. It facilitates the movement of both freight and passengers and contributes to the growth of economy. Mahatma Gandhi said, the Indian railways “brought people of diverse cultures together to contribute to India’s freedom struggle.”
- **Indian Railway was introduced in 1853**, when a line was constructed from Bombay to Thane covering a distance of 34 km. Indian Railways is the largest government undertaking in the country. **The length of Indian Railways network is 64460 km. as on 31 March 2011**.
- **Metro rail has revolutionlised the urban transport system in Kolkata and Delhi**. The replacement of diesel buses by CNG run vehicles along with introduction of metro is a welcome step towards controlling the air pollution in urban centres. **Now, the metro rail projects are running in other metropolitans like Chennai, Mumbai, Lucknow etc**.

Water Transport

Inland Waterways

- It was the chief mode of transport before the advent of railways. It, however, faced tough competition from road and railway transport.
- **India has 14,500 km of navigable waterways, contributing about 1% to the country’s transportation**. It comprises rivers, canals, backwaters, creeks, etc. At present, 5,685 km of major rivers are navigable by mechanised flat bottom vessels.

- For the development, maintenance and regulation of national waterways in the country, **the Inland Waterways Authority was set up in 1986**.
- Out of the 111 National Waterways (NWs) declared under the National Waterways Act, 2016, 13 NWs are operational for shipping and navigation and cargo/passenger vessels are moving on them. The details of operational NWs are as follows:

Details of Operational National Waterways

S. No.	National Waterway (NW) No.	Length (km)	Location (S)
1.	**NW-1:** Ganga-Bhagirathi-Hooghly River System (Haldia - Allahabad)	1620	Uttar Pradesh, Bihar, Jharkhand, West Bengal
2.	**NW-2**: Brahmaputra River (Dhubri - Sadiya)	891	Assam
3.	**NW-3**: West Coast Canal (Kottapuram - Kollam), Champakara and Udyogmandal Canals	205	Kerala
4.	**NW-4:** Phase-1 development of the stretch Muktiyala to Vijyawada of river Krishna	82	Andhra Pradesh
5. 6. 7. 8.	**Waterways in Maharashtra** **i) NW-10** (Amba River) **ii) NW-83 (**Rajpuri Creek**)** **iii) NW-85** (Revadanda Creek - Kundalika River System) **iv) NW-91** (Shastri river–Jaigad creek system)	45 31 31 52	Maharashtra
9. 10.	**NW-68 – Mandovi –** Usgaon Bridge to Arabian Sea (41 km) **NW-111 – Zuari–** Sanvordem Bridge to Marmugao Port (50 km).	41 50	Goa
11. 12.	**NW-73- Narmada river-** **NW-100- Tapi river**	226 436	Gujarat & Maharashtra
13.	**Sunderbans Waterways (NW-97):** Namkhana to AtharaBankiKhal in West Bengal.	172	West Bengal (through Indo-Bangladesh Protocol Route)

Oceanic Routes

- India has a vast coastline of approximate 7,517 km, including islands. Twelve major and 185 minor ports provide infrastructural support to these routes.
  - Oceanic routes play an important role in the transport sector of India's economy. Approximately 95 per cent of India's foreign trade by volume and 70 per cent by value moves through ocean routes.

Air Transportation

- Air transport is the fastest means of movement from one place to the other. It has reduced distances by minimising the travel time.

- It is very essential for a vast country like India, where distances are large and the terrain and climatic conditions are diverse.
- **Air transport in India made a beginning in 1911 when airmail operation commenced over a little distance of 10 km between Allahabad and Naini**. But its real development took place in post-Independent period.
- **The Airport Authority of India is responsible for providing safe, efficient air traffic and aeronautical communication services in the Indian Air Space. The authority manages 125 airports**.
- **The air transport in India is managed by two corporations, Air India and Indian Airlines after nationalisation.** Now many private companies have also started passenger services.

Oil and Gas Pipelines

- Pipelines are the most convenient and efficient mode of transporting liquids and gases over long distances. Even solids can also be transported by pipelines after converting them into slurry.
- **Oil India Limited (OIL) under the administrative set up of the Ministry of Petroleum and Natural Gas is engaged in the exploration, production and transportation of crude oil and natural gas**. It was incorporated in 1959 as a company. Asia's first cross country pipeline covering a distance of 1,157 km was constructed by OIL from Naharkatiya oilfield in Assam to Barauni refinery in Bihar. It was further extended up to Kanpur in 1966.
- Another extensive network of pipelines has been constructed in the western region of India of which Ankleshwar-Koyali, Mumbai High Koyali and Hazira-Vijaipur-Jagdishpur (HVJ) are most important.
- A 1256 km long pipeline connecting Salaya (Gujarat) with Mathura (U.P.) has been constructed. It supplies crude oil from Gujarat to Punjab (Jalandhar) via Mathura. OIL is in the process of constructing of 660 km long pipeline from Numaligarh to Siliguri.

Communication Networks

Personal Communication System

- It enables the user to establish direct contact through e-mail to get access to the world of knowledge and information. It is increasingly used for e-commerce and carrying out money transactions.
- The internet is like a huge central warehouse of data, with detailed information on various items.
- The network through internet and e-mail provides an efficient access to information at a comparatively low cost.

Mass Communication System

Radio

- **Radio broadcasting started in India in 1923 by the Radio Club of Bombay**.
- Government took this opportunity and brought this popular mode of communication under its control in **1930 under the Indian Broadcasting System. It was changed to All India Radio in 1936 and to Akashwani in 1957**.
- All India Radio broadcasts a variety of programmes related to information, education and entertainment. Special news bulletins are also broadcast at specific occasions like session of parliament and state legislatures.

Television (T.V.)

- Television broadcasting has emerged as the most effective audio-visual medium for disseminating information and educating masses. Initially, **the T.V. services were limited only to the National Capital where it began in 1959**.
- After 1972, several other centres became operational. **In 1976, TV was delinked from All India Radio (AIR) and got a separate identity as Doordarshan (DD)**. After INSAT-IA (National Television-DD1)

became operational, Common National Programmes (CNP) were started for the entire network and its services were extended to the backward and remote rural areas.

Satellite Communication

- Satellites are mode of communication in themselves as well as they regulate the use of other means of communication. However, use of satellite in getting a continuous and synoptic view of larger area has made satellite communication very vital for the country due to the economic and strategic reasons.
- **Satellite images can be used for the weather forecast, monitoring of natural calamities, surveillance of border areas**, etc.
- On the basis of configuration and purposes, satellite system in India can be grouped into two:
  - Indian National Satellite System (INSAT) and Indian Remote Sensing Satellite System (IRS). **The INSAT, which was established in 1983, is a multipurpose satellite system for telecommunication, meteorological observation and for various other data and programmes**.
  - **The IRS satellite system became operational with the launching of IRS-IA in March 1988 from Vaikanour in Russia**. India has also developed her own Launching Vehicle PSLV (Polar Satellite Launch Vehicle). These satellites collect data in several spectral bands and transmit them to the ground stations for various uses.
- **The National Remote Sensing Centre (NRSC) at Hyderabad provides facilities for acquisition of data and its processing**. These are very useful in the management of natural resources

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DAY - 60

FIVE YEAR PLANS

Five Year Plans

- The **goals of the five-year plans are growth, modernization, self-reliance, and equity**.
  - **Growth:** It refers to an **increase in the country's capacity to produce the output of goods and services within the country**. **A good indicator of economic growth, in the language of economics, is a steady increase in the Gross Domestic Product (GDP)**.
  - **Modernization:** To increase the production of goods and services the producers have to adopt new technology.
  - **Self-reliance:** A nation can promote economic growth and modernization by using its resources or by using resources imported from other nations. The first seven five year plans gave importance to self-reliance which means avoiding imports of those goods which could be produced in India itself.
  - **Equity:** It is important to **ensure that the benefits of economic prosperity reach the poor sections as well instead of being enjoyed only by the rich**.

First Five Year Plan (1951–1956)

- The **First Five-year Plan was launched in 1951** which mainly focused on the **development of the primary sector**. The **First Five-Year Plan was based on the Harrod–Domar model** with few modifications.
- **The target growth rate was 2.1% annual gross domestic product (GDP) growth; the achieved growth rate was 3.6%** the net domestic product went up by 15%.
- **At the end of the plan period in 1956, five Indian Institutes of Technology (IITs) were started as major technical institutions.** The University Grants Commission (UGC) was set up to take care of funding and take measures to strengthen higher education in the country.

Second Five Year Plan (1956–1961)

- The Second Plan focused on the development of the public sector and "rapid Industrialisation". The **plan followed the Mahalanobis model, an economic development model developed by the Indian statistician Prasanta Chandra Mahalanobis in 1953**.
- The plan attempted to determine the optimal allocation of investment between productive sectors to maximize long-run economic growth.
- It used the prevalent state-of-the-art techniques of operations research and optimization as well as the novel applications of statistical models developed at the Indian Statistical Institute. The plan assumed a closed economy in which the main trading activity would be centered on importing capital goods.
- **Hydroelectric power projects and five steel plants at Bhilai, Durgapur, and Rourkela were established with the help of Russia, Britain (the U.K) and West Germany respectively. Coal production was increased**. More railway lines were added in the northeast.

- The **Tata Institute of Fundamental Research and Atomic Energy Commission of India was established as research institutes**. In 1957, a talent search and scholarship program was begun to find talented young students to train for work in nuclear power.
- The second plan was a period of rising prices. The country also faced a foreign exchange crisis. The rapid growth in population slowed down the growth in the per capita income.
- The target growth rate was 4.5% and the actual growth rate was 4.27%.

Third Five-Year Plan (1961–1966)

- The **Third Five-year Plan stressed agriculture and improvement in the production of wheat, but the brief Sino-Indian War of 1962 exposed weaknesses in the economy and shifted the focus towards the defense industry and the Indian Army. In 1965–1966, India fought a war with Pakistan. There was also a severe drought in 1965**. The war led to inflation and the priority was shifted to price stabilization. The construction of dams continued. Many cement and fertilizer plants were also built. Punjab began producing an abundance of wheat.
- Many primary schools were started in rural areas. To bring democracy to the grass-root level, Panchayat elections were started and the states were given more development responsibilities.
- State electricity boards and state secondary education boards were formed. States were made responsible for secondary and higher education. State road transportation corporations were formed and local road building became a state responsibility.
- **The target growth rate was 5.6%, but the actual growth rate was 2.4%.**

Plan Holidays (1966–1969)

- **Due to the miserable failure of the Third Plan, the government was forced to declare "plan holidays" (from 1966–67, 1967–68, and 1968–69)**. Three annual plans were drawn during this intervening period. During 1966–67 there was again the problem of drought.
- Equal priority was given to agriculture, its allied activities, and the industrial sector.
- **The government of India declared "Devaluation of Rupee" to increase the exports of the country.** The main reasons for plan holidays were the war, lack of resources and an increase in inflation.

Fourth Plan (1969–1974)

- **The Indira Gandhi government nationalized 14 major Indian banks and the Green Revolution in India advanced agriculture**.
- **Besides, the situation in East Pakistan (now Bangladesh) was becoming dire as the Indo-Pakistan War of 1971** and Bangladesh Liberation War took funds earmarked for industrial development.
- **India also performed the Smiling Buddha underground nuclear test (Pokhran-1) in Rajasthan on May 18, 1974**, partially in response to the United States deployment of the Seventh Fleet in the Bay of Bengal. The fleet had been deployed to warn India against attacking West Pakistan and extending the war.
- **The target growth rate was 5.6%, but the actual growth rate was 3.3%**.

Fifth Plan (1974–1979)

- The **Fifth Five-Year Plan laid stress on employment, poverty alleviation (Garibi Hatao), and justice**. The plan also focused on self-reliance in agricultural production and defense. In 1978 the newly elected Morarji Desai government rejected the plan. **The Electricity Supply Act was amended in 1975, which enabled the central government to enter into power generation and transmission**.
- The Indian national highway system was introduced and many roads were widened to accommodate the increasing traffic. Tourism also expanded. **The twenty-point program was launched in 1975. It was followed from 1974 to 1979**.

- The **Minimum Needs Programme (MNP) was introduced in the first year of the Fifth Five-Year Plan (1974–78)**. The objective of the program is to provide certain basic minimum needs and thereby improve the living standards of the people. It is prepared and launched by D.P.Dhar.
- The target growth rate was 4.4% and the actual growth rate was 4.8%.

Rolling Plan (1978–1980)

- The Rolling Plan consisted of three kinds of plans that were proposed.
  - The First Plan was for the present year which comprised the annual budget and the Second was a plan for a fixed number of years, which may be 3, 4 or 5 years.
  - The Second Plan kept changing as per the requirements of the Indian economy.
  - The Third Plan was a perspective plan for long terms i.e. for 10, 15 or 20 years. Hence there was no fixation of dates for the commencement and termination of the plan in the rolling plans.
- The **main advantage of the rolling plans was that they were flexible and were able to overcome the rigidity of fixed Five-Year Plans by mending targets, the object of the exercise, projections, and allocations as per the changing conditions in the country's economy**.
- The main disadvantage of this plan was that if the targets were revised each year, it became difficult to achieve the targets laid down in the five years and it turned out to be a complex plan. Also, the frequent revisions resulted in a lack of stability in the economy.

Sixth Plan (1980–1985)

- The **Sixth Five-Year Plan marked the beginning of economic liberalization**. Price controls were eliminated and ration shops were closed. This led to an increase in food prices and an increase in the cost of living. This was the end of **Nehruvian socialism**.
- The **National Bank for Agriculture and Rural Development was established for the development of rural areas on 12 July 1982 by recommendation of the Shivaraman Committee**.
- **Family planning was also expanded to prevent overpopulation**. In contrast to China's strict and binding one-child policy, Indian policy did not rely on the threat of force. More prosperous areas of India adopted family planning more rapidly than less prosperous areas, which continued to have a high birth rate.
- **Military Five-Year Plans became coterminous with Planning Commission's plans from this plan onwards**.
- The Sixth Five-Year Plan was a great success to the Indian economy. The target growth rate was 5.2% and the actual growth rate was 5.7%.

Seventh Plan (1985–1990)

- The plan laid stress on improving the productivity level of industries by upgrading of technology.
- **The main objectives of the Seventh Five-Year Plan were to establish growth in areas of increasing economic productivity, production of food grains, and generating employment through "Social Justice"**.
- **The Seventh Plan had strived towards socialism and energy production at large**. The thrust areas of the Seventh Five-Year Plan were: social justice, removal of oppression of the weak, using modern technology, agricultural development, anti-poverty programs, a full supply of food, clothing, and shelter, increasing the productivity of small- and large-scale farmers, and making India an independent economy.
- The target growth rate was 5.0% and the actual growth rate was 6.01% and the growth rate of per capita income was 3.7%.

Annual Plans (1990–1992)

- The Eighth Plan could not take off in 1990 due to the fast-changing economic situation at the center and the years 1990–91 and 1991–92 were treated as Annual Plans.

Eighth Plan (1992–1997)

- In 1991, India faced a crisis in foreign exchange (forex) reserves, left with reserves of only about US$1 billion. Thus, under pressure, the country took the risk of reforming the socialist economy.
- At that time Dr. Manmohan Singh (later prime minister of India) launched India's free-market reforms that brought the nearly bankrupt nation back from the edge. It was the beginning of liberalization, privatization and globalization (LPG) in India.
- **Modernization of industries was a major highlight of the Eighth Plan.** Under this plan, the gradual opening of the Indian economy was undertaken to correct the burgeoning deficit and foreign debt. Meanwhile, **India became a member of the World Trade Organization on 1 January 1995. The major objectives included controlling population growth, poverty reduction, employment generation, strengthening the infrastructure, institutional building, tourism management, human resource development, involvement of Panchayati raj, Nagar Palikas, NGOs, decentralization and people's participation**.
- The energy was given priority with 26.6% of the outlay.
- The target growth rate was 5.6% and the actual growth rate was 6.8%.

Ninth Plan (1997–2002)

Objectives

- The main objective of the Ninth Five-Year Plan was to correct historical inequalities and increase the economic growth in the country with **"Growth With Social Justice & Equality"**. Other aspects which constituted the Ninth Five-Year Plan were:
  - Population control.
  - Generating employment by giving priority to agriculture and rural development.
  - Reduction of poverty.
  - Ensuring proper availability of food and water for the poor.
  - Availability of primary health care facilities and other necessities.
  - Primary education to all children in the country.
  - Empowering the socially disadvantaged classes like Scheduled castes, Scheduled tribes, and other backward classes.
  - Developing self-reliance in terms of agriculture.
  - Acceleration in the growth rate of the economy with the help of stable prices.

Tenth Plan (2002–2007)

- The main objectives of the Tenth Five-Year Plan:
  - Attain 8% GDP growth per year.
  - Reduction of poverty rate by 5% by 2007.
  - Providing gainful and high-quality employment at least to the addition to the labor force.
  - Reduction in gender gaps in literacy and wage rates by at least 50% by 2007.
  - The 20-point program was introduced.
  - Target growth: 8.1% – growth achieved: 7.7%.
  - The Tenth Plan was expected to follow a regional approach rather than a sectoral approach to bring down regional inequalities.

Eleventh Plan (2007–2012)

- Eleventh Plan was aimed **"Towards Faster & More Inclusive Growth"**
- It aimed to increase the enrolment in higher education of 18–23 years of age group by 2011–12.

- It focused on distance education, the convergence of formal, non-formal, distant and IT education institutions.
- Rapid and inclusive growth (poverty reduction).
- Emphasis on the social sector and delivery of service therein.
- Empowerment through education and skill development.
- Reduction of gender inequality.
- Environmental sustainability.
- To increase the growth rate in agriculture, industry, and services to 4%, 10%, and 9% respectively.
- Reduce the total fertility rate to 2.1.
- Provide clean drinking water for all by 2009.
- Increase agriculture growth to 4%.

Twelfth Plan (2012–2017)

- The objectives of the Twelfth Five-Year Plan were:
  - To create 50 million new work opportunities in the non-farm sector.
  - To remove gender and social gap in school enrolment.
  - To enhance access to higher education.
  - To reduce malnutrition among children aged 0–3 years.
  - To provide electricity to all villages.
  - To ensure that 50% of the rural population has access to proper drinking water.
  - To increase green cover by 1 million hectares every year.
  - To provide access to banking services to 90% of households.
- The plan **aims towards the betterment of the infrastructural projects of the nation avoiding all types of bottlenecks**.
- The document presented by the planning commission is aimed to attract private investments of up to US$1 trillion in the infrastructural growth in the 12th five-year plan, which will also ensure a reduction in the subsidy burden of the government to 1.5 percent from 2 percent of the GDP (gross domestic product). The UID (Unique Identification Number) will act as a platform for cash transfer of the subsidies in the plan.

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